

TO: Board of Directors ("Board"), Innerarity Island Association, Inc. ("HOA")

FROM: Mike Floyd

RE: Innerarity Island Sewer and Water Project: History and Current Issues

DATE: April 30, 2020

I have recently spoken with officials of Escambia County, the Emerald Coast Utility Authority ("ECUA") and the Talcon Group ("Talcon). This memorandum summarizes things I have learned from those conversations and related documents. I hope you find this information helpful.

As you know, our HOA's attorney is Suzanne Blankenship at Emmanuel, Sheppard & Condon, and she is our source for legal advice. I don't want anyone to misunderstand my own comments as legal advice or legal opinions. I am writing and speaking on these matters solely as a resident of the Island, a member of the Board, and (if relevant to any of the issues) Treasurer of our HOA.

I am very grateful to a number of people who have been impressively helpful in finding reliable, relevant information and interpreting it. Of course, though, the conclusions here are my own.

The documents referred to below are available via links at our HOA website, <https://liveinnerarityisland.org/sewer-project>, and at the Escambia County website focused on our sewer project, <https://myescambia.com/open-government/projects/project-details/innerarity-point-water-system>.

MSBU AUTHORITY AND APPROVAL PROCESS

The MSBU for this project was approved by the Escambia County Board of Commissioners ("BOCC"), as reflected in Escambia County Ordinances 2017-10 (March 2, 2017) and 2018-3 (February 1, 2018). My contact at the Escambia County Attorney's Office helpfully explained the approval process as follows:

"The [BOCC]'s authority to create MSBU special assessments is found in Section 125.01, Florida Statutes. Please note that the Board is not required to obtain the consent of the affected property owners before enacting an MSBU ordinance. However, many MSBU special assessment ordinances are "citizen initiated," and for those MSBUs the Board requires an application supported by a petition signed by a majority of the affected property owners. I have attached the Escambia County Municipal Services Benefit Units Guidelines and Procedures, which [is available at <https://myescambia.com/docs/default-source/sharepoint-administration/budget/msbu-guidelines-and-procedures.pdf?sfvrsn=2> and] explains the process for various citizen initiated MSBUs (see the note at the bottom of page 2).

"The Innerarity Island MSBU was not citizen initiated. Rather, it was the result of the County being designated by law as the receiver of the private water and waste water

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system after the Innerarity Island Development Corporation declared its intent to abandon it. The system required significant improvements, and the MSBU was created by the [BOCC] to fund them."

HORNE REPORTS, INTERLOCAL AGREEMENTS, CONSTRUCTION PLANS, AND TOTAL CONSTRUCTION COSTS

The January 2014 Horne Report prepared for Innerarity Island Development Corporation by Kenneth Horne & Associates, Inc., Civil Engineers (Executive Summary at page 2) indicated that it contemplated the following:

"Sanitary sewer system improvements would consist primarily of: a) relocation of sewer and force mains as necessary to eliminate encroachments onto private property, and b) correction of slope deficiencies in the sanitary sewer system by either reconstruction of substantial portions of the gravity collections system or replacement with a low pressure system. The reconstruction alternative would involve either replacement or major rehabilitation of all lift stations on the island while the low pressure option would replace all gravity collection on the island leaving only the relatively new gravity collection in the Russell Bayou development in service. The estimated cost for sewer related improvements is either \$4.5 million for replacement of conventional gravity sewer or \$2.3 million for installation of a low pressure system on the island."

The revised October 2015 Horne Report prepared for Escambia County (Executive Summary at page 2) indicated that it contemplated:

"Sanitary sewer system improvements would consist primarily of the construction of a low pressure sewer system to replace all gravity collection on the island leaving only the relatively new gravity collection in the Russell Bayou development in service. The existing gravity sewer collection system was found to be prone to excessively heavy infiltration/inflow and to have many line segments laid at insufficient slope. Full replacement of the gravity sewer system was eliminated from consideration due to excessive cost. The estimated cost for sewer related improvements is \$2.73 million for installation of a low pressure system on the island and upgrade of the existing Russell Bayou lift station."

The increase in projected costs from \$2.3 to \$2.73 million primarily resulted from three factors: (1) upgrades required for the electrical system at the Russell Bayou lift station; (2) use of ECUA unit prices, rather than the lower unit prices typically used for real estate developer projections; and (3) installing low-pressure pipes (though not grinder pumps or connections to replace septic tanks) on North Shore Drive.

Details of funding and construction for the sewer project appear in an Interlocal Agreement dated May 17 (and 24), 2018; an Amendment dated July 18 (and 23), 2019 to that Interlocal Agreement;

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and a Sewer – Final Construction Plan Set dated July 25, 2019. Neither the HOA nor the Board is a party to any of these documents, which were developed by ECUA and the BOCC.

The 2018 Interlocal Agreement provided in Article 4, Section 4.1 that

"[Escambia] County agrees to reimburse ECUA for the Costs of the Project as generally described in Exhibit "A", including but not necessarily limited to property and equipment costs, engineering and design services, and construction costs, in an amount not to exceed Four Million, Two Hundred Twenty Thousand Dollars. [Footnote 1 here specifies that 'This agreement to reimburse includes Costs of the Project incurred prior to entry into this Agreement as well as after.'] In the event that ECUA determines that the estimated Costs of the Project will exceed \$4,220,000 upon the opening of publicly advertised bids for construction of the Project, then either Party may elect to terminate this Agreement and not proceed with construction of the Project. In the event the Project proceeds post bidding and during the course of construction it is learned that the Costs of the Project will exceed \$4,220,000, then the Parties shall meet and decide how to proceed, if at all."

Talcon submitted the low bid of \$4,542,070 on June 6, 2019. This indicated that the original \$4.22 million do-not-exceed cost was inadequate. The BOCC and ECUA raised the do-not-exceed cost of the project to \$5.7 million in the 2019 Amendment to the Interlocal Agreement.

The increase from the \$2.73 million estimate to \$4.22 million and \$4.5 million was largely caused by three factors: (1) discovery that the Russell Bayou lift station would have to be entirely replaced, because the existing lift station lacked sufficient emergency storage capacity (approximately \$750,000); (2) construction price inflation¹ between 2015 and 2018, at approximately twice the rate of increase in the Consumer Price Index (approximately \$300,000); and (3) addition of North Shore Drive grinder pumps, sewer connections, and septic tank decommissioning (approximately \$600,000).

My understanding is that ECUA, Escambia County, and Talcon are making every effort to keep the costs of the project as close as possible to the contractor's \$4.5 million bid, and everyone wants to minimize any need to use the contingency funds. Of course, there is an inevitable tension between controlling costs and making sure residents are satisfied with the results.

WATER SYSTEM COSTS

I have been told that actual costs for the water system project were as follows:

¹ From October 2015 to July 2019, the ENR Construction Cost Index increased by 11.5%, from 10128 to 11293. During that same period, the Consumer Price Index (all urban consumers) increased by only 5.6%, from 230.860 to 243.776.

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Water system construction	\$629K
Paid to Gulf Breeze for water charges, system maintenance, etc.	166K
Inspections	25.5K
Design and permitting	85.8K
Total (approximate) water system improvement costs	<u>\$906.3K</u>

As discussed more fully below under "Application of Grant Money..." grant money covered all of the water system costs, and some of the remaining grant money was used during the water system construction to purchase grinder pumps for the sewer project.

GRINDER PUMP STATION LOCATIONS

I have heard concern that unexpected additional costs may be incurred, cutting into the contingency funding, as the result of neighbors' (including myself) insisting that the grinder pump not be installed right next to our front doors. Apparently ECUA had been unaware that so many of our sewer lines come out of our houses at the front, near the center, and therefore near the front door for many of us. Our friends at ECUA, Escambia County, and Talcon implore us to help them avoid unreasonable additional costs for the location of our grinder pumps, which may increase the amount of the MSBU that everyone has to pay. They also acknowledge the assurance we were given that "The Contractor shall be responsible for contacting the property owner to acquire the right to install the system on the property, *reach a mutual agreement on the location of the station with the property owner*, provide labor and materials for the plumbing connections to the property and to the new low pressure sewer system." This language appears in Item "2." under "Grinder Pump Station Installation" on the second page of the Sewer – Final Construction Plan Set dated July 25, 2019, and was also discussed at one or more public meetings. My understanding is that discussions have been under way among ECUA, Escambia County, and Talcon to explore additional options for grinder pump location.

My wife and I had a very pleasant conversation last week with a Talcon representative about the location of our grinder pump. I had another very pleasant conversation this week with that same representative and one other person working on the project. Both were unfailingly and impressively professional, personable, and knowledgeable.

My current understanding is that Talcon is collecting information as to homeowner preferences for locating the grinder pump and identifying those that differ from Talcon's preference. Talcon, ECUA, and the County will then identify which of those differ sufficiently from a reasonable "mutual agreement" to warrant a change order, and then identify the total costs of potential change orders to determine whether that results in an unreasonable application of the contingency funding. Based upon those determinations, there are expected to be further discussions with each resident as whether it is feasible for Talcon to install the grinder pump in the desired location, consistent with a "mutual agreement." If we cannot reach a satisfactory mutual agreement with Talcon, or if the change order

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amount is prohibitive, we have the alternative to arrange for our own independent contractors to purchase, install, and connect a grinder pump for us, which some of our neighbors are already planning to do.

APPLICATION OF GRANT MONEY AND PROPERTY SALES TO MSBU

The \$1.5 million in grant money received was more than adequate to cover the costs of the water system, and I have been assured that the overwhelming majority of that \$1.5 million has been applied to the costs of our water and sewer project, approximately as follows:

Water system construction	\$629K
Paid to Gulf Breeze for water charges, system maintenance, etc.	166K
Inspections	25.5K
Design and permitting	85.8K
Purchase 63 grinder pumps in [2017?]	157K
Purchase 62 grinder pumps in [2019?] (at [2017?] price)	155K
Sewer design and "CEI" (Construction, Engineering, & Inspection)	221K

Total (approximate) grant monies applied to water and sewer costs \$1,439.3K

This leaves approximately \$60.7K of funds from the grants, which I have been assured will be applied in full to reduce the MSBU amounts we have to pay.

I have also been assured that the proceeds from any and all sales of County-owned property on the Island have been or will be similarly applied to reduce the amount of the MSBU amounts we have to pay.

It is still my understanding and hope that Commissioner Underhill and his colleagues support our plan to keep the Seascape property owned by the County as a conservation area. However, I have not been personally involved in those discussions, and I hope we can soon move forward to make sure that those plans do not get lost in the static generated by the sewer project.

ALLOCATION OF MSBU COSTS TO HOMEOWNERS

The draft minutes (not yet approved by the Board) for the December 9, 2019 HOA meeting indicate that the estimated annual MSBU payment amounts presented at that meeting were as follows:

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	<u>10-year MSBU</u>	<u>15-year MSBU</u>
Developed lot	\$1,491.07	\$1,087.74
Undeveloped lot	\$786.35	\$573.65
Lot with septic tank	\$1,667.95	\$1,216.77
Russell Bayou	\$977.43	\$713.04

That HOA meeting took place several months after the July 2019 Amendment to the Interlocal Agreement raised the do-not-exceed amount to \$5.7 million. However, the cost allocations above were reportedly based on a 10% contingency resulting in a total estimated maximum construction price of approximately \$4.99 million. These numbers are currently thought to be more realistic than the approximately 25.6% contingency and \$5.7 maximum construction price reflected in the Amendment to the Interlocal Agreement.

As you might expect, I have focused on the “Developed lot” numbers that I expect to pay, as I have tried to gain an intuitive understanding of these numbers. I have gained a lot of comfort in the last few days from the few calculations I’ve been able to make confidently: at 4% interest per year, the present value of both the \$1,491.07 estimated annual payments for ten years and \$1,087.74 estimated annual payments for fifteen years is \$12,093.91. I’m guessing – but not yet completely certain – that this would be the estimated amount of the single up-front payment for a Developed lot.

Regardless of which contingency amount was used, I take cautious but significant comfort that this \$12K amount – even if based upon only a 10% contingency – still looks much better than the \$15,000 estimate of the up-front payment that had stuck in my mind as a rule of thumb, and vastly better than the \$20,000-per-residence guess of the up-front cost that some of our neighbors are heard to be alarmed about.

Page 2 of the Sewer – Final Construction Plan Set dated July 25, 2019 details a number of other project requirements that we understand to be incorporated into the contract with the Talcon Group. The PDF of that document is hard to read as it initially appears on the computer screen; however, using the zoom function after your web browser loads the PDF can help make the small type much easier to read.

We are still working to clarify a number of factual matters addressed in our March 26, 2020 letter to Commissioner Underhill. However, we have made significant progress in understanding a number of important facts in this complex history.