

AGENDA

**FORT SMITH BOARD OF DIRECTORS
SPECIAL STUDY SESSION**

JANUARY 3, 2012 – 12:00 NOON

**ELM GROVE COMMUNITY CENTER
1901 NORTH GREENWOOD AVE**

1. Discussion regarding Van Buren Water True-Up ~ *Requested at the December 20, 2011 regular meeting* ~
2. Discussion regarding upcoming sales tax election



MEMORANDUM

December 30, 2011

TO: Mayor and Board of Directors

FROM: Ray Gosack, City Administrator

SUBJECT: Van Buren Water True Up

At the December 20th board meeting, the board requested a second legal opinion regarding the 2009 Van Buren water true up. Mark Moll of the Jones Jackson & Moll law firm has provided that opinion, which is attached. Mr. Moll will attend the study session to answer any questions and discuss his opinion.

Van Buren is reviewing our true up calculations for 2010. Once the calculation is confirmed, we'll issue an overpayment check to Van Buren for the full amount as the board directed at the December 6th meeting. Our calculations show this amount to be \$30,884.

During the period of 2006-2010, Van Buren has paid nearly \$17.7 million in water service payments to Fort Smith. These payments were based on rates adopted by Fort Smith in conformity with our water supply agreement with Van Buren. Fort Smith's retail customers paid slightly more than \$87 million in water service charges during the same period.

Options for resolving the 2006-2009 true ups which the board may wish to consider include:

- Invoking the arbitration provision in our settlement agreement with Van Buren to pursue a true up payment for 2009.

This option would allow us to make a claim for 2009 (\$253,706), but could jeopardize the amounts tentatively agreed to for 2006, 2007, and 2008 (\$581,174). It would also leave the matter unresolved for several months and create significant expense to go through arbitration.

- Entering into a settlement agreement with Van Buren as described in the attached e-mail.

This option would conclude the true ups for 2006-2010, but would result in no payment for 2009.

The 2004, 2005, 2006, 2007, 2008 and 2010 true ups were all processed timely. The following measures have been implemented to assure that we don't have another omission as we did with the 2009 true up.

- The utility rate analyst position has been transferred to the utilities dept. The director of utilities will monitor his work to ensure the required information is provided to Van Buren timely.
- The deputy city administrator will verify that the information is provided to Van Buren within 60 days of completing the CAFR.
- The board will be advised when the required information is provided to Van Buren.
- The utility rate analyst position will not be left unduly vacant for extended periods of time.

The failure of Fort Smith to provide Van Buren with the required information for the 2009 true up is a regrettable and costly inaction. Steps have been taken to ensure the error doesn't happen again. Fort Smith must now decide how it wants to resolve the error for the 2009 true up.

Ray

Attachments

JONES, JACKSON & MOLL, PLC

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December 30, 2011

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Ray Gosack
City Administrator
City of Fort Smith
P. O. Box 1908
Fort Smith, AR 72902

Re: Dispute With Van Buren on 2009 Water Bill

Dear Mr. Gosack:

This letter will confirm your request for my opinion on whether the City of Fort Smith is entitled to exercise the true-up provision in the Van Buren water supply agreement for the year 2009. My opinion is based on the applicable contracts between the cities of Fort Smith and Van Buren, copies of which you provided to me, and certain facts which are apparently not in dispute.

The Agreements

On February 25, 1983, Fort Smith and Van Buren entered into an Agreement pursuant to which Van Buren conveyed land that it owned in Crawford County to Fort Smith and in exchange Fort Smith constructed a dam impoundment and water reservoir in order to mutually benefit the citizens of Fort Smith, Van Buren and surrounding areas. Van Buren began purchasing water from Fort Smith based on a formula that was relatively easy to use compared to the formula used today.

On December 19, 2001, Fort Smith and Van Buren entered into a Final Settlement and Release Agreement which resolved a lawsuit that Van Buren had filed against Fort Smith alleging that Fort Smith had breached the 1983 Agreement. As part of the Final Settlement and Release Agreement, the parties signed an Addendum pursuant to which Van Buren paid the protested amounts and the parties agreed to submit any future disputes concerning the sale and purchase of water to arbitration.

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On October 18, 2002, Fort Smith and Van Buren entered into a Supplement to Final Settlement Agreement and Release which set forth a Rate Model to be used in determining water rates and charges that Van Buren would pay for water purchased from Fort Smith beginning in 2004 and continuing through 2021. The Rate Model was complicated and it required inputs and formulae for indirect and direct costs of operation and maintenance, capital costs for transmission system facilities, methodologies of the American Water Works Association, and costs associated with pumping and storage facilities.

The parties also agreed in the Supplement that “[d]uring the period of the years 2004 through 2021, the Rate Model or its inputs may be changed so as to produce an adjusted rate that Van Buren shall pay for water purchased from Fort Smith in only the following two manners,” one of which changes the Rate Model (not involved for purposes of our discussion) and the other involves using the existing Rate Model, but changing the data inputs and allocation formulae so as to either allow Fort Smith to retroactively adjustment of Van Buren’s water bill for the prior year or prospectively change it for the coming year. For purposes of this discussion, I am referring to paragraph 4 (A)(1) of the Supplement which authorizes Fort Smith to make a retroactive adjustment for the prior year’s charges.

The Supplement provides that the inputs may be adjusted by Fort Smith; there is nothing in the contract that reveals an intent of the parties to adjust either the Rate Model or the data inputs and allocation formulae on an annual basis. Fort Smith can exercise its right to adjust the inputs and thereby retroactively adjust Van Buren’s water bill for the prior year by complying with a two-step procedure: (1) provide Van Buren with a comparison of actual and projected revenues and costs and other specified inputs within sixty (60) days of the completion of Fort Smith’s Comprehensive Annual Financial Report (“CAFR Comparisons”), and (2) send Van Buren a subsequent “true-up” of the Rate Model which would reflect either additional charges or a credit for the year in question. There is no time restriction on providing the true-up. In the event of a dispute, either party has the right to submit the dispute to binding arbitration.

The Facts

There have been some years (2004 and 2005) in which there was no retroactive adjustment of Van Buren’s water bill. However, during the years 2006, 2007 and 2008, Fort Smith exercised its right to retroactively adjust the inputs – and thereby adjust the amounts due in those years – by providing Van Buren the CAFR Comparisons and subsequently providing a true-up invoice for each of those years. Van Buren disputed the amounts of each of the three-year adjustments. Van Buren submitted some payments under protest and escrowed other funds to account for its potential liability.

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Neither party has requested arbitration, presumably because the parties are continuing to negotiate.

An audited CAFR for Fort Smith for the year 2009 was completed in late June 2010. Unlike the previous three years, Fort Smith did not send the CAFR Comparisons of projected and actual revenues and expenses to Van Buren which would have initiated Fort Smith's right to adjust the amount of Van Buren's water bill for the year 2009. It is not clear whether Fort Smith intentionally or unintentionally failed to send the CAFR Comparisons. Pursuant to the instruction of the Fort Smith Board of Directors, an invoice representing the 2009 true-up amount of \$253,706.00 was sent to the Van Buren Municipal Utilities Commission in November 2011.

The Law

In my opinion, the contract provision in question is not ambiguous or subject to more than one reasonable interpretation. Paragraph 4(A)(1) of the Supplement clearly indicates that Fort Smith has the right but not an obligation to compare its actual and projected costs for a year and, if appropriate, retroactively charge Van Buren an additional amount for water consumed. However, without any action on the part of Fort Smith, there is no annual adjustment and Van Buren would have no contractual duty to pay any more for the water consumed or be entitled to any credit on its account. In other words, the latest Rate Model and inputs and formulae are used to calculate the cost of water to Van Buren unless and until either the Rate Model or the inputs and formulae are changed and Fort Smith has control over whether there will be any changes.

Any changes in the inputs and formulae – and thereby any retroactively adjustment of Van Buren's water bill – may be instigated by Fort Smith through compliance with the above-referenced two-step procedure. The CAFR Comparisons / true-up procedure is a "condition precedent" to Van Buren's obligation to pay or entitlement to any credit. A condition precedent is a fact or event which the parties intend must exist or take place before a corresponding duty arises. The wording of the contract that is central to this dispute reflects an intention of the parties to make Van Buren's obligation to pay additional charges for water consumed in a prior year conditional on Fort Smith timely providing the CAFR Comparisons and a true-up invoice for the additional charge. Therefore, noncompliance by Fort Smith results in a forfeiture of Fort Smith's right to make an adjustment in the amount that Van Buren owes for water consumed during the prior year.

In the alternative, even if, despite the language of the contract, the parties intended there to be an annual adjustment, it is my opinion that Fort Smith would be

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estopped or prevented from seeking to impose an adjustment for the year 2009 by failing to timely comply with the two-step procedure which required Fort Smith to provide Van Buren with the CAFR Comparisons and a true-up calculation.

Under contract law, there is a doctrine of substantial performance whereby a party may recover on a contract even if the party did not do everything that the contract required of the party if the party's performance was substantial. In this case, however, I do not believe it could be said that Fort Smith substantially performed the condition precedent because Fort Smith never provided the CAFR Comparisons and the true-up amount was not given to Van Buren until November of this year. There is language in the contract which states that the appropriate adjustment for a reported year shall be applied either as an additional charge or a credit against charges in the *immediately following annual period* with one-twelfth of the adjustment applied to each calendar month's bill. Thus, even if Fort Smith was given some leeway on the obligation of providing the CAFR Comparisons within 60 days from the date the CAFR was completed, Van Buren simply did not receive either the CAFR Comparisons or the true-up calculation in time in 2010 to adjust the rate that it charges its citizens for water in the following year. For these reasons, I believe that a court would conclude that Fort Smith did not substantially comply with the two-step procedure for adjusting Van Buren's water bill for the year 2009.

My opinion is the same whether Fort Smith intentionally or negligently failed to send the CAFR Comparisons and timely send the true-up amount. Under either scenario, Van Buren has no contractual obligation to pay an adjusted amount for water consumed in 2009.

Prior Years' True-Ups Owed by Van Buren

You also asked me for an opinion concerning whether Fort Smith had any risk of forfeiting the 2006, 2007 and 2008 true-up adjustments owed by Van Buren if Fort Smith pursued collection of the 2009 true-up amount of \$253,706.00. It is my understanding that Van Buren owes \$327,226.00 for 2006, \$129,227.00 for 2007, and \$124,721.00 for 2008.

In my opinion Fort Smith has no risk of adversely affecting Van Buren's legal obligation to pay the adjusted water bills for 2006, 2007 and 2008 by pursuing collection of an alleged amount due for 2009. My understanding is that Van Buren has offered to pay the amounts due for 2006 - 2008 provided Fort Smith relinquishes its claim for 2009.

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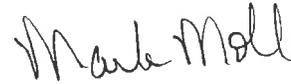
While Van Buren could, of course, withdraw from negotiations if Fort Smith pursued collecting an adjusted amount for 2009, Fort Smith could exercise its right to submit the 2006 through 2008 and even the 2009 claim, to binding arbitration. Fort Smith's position with respect to 2009 would have no bearing on the amounts owed by Van Buren for 2006 - 2008.

Thank you for the opportunity to render this opinion to the City for Fort Smith. I will be pleased to answer any questions that you may have concerning these matters.

Yours very truly,

JONES, JACKSON & MOLL, PLC

By:



Mark Moll

MAM:jlj

Gosack, Ray

From: Gosack, Ray
Sent: Wednesday, December 14, 2011 4:53 PM
To: Andre' Good; Andre' Good (good4ward2@gmail.com); Dingman, Jeff; Don Hutchings; George Catsavis (georgecatsavis@gmail.com); Philip Merry (philip_merry@ajg.com); pweber5469@aol.com; Sandy Sanders (SSanders@FortSmithAR.gov); Settle, Kevin (Board of Directors); Steve Tyler (sksttyler@sbcglobal.net)
Cc: Parke, Steve; Bushkuhl, Kara; Kimbrough, Mitzi; 'Jerry Canfield'
Subject: Van Buren Water True Up

I met today with C.E. Dougan, chairman of the Van Buren utilities commission, and Gary Smith, manager of Van Buren utilities to discuss the water true up payments. We spent most of our time discussing the 2009 water true up, and payment terms for the amounts Van Buren owes to Fort Smith.

Regarding the 2009 true up amount, Van Buren isn't willing to pay any additional amount for the following reasons:

- Van Buren believes it's on solid ground legally to not owe any payments for 2009
- Van Buren can't provide a rationale explanation to its citizens why it would make a payment for 2009 when Fort Smith didn't follow the contract requirements for that year
- Van Buren disagrees with the calculations for 2006-08 but tentatively accepted the amounts calculated by Fort Smith in the context of settling and getting behind them the true up disagreements for 2006-2009. If Fort Smith pursues arbitration/litigation to receive a payment for 2009, then Van Buren won't accept the amounts calculated by Fort Smith for 2006-08 and will challenge the true up amounts for all years.
- Van Buren has nothing to gain by making a payment for 2009

I asked if there was any circumstance under which Van Buren would consider paying a true up amount for 2009. Mr. Dougan replied that there wasn't.

We discussed terms for the payment of amounts owed by Van Buren. The amount is \$581,174. Van Buren had originally proposed paying \$161,000 (the checks previously issued by Van Buren to Fort Smith) of this amount up front and paying the balance in equal monthly installments over 3 years. I asked if Van Buren could pay up front not only the \$161,000 but also the \$236,000 which they're holding in a cash reserve, and then pay the balance (\$184,174) in equal installments over 12 months with interest. After considerable discussion, Van Buren said that they could live with this arrangement but didn't believe that they should have to pay interest on the amount which would be paid out over 12 months (\$184,174). They cited the provision in the agreement which allows them to make true up payments in equal monthly installments over a 12-month period after the true up payment amount is determined. I concur with this analysis.

In summary, Van Buren isn't willing to pay any additional amount for 2009, but is willing to pay up front \$397,000 and the balance of \$184,174 in equal monthly installments without interest during 2012.

If this true up settlement arrangement is acceptable, we'll prepare an agreement which would likely be ready for the January 3rd board meeting. If you'd like to have a study session discussion prior to considering a settlement agreement, please let me know.

Ray

R-262-02

City of Fort Smith
Copy

SUPPLEMENT TO FINAL SETTLEMENT AND RELEASE AGREEMENT

This SUPPLEMENT TO FINAL SETTLEMENT AND RELEASE AGREEMENT (“Supplement”) is made and entered into by and between the City of Van Buren, Arkansas, and the Van Buren Water and Sewer Commission (collectively referred to as “Van Buren”), and the City of Fort Smith, Arkansas (“Fort Smith”) on this 18th day of October, 2002. Van Buren and Fort Smith will be referred to collectively in this Supplement as “the parties.”

WHEREAS, Van Buren and Fort Smith entered into a Final Settlement and Release Agreement on December 19, 2001, to settle a lawsuit between them alleging that Fort Smith breached the parties’ 1983 Agreement regarding the impoundment of water on Lee Creek in Crawford County and the furnishing of water from the Fort Smith impoundments to Van Buren (“the 1983 Agreement”);

WHEREAS, the parties agreed in their settlement to submit to binding arbitration the determination of a method for computing the rate under Paragraph 3, Subparagraph Second, of the 1983 Agreement that Van Buren shall pay for water purchased from Fort Smith for the years 2004 through 2021;

WHEREAS, the parties desire to define the elements of the Rate Model that shall be used to determine the rate under Paragraph 3, Subparagraph Second, of the 1983 Agreement that Van Buren shall pay for water purchased from Fort Smith for the years 2004 through 2021, and to define the circumstances and the manner in which that Rate Model may be adjusted during that

time period;

WHEREAS, this Supplement does hereby incorporate by reference the parties' Final Settlement and Release Agreement executed on December 19, 2001, and augment that agreement by the addition of the mutual promises and agreements contained in this Supplement;

WHEREAS, the parties acknowledge that full, valid, and binding consideration exists for the execution of this Supplement and that such consideration includes conformance to the unique contract provisions regarding water rates and other matters in the 1983 Agreement and the mutual promises contained herein;

NOW THEREFORE, in consideration of the mutual terms, conditions, and agreements contained herein, the parties acknowledge and agree as follows:

1. Regarding the issue submitted to arbitration, Van Buren and Fort Smith agree that the "Rate Model" (identified below) shall be utilized to determine water rates and charges imposed by Fort Smith on all of its classes of customers (subject to paragraph 7 below) including the water rates and charges that Van Buren shall pay for water purchased from Fort Smith beginning with the year 2004, including the adjustments directed by the Arbitrators' Award of September 20, 2002, and the parties' agreement as requested by the Arbitrators' Award regarding the following issues raised by Van Buren and presented to the Arbitrators for decision:

1. Regarding Fort Smith's "indirect costs" of operation, those costs directly linked to water service shall be included in the costs charged to Van Buren as currently reflected in the Rate Model and no portion of the following Fort Smith general, overhead "indirect costs" shall be charged to Van Buren: Budget Account 4100 (Mayor); Budget Account 4101 (Board of Directors); Budget Account 4102 (City

Administrator); Budget Account 4103 (Dev/Engineer); Budget Account 4105 (City Clerk); Budget Account 4106 (Planning and Zoning); Budget Account 4204 (City Attorney); Budget Account 4405 (Internal Audit);

2. Operation and maintenance and capital related costs for transmission system facilities located south of the Arkansas River may be included in the costs charged to Van Buren in the Rate Model provided "transmission system facilities" shall only include water lines 16" and greater in diameter now in service, new water lines 24" and greater in diameter and placed into service after the date of this Supplement and the existing 12" lines and other lines identified in yellow on the attached map marked as Exhibit 1 and incorporated herein; and,
3. No portion of pumping and storage facilities other than those located at treatment plants shall be allocated to the costs utilized to determine the rates and charges to Van Buren.

The Rate Model shall be based on the Award attached hereto, the foregoing agreements and the following AWWA methodologies incorporated into the Rate Model:

1. Cash basis of determining revenue requirements;
2. Forward looking test years;
3. Use of utility basis of cost allocation and allocation of costs except as may be modified by the Award herein. It is agreed by the parties that the term "utility basis of cost allocation" means allocation of capital costs to cost functions on the basis of net book value with any appropriate adjustments, and allocation of operation and maintenance expense to cost functions.

4. Commodity - demand basis of cost allocation.

The Rate Model is identified by the attached electronic format and schedules of inputs and outputs.

2. The Rate Model shall be audited regarding water rates and charges by Mr. Chris Woodcock and his firm, Woodcock & Associates, Inc., for accuracy, consistency and compliance with AWWA Manual M-1 (Fifth Edition), the implementation of the September 20, 2002, Award herein, and this Supplement; provided, the audit shall not include an examination of the engineering and operation assumptions and cost allocations incorporated into the Rate Model except as impacted by any Award and the agreements stated herein. Woodcock & Associates, Inc. may consult with such persons deemed appropriate in conducting the audit. Although this audit is a part of the arbitration process, it may be conducted by Mr. Woodcock and his firm as they would perform normal consulting services. Any change or adjustment proposed from the audit shall be incorporated into the Rate Model unless a party objects to such change or adjustment and that objection is sustained by the other two Arbitrators. The cost of the audit shall be borne equally by the parties.

3. The parties agree that an Unaccounted for Water Study ("Study") will be accomplished according to the protocol attached as Exhibit 2 at a cost shared equally by the parties. The preliminary result of the Study will be provided to the parties by January 1, 2004. Either party may comment on the Study in writing by February 20, 2004. The final result of the Study shall be stated in writing by March 15, 2004. The final result shall be incorporated into the Rate Model unless any written objection of a party is sustained by the Arbitrators. The unaccounted for water approved factor resulting from the Study shall continue to be used in the

Rate Model until Fort Smith has completed a subsequent unaccounted for water study according to the foregoing protocol for a subsequent twelve (12) month period. The preliminary unaccounted for water factor for the year 2004 to be used in the Rate Model shall be 9.7 % as used and applied in the Arthur Young study of 1986. The finally determined 2004 unaccounted for water factor will be used in the year 2004 "true up" as provided for in paragraph 4.A.1. below.

4. The parties agree that during the period of the years 2004 through 2021, the Rate Model or its inputs may be changed so as to produce an adjusted rate that Van Buren shall pay for water purchased from Fort Smith in only the following two manners:

A. Utilizing the Rate Model and without performing an independent cost of service analysis, the data inputs and allocation formulae (and resulting rate and charges for Van Buren) may be adjusted by Fort Smith under either of the two following circumstances:

1. Within sixty (60) days of the completion of Fort Smith's audited CAFR for the year 2004 or any subsequent year through 2021 ("the reported year"), Fort Smith will provide Van Buren with a comparison of actual and projected annual revenues, other income, O & M expenses, capital expenditures, capital additions and retirements to plant, fund transfers, and billed water volumes, and other projected factors (including Fort Smith's then current CIP) in the Rate Model. The projected values shown in this comparison shall be those recognized as data inputs to that Rate Model application used as the basis for the water rates in effect during the reported year. The actual values corresponding to each of these projected values shall be shown for purposes of comparison. At the reasonable request of Van Buren representatives, Fort Smith will provide timely responses, explanations, and supporting information regarding any reported values.

Van Buren will also have the right of access to Fort Smith's records to perform at Van Buren's expense an independent audit of any or all the information provided. Within sixty (60) days of its receipt of this comparison, Van Buren may elect to have Fort Smith prepare a "true up" of the Rate Model in which it will substitute actual values for the projected values recognized in deriving the rate in effect during the reported year. Fort Smith may accomplish the "true up" regardless of the Van Buren election. The resulting allocation of costs of service and rates and charges applicable to Van Buren will be applied to actual Van Buren billed sales volume and compared with actual billings for the period to derive the adjusted charges applicable to the reported year. The adjustment may apply only to Van Buren without applying to all classes of customers. The parties will negotiate in good faith regarding any differences concerning the "true up." Any dispute which the parties cannot resolve will be subject to arbitration according to the procedures set forth in the parties' Arbitration Agreement of December 19, 2001 ("Arbitration Agreement"). Upon completion of the resolution of the "true up" for the reported year, the appropriate adjustment (either positive or negative) for the reported year shall be applied (either as an additional charge or a credit against charges) in the immediately following annual period (1/12 of the adjustment applied to each calendar month's bill). Any costs associated with the calculation of the adjusted charges (i.e., the costs of entering the actual values presented in Fort Smith's annual comparison of actual and projected data input values into the Rate Model, using the Rate Model to calculate adjusted rates and charges for the reported year, and calculating the amount of added charges or credits due) shall be payable by the party financially benefitting from the adjustment.

2. Fort Smith, at its expense, so long as it does not change the methodologies identified in paragraph 1 above, may amend the data inputs and allocation formulae in the Rate Model to reflect then current information; provided then current information shall be in the form of Fort Smith officially approved studies or budgets. For example, and not as a limitation on the types of change which might be made, Fort Smith may adjust the Fort Smith capital improvement program (CIP) expenditures utilized in the Rate Model to reflect modifications Fort Smith has made in the CIP or to reflect more accurate information regarding cost of individual elements of the CIP. Upon determination of information which Fort Smith desires to propose as a basis for amending the information in the Rate Model so as to produce a future rate for water purchased by Van Buren, Fort Smith shall provide a complete copy of the Rate Model application as adjusted and identify in writing the adjusted information and the basis therefore and the proposed resulting rates and charges to Van Buren at least sixty (60) days prior to implementing the new rate. Van Buren may object, in part or in whole, to the inclusion of the new information and the proposed new rate within the sixty (60) day period. The parties will negotiate in good faith a resolution of the issue. If the issue is not resolved by the parties within ninety (90) days of the effective date of the new rate, either party may submit the matter for determination according to the arbitration procedures set forth in the parties' Arbitration Agreement. Any disputed portion of the proposed additional rate (but not the previous rate) will be escrowed, with interest, during the period of dispute resolution and paid to the prevailing party at the conclusion of the proceeding. No charge shall be imposed on Van Buren under any version of the Rate Model as authorized in this paragraph 4.A.2. unless rates as then determined for all classes of customers shall be adopted

simultaneously by Fort Smith.

B. At any time Fort Smith proposes to change the Rate Model by changing any of the procedures, methodologies or pricing structures identified in paragraph 1 above, the change shall require Fort Smith to conduct a new cost of service analysis. In such event Fort Smith shall provide Van Buren with a written statement of the cause it believes warrants such a change; provided, however, such statement shall not limit the analysis and shall not be a basis of challenge of any rate resulting from the analysis. Any cost of service analysis shall be performed utilizing the latest American Water Works Association approved methodologies and shall give full force and effect to the 1983 Agreement as interpreted by the Award and agreements herein. Any cost of service analysis shall be performed by a professional rate consultant mutually acceptable to both Fort Smith and Van Buren. In such event, Fort Smith shall propose in writing to Van Buren a professional rate consultant. Van Buren shall accept or reject Fort Smith's proposal within thirty (30) days of receipt of the Fort Smith proposal. If Van Buren rejects the Fort Smith proposal, Van Buren shall propose a substitute professional rate consultant. The parties shall negotiate in good faith to reach a mutually acceptable professional rate consultant. If the dispute is not resolved within ninety (90) days, any party may cause the issue to be submitted for determination by arbitration according to the procedures set forth in the parties' Arbitration Agreement. The award of the arbitrators shall result in the selection of a professional rate consultant of national reputation and familiarity with the methodologies approved by the American Water Works Association, and familiarity with wastewater rate issues and any wastewater standards to which Fort Smith is contractually bound with any wastewater user of the Fort Smith system. The cost of service analysis shall determine, as to Van Buren, a rate that Van

Buren shall pay for water purchased from Fort Smith according to paragraph 3, subparagraph second, of the 1983 Agreement. Van Buren shall have the right to periodically inquire of the rate consultant and to review all then existing work papers and data compilations. No charge shall be imposed on Van Buren under any version of the Rate Model as authorized in this paragraph 4.B. unless rates and charges as then determined for all classes of customers shall be adopted simultaneously by Fort Smith.

5. The rate model resulting from an additional cost of service analysis shall be subject to change according to the procedures of paragraph 2A above.

6. In any subsequent arbitration proceeding conducted pursuant to this Supplement, the Arbitrators shall award the cost of arbitration, limited to Arbitrator expenses and arbitration hearing expenses, but not including the parties' witness and legal expenses and fees, to the party the arbitrators determine to be the prevailing party.

7. There is no intention of Van Buren and Fort Smith to obligate Fort Smith to determine rates and charges for users of the Fort Smith water system other than Van Buren according to the agreements and determinations herein. There is no intention of Van Buren and Fort Smith to bestow beneficiary status on any other water system user with reference to the agreements and determinations herein. As noted above, the agreements and determinations contained herein are based on the unique provisions of the 1983 Agreement. Fort Smith has the right to determine rates and charges for users of the water system other than Van Buren, and to make required changes in the Rate Model consistent therewith, without conformance to the provisions of this Supplement so long as Fort Smith does not adversely affect the rates and

charges of Van Buren in doing so.

IN WITNESS WHEREOF, each of the parties has caused this Supplement to be
duly executed.

City of Van Buren, Arkansas

By: [Signature]
Mayor

Attest: [Signature]
City Clerk

Date: 11/20/02

Van Buren Water and Sewer Commission

By: [Signature]
Chairman

Attest: [Signature]
Secretary

Date: 11/23/02

City of Fort Smith, Arkansas

By: [Signature]
Mayor

Attest: [Signature]
City Clerk

Date: Nov. 7, 2002

Protocol for Unaccounted-for Water Study -- Exhibit 2

The unaccounted-for water study shall be supervised by an independent, qualified firm selected by Fort Smith and approved by Van Buren or Arbitrator Chris Woodcock. The selected firm shall provide the scope of services for the study which shall reasonably incorporate the following:

1. Review Fort Smith's meter replacement and maintenance program.
2. Secure accurate measures of the total water produced and conveyed to the water transmission/ distribution system, including, without limitation, water conveyed to the transmission/distribution system at the Waldron-Midland facilities site. For this purpose, all production meters and measurement meters shall be calibrated to reasonably ensure that they are providing accurate measures of the total volume of water produced and entering the transmission/distribution systems. Any meters found to be providing significantly inaccurate measures must be repaired or replaced and calibrated so that accurate measurements can be reasonably assured. None of the foregoing language shall diminish the obligation of the selected firm to comport to the professional standards and to apply such standards recognized in the industry for such study.
3. Determine the consumption of any customers who are served between the treatment plant and the point of production metering and add that consumption to the production volumes registered on the meters. If these volumes are significant (i.e., more than one percent of total volume billed), these meters also shall be calibrated and repaired or replaced, if necessary, to assure the accurate measurement of such consumption.
4. Measure production using newly calibrated and accurate meters for a study period of at least twelve consecutive months starting as soon as possible and no later than November 1,

2002.

5. Tabulate and summarize the metered water usage and other relevant billing information for the period studied in a manner that permits the rates of charge in effect for the period to be applied to calculate total resulting charges. The consultant shall compare the calculated charges to the total revenues actually recovered in the ordinary course for the corresponding period. The consultant may adjust the total revenues in the event the period under study includes extraordinary, nonrecurring circumstances rendering the actual revenue recovery unreliable as a predictor of future events. If the total calculated charges are significantly different than the total revenues (adjusted for abnormal factors) actually recovered, then this information shall be recognized to adjust billed volume totals in the study.

By comparing accurate measures of total production and water conveyed to the transmission/distribution system at the Waldron-Midland facilities site with properly reconciled and adjusted (if necessary) metered volumes of water over the same period of time, a reliable measure of water production that is not reflected in the volume of water metered and sold may be derived. That data then shall be applied to the Rate Model in the same manner as the data was applied in the Arthur Young study of 1986.

DAILY & WOODS
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OF COUNSEL

HARRY P. DAILY (1886-1965)
JOHN P. WOODS (1886-1976)
JOHN S. DAILY (1912-1987)
BEN CORE (1924-2007)

November 14, 2011

Mr. Ray Gosack
City Administrator
City of Fort Smith
623 Garrison Avenue, 3rd Floor
Fort Smith, AR 72901

Re: Potential Year 2009 Water Cost "true up" with City of Van Buren Pursuant to Paragraph 4.A.1. of the Supplement to Final Settlement and Release Agreement with Van Buren

Dear Mr. Gosack:

At your request, we have reviewed the 2002 Supplement to Final Settlement and Release Agreement ("Agreement") with the City of Van Buren. In particular, we have reviewed the provisions of paragraph 4 of that Agreement.

Paragraph 4 deals with two methods by which the rate model or its inputs may be changed so as to produce an adjusted rate that Van Buren will pay for water purchased from Fort Smith. Pursuant to the parties' agreement, and without performing an independent cost of services analysis, the rates to be paid by Van Buren may be adjusted in only the two described manners. Pertinent here, a potential rate adjustment may be based on a comparison of projected values used with reference to a contract year to the actual values pertinent during the subject year as reflected by Fort Smith's audited CAFR.

The Agreement requires that, within sixty days of completion of Fort Smith's audited CAFR for the year 2004 and subsequent years through 2021, Fort Smith will provide to Van Buren information regarding a comparison of the actual annual factors of the rate model as compared to those same factors projected prior to the year. Based on the information provided, Van Buren has a period of sixty days in which to request a "true up" of the rate model substituting the actual values for the projected values. Fort Smith may accomplish the "true up" "regardless of the Van Buren election."

We have been advised that, for the year 2009, Fort Smith did not within sixty days of the completion of Fort Smith's audited CAFR provide the required information to Van Buren.

Based on the factual information of the preceding paragraph, it is our opinion that Van Buren could successfully contend that Fort Smith has waived the potential of a true up for the year 2009 and is

estopped from accomplishing the "true up" for 2009.

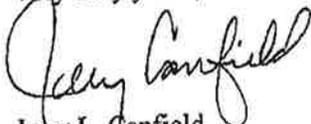
We express the foregoing opinion in spite of our established practice of viewing disputed fact situations and principles of law in the light most favorable to the City so that the City's actions can be taken by its policy makers and not dictated by our legal opinions. In this situation, the ability of Fort Smith to adjust the rates established by the rate model for the year 2009 can take place only pursuant to the procedures of paragraph 4.A. of the Agreement. If the procedures of 4.A. are not followed, the rate established by the rate model is applicable to water purchased by Van Buren in the year 2009. As the facts we have been asked to assume indicate, Fort Smith did not invoke the provisions of paragraph 4.A. by providing the information necessary to accomplish a true up within sixty days of completion of Fort Smith's 2009 audited CAFR.

We have formed our above stated opinion irrespective of the fact that the Agreement provision is "mandatory." That is, the contract requires Fort Smith to present the information within sixty days from completion of the audited CAFR. As the provision is mandatory, could it not be argued that Van Buren could enforce the provision after the fact and, thus, Fort Smith should be allowed to accomplish the providing of the information after the fact? After consideration, we do not believe that the mandatory language of the provision could be utilized by Fort Smith to make the argument raised by the preceding question.

Our opinion is based on principles of contractual waiver and estoppel provided for in Arkansas law. Waiver and estoppel defenses to contract claims are well established in Arkansas law and are covered by the Arkansas Model Jury Instructions ("AMI"). AMI 2436 provides that a party has waived a right under a contract if that party knew that the contract right existed and the right was voluntarily and intentionally abandoned. With reference to waiver, Fort Smith might argue that, in spite of its knowledge of the contract provision, the provision was not abandoned but that, by mistake, it was not timely implemented. Nevertheless, the defense of estoppel is applicable. A party having a contract right may be estopped from raising that contract right if the party knew of the right, reasonably should have expected that the other party was relying on its acting or not acting with reference to providing information, that the other party was ignorant of the facts necessary to implement the contract provision and that the other party relied in good faith on silence or failure to act. AMI 2438. We believe that Van Buren could legitimately present an estoppel defense based on Fort Smith's not providing, within the time period provided for by the Agreement, information on which the true up could have been accomplished.

Thank you for your attention in this matter.

Very truly yours,



Jerry L. Ganfield
JLC/cmm



November 16, 2011

Mr. C.E. Dougan, Chairman
Van Buren Municipal Utilities Commission
2806 Bryan Road
Van Buren, Arkansas 72956

Dear Mr. Dougan:

During the November 15, 2011 meeting of the Fort Smith Board of Directors, the board directed me to send Van Buren an invoice for the 2009 water true up. The true up provision is provided for in the supplement to final settlement and release agreement between Van Buren and Fort Smith dated October 18, 2002. Our calculations for 2009 show the true up amount to be \$253,706 owed by Van Buren to Fort Smith. Please consider this letter as an invoice for the 2009 water true up payment in the amount of \$253,706.

Sincerely,

A handwritten signature in black ink that reads "Ray Gosack".

Ray Gosack
City Administrator

E-mail: rgosack@fortsmithar.gov

cc: Mayor and Board of Directors
The Honorable Bob Freeman
Steve Parke, Director of Utilities
Kara Bushkuhl, Director of Finance

623 Garrison Avenue
P.O. Box 1908
Fort Smith, Arkansas 72902
(479) 785-2801
Administrative Offices FAX (479) 784-2430

Board Info
Steve Palle, Utilities
Kara Bush-Kuhl, Finance

VAN BUREN MUNICIPAL UTILITIES

Commission:
C.E. Dougan
John Barnwell
J.W. Floyd
Jim Williamson
Todd Young

“Providing Water, Sewer, and Sanitation Services”
2806 Bryan Road / P.O. Drawer 1269
Van Buren, Arkansas 72957
479-474-5067 / Fax 479-471-8969

Attorney
Paul Gant
Treasurer
Bryant Larcade
Secretary
Kathy Geppert

November 21, 2011

Mr. Ray Gosack
City Administrator, City of Fort Smith, Arkansas
P. O. Box 1908
Fort Smith, AR 72902

Dear Mr. Gosack;

I am in receipt of your letter dated November 16, 2011 regarding the water true up calculation for 2009. I have watched the re-broadcast of the November 14th Fort Smith board meeting. The Board's perception appears to be narrowly focused on only the 2009 true up. As a result, Van Buren is cast in a very disparaging light. The issues encompass more than just 2009 and I am of the opinion that your Board desires and deserves some explanation regarding Van Buren's position.

There seemed to be numerous questions concerning specific time frames within the Agreement applicable to the true up process. As you know, these time frames are critical given that budgets may need to be adjusted and Van Buren may have to implement a rate increase in order to pay the true up amount due during the next annual twelve month period. It was anticipated the time frames contained within the Agreement would typically conclude sometime in October to provide sufficient time to make adjustment to budgets and to pass a rate ordinance before payment would begin at the first of the next annual period.

There was also a lot of discussion concerning the \$161,000 remitted to Fort Smith by Van Buren and that not cashing the checks remitted was necessary to avoid satisfying in full additional amounts that might be owed by Van Buren. I assume you were acting on the advice of counsel but to imply that Van Buren was remitting this amount as payment in full for 2006 is simply a misstatement of facts. I communicated to you that Van Buren had calculated an amount of \$397,000 which we agreed may be owed to Fort Smith for 2006. We knew we owed at least \$161,000 because of increased treatment cost. I communicated that Van Buren would begin immediately remitting monthly 1/12 of this amount to Fort Smith. The difference of \$236,000 would be maintained in a cash reserve pending final resolution of the issues being discussed.

Beginning in July 2005 to present, Van Buren has informed Fort Smith of what it believes to be legitimate issues with the rate modeling process. Repeated errors together with the inconsistency in results have diminished our confidence in Fort Smith's ability to produce accurate information. This combined with an honest disagreement between the parties as to the reallocation of cost in the true up process encompass most of the issues. All of the issues have been thoroughly discussed and are well documented. However, some of the issues raised remain unresolved to this date. Following is a chronology of key events which will explain Van Buren's frustration with the true up process and our position regarding the amount Fort Smith believes is owed.

Serving Van Buren and Crawford County since 1893

October 22, 2007 Van Buren is informed that it owes an additional amount of \$480,774 for 2006. Van Buren is unable to verify the accuracy of this number. Subsequently, we discover the original comparative data provided is wrong. We calculate an amount of \$397,000 may be owed based on the revised information provided.

September 4, 2008 Van Buren is informed that it owes an additional amount of \$205,190.90 for 2007. Van Buren never received an electronic copy of Tyler Mitchell's calculations for the 2007 true up. As a result we were unable to audit the true up model and the data used to arrive at the \$205,190.90 or to verify that the data used was in fact the cost data provided earlier.

August 28, 2009 Van Buren receives the comparative cost data for 2008 and an electronic file containing the rate model. We were never able to reconcile the cost data to the electronic file. We concluded that the electronic file did not contain the true up data. Other than these documents Van Buren does not show that it received any billing or notification for additional amounts that might be owed for 2008.

October 21, 2010 Fort Smith is informed that Van Buren did not receive the 2009 true up data."

November 17, 2010 The City Wire published that Van Buren owed Fort Smith in excess of \$1.2 million, \$455,470 for 2006, \$205,191 for 2007 and \$539,453. These amounts were published again June 24, 2011.

September 3, 2011 it is reported in the Times Record that the more than \$1 million owed to Fort Smith by Van Buren is now \$581,174 and that the 2009 and 2010 amounts are still being calculated. The question that begs to be asked is what is the reason for the difference in amounts published? Would the difference been discovered had Van Buren not questioned the amounts Fort Smith presented as being owed?

The consensus in the November board meeting was to send Van Buren a bill, giving Van Buren the opportunity to do the right thing. One could assert that Fort Smith should be given the same opportunity. Van Buren simply request that Fort Smith accept responsibility for it's culpability in this matter.

The above listed events should demonstrate that the rate modeling process, especially the annual true up, has not worked as intended. Mr. Canfield correctly reminded the Board that Fort Smith is in control of the process. The rate model, data, data entry, calculations and accuracy of the information produced all belong to Fort Smith. Van Buren should be able to rely on the data provided and the result produced. As evidenced by the above referenced news reports this has not been the case.

The Agreement stipulates that any dispute between the parties during the true up process that cannot be resolved will be subject to arbitration. While I am of the opinion that Van Buren could present a good argument for not paying any amount, we do not feel this is appropriate or necessary. There comes a time when it is appropriate to agree to disagree and move on. I was of the opinion that representatives of Fort Smith and Van Buren had reached that point and agreement.

I would ask that it be communicated to the Fort Smith Board of Directors that Van Buren's agreement to pay any amount was intended to settle all amounts in question for the years in question. The Board should be aware that Van Buren's review of the cost incurred for the years 2006 through 2009 indicates that Van Buren's obligation is significantly less than the \$581,000. However, this amount was viewed by Van Buren as a reasonable and fair compromise given all that has transpired.

To avoid further confusion I will repeat Van Buren's proposal contained in an e-mail memo to Mr. Steve Parke dated October 18, 2011. This e-mail memo was in response to his letter dated September 14, 2011 and reads as follows:

The Van Buren Utilities Commission has authorized payment in the amount of \$581,173 for water purchased from Fort Smith which will satisfy in full all amounts owed for the years 2006 through 2009. Van Buren City Council met last night and voted to increase Van Buren's water rates to facilitate payment of this amount.

I would propose the following:

Fort Smith will cash the checks from Van Buren it presently has in hand totaling \$161,000 or return the checks to Van Buren and we will issue a new check for an identical amount. Van Buren proposes to pay the remaining balance of \$420,173 in equal installments of \$11,671.47 with the first payment to be remitted January 2012 and each month thereafter until paid in full.

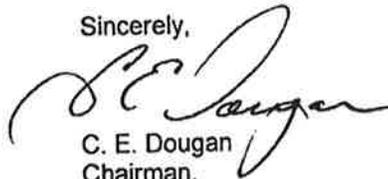
Unless Fort Smith and Van Buren otherwise agree, Van Buren will pay any amounts due to Fort Smith resulting from true up calculations for the year 2010 and subsequent years in twelve equal monthly installments in addition to the monthly amount shown above.

Should the true up calculation for 2010 or any subsequent year result in an amount due to Van Buren, we would request that the amount be first credited to any balance owed by Van Buren to Fort Smith for prior years true up calculations. Van Buren will not adjust the monthly amount being paid to Fort Smith resulting from any credit but would use the credit amount to decrease the time necessary for satisfying in full amounts owed to Fort Smith.

Fort Smith, with Van Buren's concurrence, has retained the services of Burns and McDonnell to review and make revisions to the rate model. Also, the Rate Analyst position has been filled. Although I have not seen Mr. Sandy's work, he seems very capable. My communication with you and Mr. Parke has always been received courteously and professionally. Even though we have disagreed there has been a mutual respect for each others position. I believe we both view the above as being positive. I am confident that we will be able to continue to work through issues that arise as we fulfill our responsibility to our respective cities.

I trust you will forward this correspondence to your Mayor, City Board, and other interested parties.

Sincerely,



C. E. Dougan
Chairman,
Van Buren Municipal Utilities Commission

Cc: The Honorable Bob Freeman
Steve Parke, Director of Utilities
Gary Smith, Manager, Van Buren Utilities

¹ Ref. letter dated 4/14/2008

¹ E-mail memo dated 10/21/2010

BOARD INFO

City of Van Buren, Arkansas

1003 Broadway • Van Buren, Arkansas 72956

cc: Steve Finkle, Utilities
Kara Bushby, Finance
Jeff Dingman, Admin.

November 22, 2011

Mayor Sandy Sanders
City of Fort Smith
P. O. Box 1908
Fort Smith, AR 72902

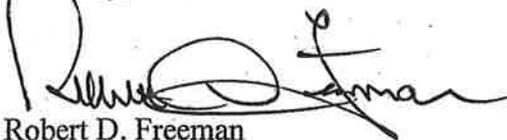
Dear Mayor Sanders,

I am enclosing a copy of the Van Buren Municipal Utilities response to Mr. Gosack's letter dated November 16, 2011. I am requesting that you share this letter with the City of Fort Smith Board of Directors.

I also discussed during our City Council meeting last night the request for a joint meeting of the Van Buren City Council, the Van Buren Utilities Commission, and the Fort Smith Board of Directors. We are of the opinion that the proposed meeting would not be constructive with such a large group, however, if after reading the enclosed response, you, Mr. Gosack, or any of the Directors have questions, I along with Mr. C.E. Dougan, Chairman of the Utilities Commission, will be glad to meet and address those questions.

Please feel free to contact me at 479-474-1541.

Sincerely,



Robert D. Freeman
Mayor

Enclosure

PROGRESS IS



OUR PROJECT

VAN BUREN CCF AND AMOUNT PAID FOR YEARS 2006-2010

	CCF	AMOUNT PAID
2006	2,530,390	\$3,228,703.66
2007	2,540,434	\$3,308,734.25
2008	2,568,825	\$3,605,481.81
2009	2,552,907	\$3,583,674.15
2010	2,804,067	\$3,927,763.34
TOTAL	12,996,623	\$17,654,357.21

CCF = 748 gallons

Average daily usage for the 5-year period is 5.3 million gallons

RETAIL WATER SALES

	<u>Gallons used</u>	<u>CCF Used</u>	<u>\$ Amt</u>
2006	5,628,156,204	7,524,273	16,126,056.23
2007	5,188,271,616	6,936,192	16,039,873.44
2008	4,931,984,376	6,593,562	17,794,224.06
2009	4,625,122,612	6,183,319	17,253,071.68
2010	4,904,005,436	6,556,157	18,814,676.19
Total	25,277,540,244	33,793,503	87,027,901.60

Retail customers



MEMORANDUM

December 30, 2011

TO: Mayor and Board of Directors

FROM: Ray Gosack, City Administrator

SUBJECT: Sales Tax Election

Directors Weber, Merry and Catsavis requested a review of the funding scenario for a variety of projects planned for the March sales tax election. The board had previously discussed using:

- sales tax bonds supported by a 3/4% sales tax for the fire service improvements, wet weather sanitary sewer improvements, and water transmission and storage system improvements as shown below.

PROJECT/PURPOSE	PROJECT COST	DEBT SERVICE RESERVE	BOND ISSUANCE COSTS	TOTAL
Refinancing of Existing Sales Tax Bonds	\$52,000,000	\$2,600,000	\$780,000	\$55,380,000
Fire Service Improvements	\$8,551,000	\$430,735	\$128,265	\$9,110,000
Wet Weather Sanitary Sewer Improvements	\$66,730,000	\$3,339,050	\$1,000,950	\$71,070,000
Water Transmission System Improvements	\$26,400,000	\$1,324,000	\$396,000	\$28,120,000
TOTAL	\$153,681,000	\$7,693,785	\$2,305,215	\$163,680,000

- a 1/4% sales tax for parks and recreation improvements and fire dept. costs as shown on the attached spreadsheet.

Some board members have asked to consider shifting the aquatic center project at Ben Geren Regional Park from the 1/4% sales tax to the bonded projects supported by the 3/4% sales tax. This would provide additional funding for other parks projects, and likely accelerate the ballfield projects. It would increase the number of ballot questions from 5 to 6, and would add an estimated 3 months to the life of the sales tax bonds.

If the board desires to make this change, we'll attempt to have a revised ordinance for the January 3rd regular meeting. If a revised ordinance can't be prepared in time, the ordinance in the meeting packet can be amended during the regular meeting to include the aquatic center project.



Attachment

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
1/8% FOR FIRE SERVICES						
Revenue	600,000	2,436,000	2,472,540	2,509,628	2,547,273	2,585,482
Purposes						
Station 11 Operations		287,500	1,150,000	1,173,000	1,196,460	1,220,389
Firefighter Equipment		190,000				
Aerial Apparatus Staffing	139,000	555,000	566,100	577,422	588,970	600,750
Command Staffing	51,000	204,000	208,080	212,242	216,486	220,816
Training		50,000	50,000	50,000	50,000	50,000
Training Center Construction	400,000	750,000				
Apparatus Replacement		400,000	450,000	450,000	475,000	475,000
TOTAL - FIRE	590,000	2,436,500	2,424,180	2,462,664	2,526,917	2,566,955
ENDING BALANCE	10,000	(500)	48,360	46,964	20,356	18,526

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
1/8% FOR PARKS SERVICES						
Revenue	600,000	2,436,000	2,472,540	2,509,628	2,547,273	2,585,482
Purposes						
Aquatic Center	550,000	2,175,000	1,275,000			
Aquatic Center Operations			75,000	76,500	78,030	79,591
Ben Geren Park Ballfields			625,000	625,000		
Chaffee Crossing Ballfields			250,000	800,000	550,000	
Parks Maintenance O & M Budget	50,000	250,000	250,000	300,000	500,000	700,000
Trails				575,000	625,000	600,000
Misc. Park Improvements					275,000	
Fort Smith Park Playground					100,000	
Creekmore Park Tennis Courts					250,000	
Creekmore Park Land Acq. & Parking						250,000
Tilles Park Tennis					20,000	
Soccer Fields & Park Along Riverfront Dr.						800,000
Neighborhood Park Construction				125,000	150,000	150,000
TOTAL - PARKS	600,000	2,425,000	2,475,000	2,501,500	2,548,030	2,579,591
ENDING BALANCE	0	11,000	(2,460)	8,128	(757)	5,891