

IRONHOUSE SANITARY DISTRICT

DRAFT WASTEWATER REVENUE PROGRAM

**Wastewater Treatment Plant Improvement Project
C-06-5046-110**

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DRAFT WASTEWATER
REVENUE PROGRAM

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BARTLE WELLS ASSOCIATES
Independent Public Finance Advisors
1889 Alcatraz Avenue
Berkeley CA 94703
Tel 510.653.3399
Fax 510.653.3769
www.bartlewells.com

Ironhouse Sanitary District Draft Wastewater Revenue Program

Wastewater Treatment Plant Improvement Project C-06-5046-110

Background

Ironhouse Sanitary District (ISD) provides wastewater collection, treatment, and effluent disposal services to a service area encompassing the City of Oakley and Bethel Island in eastern Contra Costa County. ISD's existing wastewater treatment plant has been in operation for almost 22 years. ISD serves approximately 13,000 accounts, of which about 97% are residential. ISD was originally founded as the Oakley Sanitary District in 1945, and after merging with two other regional districts, was renamed Ironhouse Sanitary District in 1992.

ISD is applying for a State Revolving Fund Loan (SRF Loan) from the State Water Resources Control Board (SWRCB) to help finance construction of new wastewater treatment and disposal facilities. These new facilities are needed to meet anticipated wastewater discharge permit requirements and accommodate growth. Federal and state regulations require SRF Loan applicants to prepare and implement a Draft Revenue Program demonstrating how ISD's rates and charges will a) adequately fund projected annual operating and maintenance expenses, including the costs of repairs and replacements, as well as debt service and other financial obligations of the SRF Loan, and b) equitably recover costs from ISD's customer base in proportion to the cost of collecting and treating each customer's wastewater discharge. This report demonstrates that ISD meets these requirements.

Financial projections indicate ISD will need to adopt substantial rate increases over the next five years to fund a) projected debt service payments and a required reserve fund for the SRF Loan, b) substantially higher operating costs for the new treatment facility, and c) ongoing operating cost inflation. Expansion capacity in the new plant is projected to be funded from growth via ISD's Plant Capacity Fees. However, ISD is aware that it will legally be required to raise rates as needed to meet its SRF Loan obligations, regardless of growth.

ISD plans to phase in the required rate adjustments in order to minimize the annual impact on ratepayers while ensuring adequate revenue recovery to fund future operating, capital, and debt service expenses. In June 2006 ISD adopted its first in a series of six anticipated annual rate adjustments. By gradually adjusting rates, starting in June 2006, ISD will minimize the need for a large future rate spike, generate a substantial amount of pay-as-you-go funding for the new treatment plant, reduce debt financing needs, and position itself to meet its long-term revenue requirements.

ISD also updated and, in June 2006, increased its capacity fees to ensure new development fully funds its share of capacity in existing and future facilities. The financial plan assumes a portion of revenues will be generated by capacity fees and service charges from a reasonable level of growth. ISD is aware that additional rate adjustments may be needed if growth occurs at lower-than-anticipated levels, in order to compensate for reduced capacity fee revenues and growth-related service charges.

New Treatment Plant Capital Costs

ISD's Wastewater Facilities Plan Update develops cost estimates for new wastewater treatment and disposal alternatives. Capital costs for these alternatives range from \$57 to \$98 million for the first 4.3 mgd phase of construction. ISD currently estimates that the project will cost approximately \$64 million.

Preliminary Financing Plan

Financial projections indicate that up to \$24.8 million of project costs can be funded on a pay-as-you-go basis using a combination of existing fund reserves, projected Plant Expansion Fees, and revenues set aside from proposed rate increases over the next five years as the project is being built.

ISD anticipates financing the remaining \$39.2 million with a low-rate State Revolving Fund (SRF) Loan. However, ISD may need or may want to use the SRF Loan to fund a larger portion of project costs.

| Anticipated Funding Sources | |
|-----------------------------|-------------------|
| Projected Cash Funding | \$24,800,000 |
| SRF Loan Financing | <u>39,200,000</u> |
| Total | 64,000,000 |

ISD is already well on its way to achieving its cash funding target for the project. As of January 31, 2007, ISD had accumulated approximately \$11 million in restricted fund reserves that it anticipates using to help fund the new treatment facilities.

The table on the following page shows debt service estimates for SRF Loans that generates \$39.2 million, ISD's anticipated SRF funding requirement, and also \$45 million, assuming a reduced cash contribution toward the project, such as due to minimal growth over the next few years. The table shows debt service for each scenario with both a conventional SRF Loan and a 0% Matching SRF Loan. Preliminary analysis indicates that the 0% Matching Loan would result lower debt service payments based on current interest rates.

Annual debt service on a \$39.2 million SRF Loan is currently estimated at about \$2.4 million assuming ISD pursues a Matching SRF Loan, or about \$2.7 million with a conventional SRF Loan at the projected rate of 2.5%, higher than the current rate. SRF Loans also require ISD to set aside 5% of the loan amount in a separate Wastewater Capital Reserve Fund (WCRF) that can be used for project repairs and replacements. ISD can satisfy the WCRF requirement by setting aside 1/10th of the annual debt payment annually for 10 years.

For comparison, if ISD decided to borrow \$45 million through the SRF Loan program, annual debt service would be about \$2.8 million with a Matching SRF Loan, and roughly \$3.2 million with a conventional SRF Loan assuming interest rates increase a little between now and loan award date..

SRF Loans provide two big advantages over conventional bond financing. Most important, they offer low, subsidized interest rates. The effective interest rates for a Matching SRF Loan is below 2% and for a standard 20-year SRF Loan is currently well below 2.5%. Another advantage is that the first debt service payment on an SRF Loan is not due until one year following project startup. This gives ISD time to phase in necessary rate increases.

| SRF Loan Debt Service Estimates | | | | |
|--|--------------------------------|---------------------------------|--------------------------------|---------------------------------|
| | \$39.2 Million Proceeds | | \$45.0 Million Proceeds | |
| | Standard SRF Loan | 0% Matching SRF Loan | Standard SRF Loan | 0% Matching SRF Loan |
| Project Cost | \$64,000,000 | \$64,000,000 | \$64,000,000 | \$64,000,000 |
| Construction Start Date | 03/01/08 | 03/01/08 | 03/01/08 | 03/01/08 |
| New Plant Startup Date | 09/01/10 | 09/01/10 | 09/01/10 | 09/01/10 |
| 1st Debt Service Payment Due | 09/01/11 | 09/01/11 | 09/01/11 | 09/01/11 |
| 0% SRF MATCHING LOAN | | | | |
| SRF Funding Requirement | | | | |
| Total Project Cost | \$64,000,000 | \$64,000,000 | \$64,000,000 | \$64,000,000 |
| Less Cash Contribution | <u>(24,800,000)</u> | <u>(24,800,000)</u> | <u>(17,000,000)</u> | <u>(17,000,000)</u> |
| SRF Funding Requirement | 39,200,000 | 39,200,000 | 47,000,000 | 47,000,000 |
| SRF Loan Amount | | | | |
| SRF Funding Requirement | 39,200,000 | 39,200,000 | 47,000,000 | 47,000,000 |
| Required SRF Cash Match | 0 | 7,840,000 | 0 | 9,400,000 |
| Est. Accrued Interest Through Sept-2011 | <u>2,600,000</u> | <u>0</u> | <u>2,900,000</u> | <u>0</u> |
| Total Loan Amount | 41,800,000 | 47,040,000 | 49,900,000 | 56,400,000 |
| Loan Term (Years) | 20 | 20 | 20 | 20 |
| Interest Rate (Est.) | 2.50% | 0.00% | 2.50% | 0.00% |
| Annual Loan Payment | 2,681,000 | 2,352,000 | 3,201,000 | 2,820,000 |
| WW Capital Reserve Fund Requirement | | | | |
| 0.5% of Loan Amount for 10 Years | 209,000 | 235,200 | 249,500 | 282,000 |

Capacity & Cost Allocation

The new facility will have the capacity to process 4.3 million gallons per day (mgd) of wastewater (average dry weather flow) with the potential to be expanded to 8.6 mgd. Approximately 2.3 mgd of capacity, 53.5% of total, is needed to meet the flow requirements of existing customers as of June 30, 2006. The remaining 2.0 mgd, 46.5% of total, will provide expansion capacity to meet the demands of growth. Based on these capacity allocations, about \$34.2 million of project costs are allocated to existing customers and \$29.8 million allocated to expansion capacity.

The table on the following page allocates project costs, funding sources, and debt to existing customers and expansion capacity.

| Allocation of Cost, Capacity, & Debt | | | |
|--|--------------------|--------------------|------------------|
| | Existing Customers | Expansion Capacity | Total |
| Plant Capacity Allocation | | | |
| Flow (mgd) | 2.30 | 2.00 | 4.30 |
| % of total | 53.5% | 46.5% | 100.0% |
| Cost Allocation | | | |
| Treatment plant project cost | \$34,233,000 | \$29,767,000 | \$64,000,000 |
| % of total | 53.5% | 46.5% | 100.0% |
| Projected Cash Contribution | | | |
| Plant Expansion Fee Reserves | 5,000,000 | - | 5,000,000 |
| Future Plant Expansion Fees | - | 8,200,000 | 8,200,000 |
| Rate Adjustments (Set Aside) | 6,300,000 | - | 6,300,000 |
| Connection Fees | 3,300,000 | - | 3,300,000 |
| Royalties | <u>2,000,000</u> | <u>-</u> | <u>2,000,000</u> |
| Total | 16,600,000 | 8,200,000 | 24,800,000 |
| SRF Loan Funding Requirement | | | |
| % of Total | 45.0% | 55.0% | |
| Estimated SRF Loan Payment | | | |
| | 1,058,000 | 1,294,000 | 2,352,000 |
| SRF Annual Reserve Fund Set Aside | | | |
| | 105,800 | 129,400 | 235,200 |

Capital Financing Requirements

Existing Customers: Financial projections indicate that existing customers' \$34.2 million share of project costs can be offset with about \$16.8 million of pay-as-you-go funding from a combination of existing fund reserves and rate increases over the next five years. ISD has already begun to gradually raise rates in anticipation of receiving SRF Loan financing. The rate increases will generate excess revenues each year, which can be used to provide cash funding for the project, until SRF Loan debt service payments start becoming due, at which point the revenues will be used to pay debt service. The remaining \$17.4 million of costs allocated to existing customers would be financed via an SRF Loan resulting in an annual debt service obligation of about \$1.1 million. This portion of debt service will be recovered by ISD's service charges.

Expansion Capacity: Based on slightly conservative growth projections and a new, higher Plant Capacity Fee adopted in September 2006, new development is expected to contribute at least \$8.0 million in cash funding toward construction via Plant Capacity Fees. The remaining \$21.8 million of expansion-related costs would be financed via an SRF Loan resulting in a \$1.3 million share of total debt service. This share of debt service should be recovered by ISD's future Plant Capacity Fees. Any additional Plant Capacity Fees collected prior to September 2010 could be used to further offset the need for debt financing.

Due to the unpredictability of growth, revenues from Plant Capacity Fees may not be adequate to pay the expansion-related share of debt service every year. In order to mitigate the fluctuations in growth-related revenues, it is recommended ISD maintain a minimum of 150% of expansion-related debt service in the Expansion Reserve Fund. These reserves will provide a cushion to cover temporary shortfalls in Plant Expansion Fees. At the same time, ISD should recognize that a prolonged period of low or no growth could result in the need for additional rate increases since ISD would still be obligated to make the full debt service payment from service charges, regardless of growth. ISD recently updated its Plant Capacity Fees and other connection fees to ensure new development pays its full share of infrastructure costs.

ISD will be required to make a legally binding pledge to raise rates as needed to meet its SRF Loan debt service obligations. If no Plant Capacity Fees were recovered, for any reason, ISD would have to raise its service charges to ensure adequate debt repayment. Of course, over the long run, the goal is that Plant Capacity Fee revenues will fund or reimburse ISD for any expenditure made on behalf of new development.

New Treatment Plant Operating Costs

The new plant will be designed to meet new, more stringent, wastewater discharge permit requirements and will be more expensive to operate than ISD's current facility. ISD estimates that operating costs will increase substantially when the new plant comes online due to higher electricity needs and costs, increased staffing requirements, and higher effluent disposal costs. ISD will need to start funding these higher operating costs when the new plant comes online in September 2010.

In 2010/11, operating cost increases are estimated at \$1.8 million assuming a partial year of operations. In 2011/12, the first full year of new plant operations, ISD will need to fund an additional \$2.3 million of operating costs. Although some of these new costs will be offset by growth in ISD's customer base, ISD will need to continue gradually raising rates so that it can fund the higher projected operating costs when the plant comes online. ISD's continued rate increase over the next five years includes anticipated future operation and maintenance costs.

Total Revenue Requirements

Substantial rate increases will be required over the next five years to fund the capital and operating costs of the new wastewater treatment plant. Major new costs will include:

- **SRF Loan debt service: \$2.4 million beginning 2011/12**
About \$1.1 million is allocated to existing customers and should be recovered via service charges. Approximately \$1.3 million is expansion-related and should be recovered by future annual Plant Capacity Fees. The annual debt service payment will be higher if ISD provides less cash funding than currently anticipated toward the project and ultimately increases the size of the loan.
- **New O&M costs: \$1.8 million in 2010/11 (partial year) to \$2.3 million in 2011/12 (full year)**
These costs will be recovered by District rates, and can be partially offset by other revenue streams benefiting ISD's customer base. Financial projections assume the new plant comes online in September 2010, resulting in a partial year of new O&M costs.

ISD will face a total of \$4.8 million in new debt service and operating revenue requirements by 2011/12, and will also need to raise rates to fund cost inflation and other budget increases, if any.

Cash Flow Projections

The following tables show 10-year financial projections through 2015/16. The first table shows anticipated cash flows under a moderate growth scenario, and the second table shows projections under a low growth scenario. Under the low growth scenario, ISD would a) receive fewer development impact fee revenues, which would reduce the amount of cash funding ISD could contribute to the project, b) incur more debt and be obligated to fund higher debt service payments, and c) recover service charge from a small customer base. All of these factors would contribute to the need for higher rate increases under a low growth scenario.

Ironhouse Sanitary District Cash Flow Projections

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | 2013/14 | 2014/15 | 2015/16 |
|---------------------------------------|-----------------|-----------------|-----------------|-------------|------------|------------|------------|------------|------------|------------|
| Annual Rate per EDU | \$412 | \$450 | \$490 | \$530 | \$570 | \$610 | \$625 | \$640 | \$660 | \$680 |
| Beginning EDUs | 12,430 | 12,850 | 13,350 | 13,850 | 14,350 | 14,650 | 14,950 | 15,250 | 15,550 | 15,850 |
| Total New EDUs | 420 | 500 | 500 | 500 | 300 | 300 | 300 | 300 | 300 | 300 |
| New EDUs | 220 | 300 | 306 | 500 | 300 | 300 | 300 | 300 | 300 | 300 |
| Prepaid EDUs | 200 | 200 | 194 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Interest Rate | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% |
| Operating/Capital Cost Escalation | <i>included</i> | <i>included</i> | <i>included</i> | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% |
| Beginning Fund Reserves | 15,755,000 | 17,305,000 | 18,023,000 | 19,071,000 | 13,028,000 | 12,629,000 | 12,817,000 | 12,954,000 | 13,028,000 | 13,086,000 |
| Revenues | | | | | | | | | | |
| Sewer Service Charges | 5,121,000 | 5,783,000 | 6,542,000 | 7,341,000 | 8,180,000 | 8,937,000 | 9,344,000 | 9,760,000 | 10,263,000 | 10,778,000 |
| Sewer Use Charge (New EDUs) | 87,000 | 113,000 | 123,000 | 133,000 | 86,000 | 92,000 | 94,000 | 96,000 | 99,000 | 102,000 |
| Fees (Insp. Pn Chk. Franchise) | 386,700 | 315,500 | 430,000 | 289,000 | 173,000 | 173,000 | 173,000 | 173,000 | 173,000 | 173,000 |
| Interest (All Funds) | 551,000 | 606,000 | 631,000 | 667,000 | 456,000 | 442,000 | 449,000 | 453,000 | 456,000 | 458,000 |
| Ad Valorem Taxes | 170,000 | 225,000 | 225,000 | 225,000 | 225,000 | 225,000 | 225,000 | 225,000 | 225,000 | 225,000 |
| Plant Capacity Fees | 3,300,000 | 2,353,000 | 2,401,000 | 2,732,000 | 1,680,000 | 1,722,000 | 1,765,000 | 1,809,000 | 1,855,000 | 1,901,000 |
| Trunkline Capacity Fees | 346,000 | 425,000 | 433,000 | 487,000 | 299,000 | 307,000 | 314,000 | 322,000 | 330,000 | 339,000 |
| Connection Fees | 621,250 | 713,000 | 731,000 | 750,000 | 461,000 | 472,000 | 484,000 | 496,000 | 508,000 | 521,000 |
| Cattle & Hay Sales | 650,000 | 585,000 | 560,000 | 560,000 | 560,000 | 560,000 | 560,000 | 560,000 | 560,000 | 560,000 |
| Gas Royalties | 750,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 200,000 | 200,000 | 200,000 | 200,000 | 200,000 |
| Lease Agmts/RD 830 Reimb/Other | 147,000 | 313,800 | 146,800 | 146,800 | 146,800 | 146,800 | 146,800 | 146,800 | 146,800 | 146,800 |
| Total Revenues | 12,129,950 | 12,432,300 | 13,222,800 | 14,330,800 | 13,266,800 | 13,276,800 | 13,754,800 | 14,240,800 | 14,815,800 | 15,403,800 |
| Expenses | | | | | | | | | | |
| Operating & Maintenance | | | | | | | | | | |
| Salaries/Administration | 3,087,150 | 3,554,400 | 3,723,400 | 3,910,000 | 4,106,000 | 4,311,000 | 4,527,000 | 4,753,000 | 4,991,000 | 5,241,000 |
| Professional Services | 416,540 | 418,000 | 383,500 | 403,000 | 423,000 | 444,000 | 466,000 | 489,000 | 513,000 | 539,000 |
| Maintenance Expenses | 838,500 | 915,000 | 873,500 | 917,000 | 963,000 | 1,011,000 | 1,062,000 | 1,115,000 | 1,171,000 | 1,230,000 |
| Office Expenses | 128,600 | 109,000 | 126,000 | 132,000 | 139,000 | 146,000 | 153,000 | 161,000 | 169,000 | 177,000 |
| Insurance | 244,990 | 160,600 | 168,300 | 177,000 | 186,000 | 195,000 | 205,000 | 215,000 | 226,000 | 237,000 |
| Cattle Operation | 358,960 | 345,500 | 353,900 | 372,000 | 391,000 | 411,000 | 432,000 | 454,000 | 477,000 | 501,000 |
| Add O&M for New WWTP | 0 | 0 | 0 | 0 | 1,780,000 | 2,260,000 | 2,380,000 | 2,500,000 | 2,640,000 | 2,772,000 |
| Reclamation Assessments | 304,300 | 324,400 | 336,000 | 346,000 | 356,000 | 367,000 | 378,000 | 389,000 | 401,000 | 413,000 |
| Other (Frm Fee Transfer & Fee Reimbs) | 22,000 | 25,000 | 25,000 | 26,000 | 27,000 | 28,000 | 29,000 | 30,000 | 32,000 | 34,000 |
| Subtotal | 5,401,040 | 5,851,900 | 5,989,600 | 6,283,000 | 8,371,000 | 9,173,000 | 9,632,000 | 10,106,000 | 10,620,000 | 11,144,000 |
| Debt Service & Capital | | | | | | | | | | |
| Outstanding Debt Svc & Repayment | 526,000 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| SRF Loan Debt Service, Projected | 0 | 0 | 0 | 0 | 0 | 2,352,000 | 2,352,000 | 2,352,000 | 2,352,000 | 2,352,000 |
| Rail Cr/JI Use/Lgl Reedy #1/Rly/Lgl | 208,000 | 90,000 | 35,000 | 50,000 | 53,000 | 56,000 | 59,000 | 62,000 | 65,000 | 68,000 |
| Capital Purchases & Projects | 360,000 | 192,000 | 115,000 | 200,000 | 210,000 | 221,000 | 232,000 | 244,000 | 256,000 | 269,000 |
| Replacement Rsvr Projects | 445,000 | 200,000 | 140,000 | 200,000 | 210,000 | 221,000 | 232,000 | 244,000 | 256,000 | 269,000 |
| Expansion Fund Projects | 1,520,000 | 630,000 | 125,000 | 250,000 | 263,000 | 276,000 | 290,000 | 305,000 | 320,000 | 336,000 |
| Plant Expansion, Cash Funding | 520,000 | 3,500,000 | 4,000,000 | 12,500,000 | 3,800,000 | 0 | 0 | 0 | 0 | 0 |
| Trunkline Projects (District Share) | 700,000 | 700,000 | 1,220,000 | 500,000 | 500,000 | 525,000 | 551,000 | 579,000 | 608,000 | 638,000 |
| TLC Reimbursements (70%) | 850,000 | 500,000 | 500,000 | 341,000 | 209,000 | 215,000 | 220,000 | 225,000 | 231,000 | 237,000 |
| Miscellaneous/contingency | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 |
| Subtotal | 5,179,000 | 5,862,000 | 6,185,000 | 14,091,000 | 5,295,000 | 3,916,000 | 3,986,000 | 4,061,000 | 4,138,000 | 4,219,000 |
| Total Expenses | 10,580,040 | 11,713,900 | 12,174,600 | 20,374,000 | 13,666,000 | 13,089,000 | 13,618,000 | 14,167,000 | 14,758,000 | 15,363,000 |
| Transfer to SRF WCRF | 0 | 0 | 0 | 0 | 0 | 235,200 | 235,200 | 235,200 | 235,200 | 235,200 |
| Revenues Less Expenses | 1,549,910 | 718,400 | 1,048,200 | (6,043,200) | (399,200) | 187,800 | 136,800 | 73,800 | 57,800 | 40,800 |
| Ending Fund Reserves | 17,304,910 | 18,023,400 | 19,071,200 | 13,027,800 | 12,628,800 | 12,816,800 | 12,953,800 | 13,027,800 | 13,085,800 | 13,126,800 |
| Debt Service Coverage on SRF Loan | - | - | - | - | - | 1.74 | 1.75 | 1.76 | 1.78 | 1.81 |

Ironhouse Sanitary District Cash Flow Projections (Low Growth Scenario)

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | 2013/14 | 2014/15 | 2015/16 |
|---------------------------------------|------------|-------------|-------------|-------------|------------|------------|------------|------------|------------|------------|
| Annual Rate per EDU | \$412 | \$460 | \$510 | \$570 | \$640 | \$740 | \$765 | \$790 | \$815 | \$840 |
| Beginning EDUs | 12,430 | 12,850 | 13,050 | 13,250 | 13,450 | 13,650 | 13,850 | 14,050 | 14,250 | 14,450 |
| Total New EDUs (Low Growth) | 420 | 200 | 200 | 200 | 200 | 200 | 200 | 200 | 200 | 200 |
| New EDUs | 220 | 0 | 6 | 200 | 200 | 200 | 200 | 200 | 200 | 200 |
| Prepaid EDUs | 200 | 200 | 194 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Interest Rate | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% | 3.5% |
| Operating/Capital Cost Escalation | included | included | included | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% |
| Beginning Fund Reserves | 15,755,000 | 17,305,000 | 15,818,000 | 14,508,000 | 12,592,000 | 13,083,000 | 13,146,000 | 13,223,000 | 13,304,000 | 13,360,000 |
| Revenues | | | | | | | | | | |
| Sewer Service Charges | 5,121,000 | 5,911,000 | 6,656,000 | 7,553,000 | 8,608,000 | 10,101,000 | 10,595,000 | 11,100,000 | 11,614,000 | 12,138,000 |
| Sewer Use Charge (New EDUs) | 87,000 | 46,000 | 51,000 | 57,000 | 64,000 | 74,000 | 77,000 | 79,000 | 82,000 | 84,000 |
| Fees (Insp. Pn Chk. Franchise) | 386,700 | 315,500 | 430,000 | 116,000 | 116,000 | 116,000 | 116,000 | 116,000 | 116,000 | 116,000 |
| Interest (All Funds) | 551,000 | 606,000 | 554,000 | 508,000 | 441,000 | 458,000 | 460,000 | 463,000 | 466,000 | 468,000 |
| Ad Valorem Taxes | 170,000 | 225,000 | 225,000 | 225,000 | 225,000 | 225,000 | 225,000 | 225,000 | 225,000 | 225,000 |
| Plant Capacity Fees | 3,300,000 | 793,000 | 802,000 | 1,093,000 | 1,120,000 | 1,148,000 | 1,177,000 | 1,206,000 | 1,236,000 | 1,267,000 |
| Trunkline Capacity Fees | 346,000 | 147,000 | 148,000 | 195,000 | 199,000 | 204,000 | 210,000 | 215,000 | 220,000 | 226,000 |
| Connection Fees | 621,250 | 285,000 | 292,000 | 300,000 | 307,000 | 315,000 | 323,000 | 331,000 | 339,000 | 347,000 |
| Cattle & Hay Sales | 650,000 | 585,000 | 560,000 | 560,000 | 560,000 | 560,000 | 560,000 | 560,000 | 560,000 | 560,000 |
| Gas Royalties | 750,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 200,000 | 200,000 | 200,000 | 200,000 | 200,000 |
| Lease Agmts/RD 830 Reimb/Other | 147,000 | 313,800 | 146,800 | 146,800 | 146,800 | 146,800 | 146,800 | 146,800 | 146,800 | 146,800 |
| Total Revenues | 12,129,950 | 10,227,300 | 10,864,800 | 11,753,800 | 12,786,800 | 13,547,800 | 14,089,800 | 14,641,800 | 15,204,800 | 15,777,800 |
| Expenses | | | | | | | | | | |
| Operating & Maintenance | | | | | | | | | | |
| Salaries/Administration | 3,087,150 | 3,554,400 | 3,723,400 | 3,910,000 | 4,106,000 | 4,311,000 | 4,527,000 | 4,753,000 | 4,991,000 | 5,241,000 |
| Professional Services | 416,540 | 418,000 | 383,500 | 403,000 | 423,000 | 444,000 | 466,000 | 489,000 | 513,000 | 539,000 |
| Maintenance Expenses | 838,500 | 915,000 | 873,500 | 917,000 | 963,000 | 1,011,000 | 1,062,000 | 1,115,000 | 1,171,000 | 1,230,000 |
| Office Expenses | 128,600 | 109,000 | 126,000 | 132,000 | 139,000 | 146,000 | 153,000 | 161,000 | 169,000 | 177,000 |
| Insurance | 244,990 | 160,600 | 168,300 | 177,000 | 186,000 | 195,000 | 205,000 | 215,000 | 226,000 | 237,000 |
| Cattle Operation | 358,960 | 345,500 | 353,900 | 372,000 | 391,000 | 411,000 | 432,000 | 454,000 | 477,000 | 501,000 |
| Add'l O&M for New WWTP | 0 | 0 | 0 | 0 | 1,780,000 | 2,260,000 | 2,380,000 | 2,500,000 | 2,640,000 | 2,772,000 |
| Reclamation Assessments | 304,300 | 324,400 | 336,000 | 346,000 | 356,000 | 367,000 | 378,000 | 389,000 | 401,000 | 413,000 |
| Other (Frm Fee Transfer & Fee Reimbs) | 22,000 | 25,000 | 25,000 | 26,000 | 27,000 | 28,000 | 29,000 | 30,000 | 32,000 | 34,000 |
| Subtotal | 5,401,040 | 5,851,900 | 5,989,600 | 6,283,000 | 6,871,000 | 7,473,000 | 7,963,000 | 8,453,000 | 8,943,000 | 9,433,000 |
| Debt Service & Capital | | | | | | | | | | |
| Outstanding Debt Svc & Repayment | 526,000 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| SRF Loan Debt Service, Projected | 0 | 0 | 0 | 0 | 0 | 2,820,000 | 2,820,000 | 2,820,000 | 2,820,000 | 2,820,000 |
| Rail Cr/JI Use/Lgl Reedy #1/Rly/Lgl | 208,000 | 90,000 | 35,000 | 50,000 | 53,000 | 56,000 | 59,000 | 62,000 | 65,000 | 68,000 |
| Capital Purchases & Projects | 360,000 | 192,000 | 115,000 | 200,000 | 210,000 | 221,000 | 232,000 | 244,000 | 256,000 | 269,000 |
| Replacement Rsrsv Projects | 445,000 | 200,000 | 140,000 | 200,000 | 210,000 | 221,000 | 232,000 | 244,000 | 256,000 | 269,000 |
| Expansion Fund Projects | 1,520,000 | 630,000 | 125,000 | 250,000 | 263,000 | 276,000 | 290,000 | 305,000 | 320,000 | 336,000 |
| Plant Expansion, Cash Funding | 520,000 | 3,500,000 | 4,000,000 | 6,000,000 | 2,500,000 | 0 | 0 | 0 | 0 | 0 |
| Trunkline Projects (District Share) | 700,000 | 700,000 | 1,220,000 | 500,000 | 500,000 | 525,000 | 551,000 | 579,000 | 608,000 | 638,000 |
| TLC Reimbursements (70%) | 850,000 | 500,000 | 500,000 | 137,000 | 139,000 | 143,000 | 147,000 | 151,000 | 154,000 | 158,000 |
| Miscellaneous/contingency | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 |
| Subtotal | 5,179,000 | 5,862,000 | 6,185,000 | 7,387,000 | 3,925,000 | 4,312,000 | 4,381,000 | 4,455,000 | 4,529,000 | 4,608,000 |
| Total Expenses | 10,580,040 | 11,713,900 | 12,174,600 | 13,670,000 | 12,296,000 | 13,485,000 | 14,013,000 | 14,561,000 | 15,149,000 | 15,752,000 |
| Transfer to SRF WCRF | 0 | 0 | 0 | 0 | 0 | 235,200 | 235,200 | 235,200 | 235,200 | 235,200 |
| Revenues Less Expenses | 1,549,910 | (1,486,600) | (1,309,800) | (1,916,200) | 490,800 | 62,800 | 76,800 | 80,800 | 55,800 | 25,800 |
| Ending Fund Reserves | 17,304,910 | 15,818,400 | 14,508,200 | 12,591,800 | 13,082,800 | 13,145,800 | 13,222,800 | 13,303,800 | 13,359,800 | 13,385,800 |
| Debt Service Coverage on SRF Loan | - | - | - | - | - | 1.55 | 1.58 | 1.61 | 1.63 | 1.64 |

Projected Rate Increases

Both the moderate growth and low growth financial projections demonstrate that ISD will be able to fund projected revenue requirements, including operating cost increases and SRF Loan debt service, with a series of gradual \$50 to \$60 annual rate adjustments, equivalent to roughly a \$4 to \$5 monthly rate increase each year for the next five years under moderate growth and low growth scenarios respectively.

The first table on the following page shows projected revenue requirements, EDUs, rates under the moderate growth scenario. From 2005/06 through 2011/12, the year of the first SRF Loan debt service payment, ISD will need to raise rates from the 2005/06 level of \$360 to over \$610 per year. This equates to a rate increase of roughly \$240 over the period, or about \$20 per month over five years under the moderate growth scenario. In order to steadily phase in this increase over six years, beginning in 2006/07, ISD would have to raise rates by about \$40 per year every year through 2011/12.

ISD has already taken the first step when it raised rates from \$360 to \$412 per EDU earlier this year (2006/07). ISD should continue to gradually raise rates each year in anticipation of the SRF Loan, but may have to adjust course depending on a number of factors such as growth, actual project cost, future operating cost inflation, etc.

It is recommended ISD gradually phase in the necessary rate increases so that revenues will be adequate to fund projected operating costs and SRF Loan debt service when the new treatment facility comes online. Phasing in the required rate increases over time provides a number of benefits:

- Enables ISD to gradually and steadily raise rates over six years, beginning in 2006/07, rather than postponing until a major rate spike is required.
- Additional revenues generated from the rate increases will provide pay-as-you-go funding for design and construction costs of the new treatment facility. These revenues will be used exclusively to fund existing customers' share of project costs. This will reduce existing customers' share of financing needs and result in a smaller SRF Loan, lower annual debt service, and ultimately slightly lower rates over the long-term.
- Puts ISD in much stronger financial position to issue bonds if an SRF Loan is not obtained.

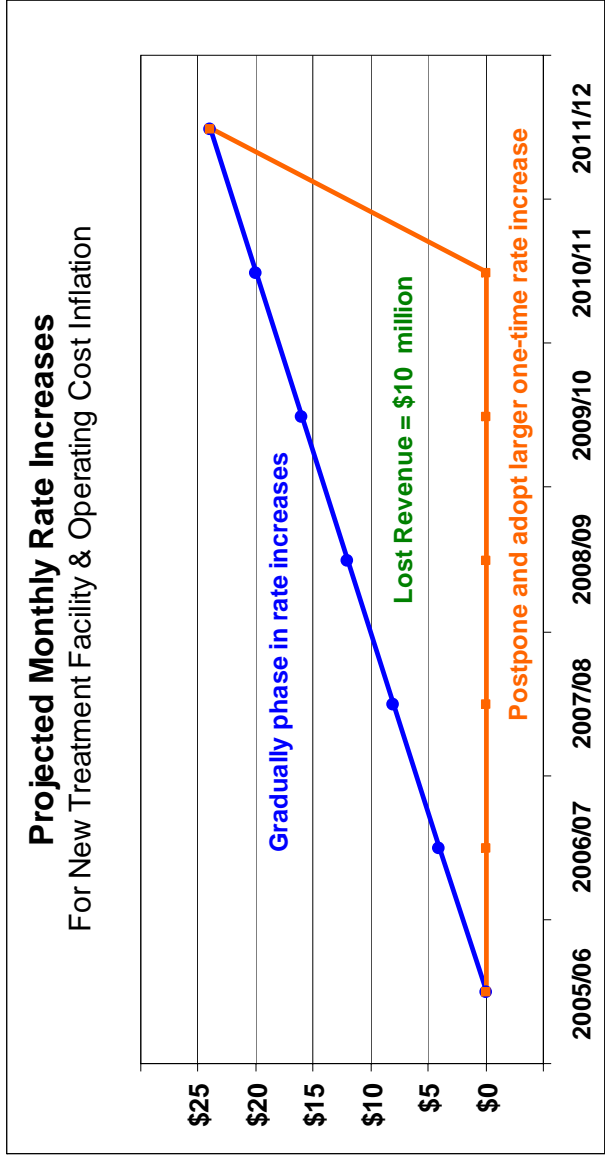
The chart on the following page compares the effects of a gradual phase in of rate increases with a scenario of postponing rate increases for a few years before adopting a larger one-time rate increase. The area between the lines on the chart represents the revenues that would be generated over the next five years by the incremental, annual rate increases. These revenues could be used to help fund the project and reduce the need for debt financing. These revenues would not be recovered if ISD opted to postpone rate adjustments and adopt a much larger, one-time rate increase in a few years.

The rate requirements presented in this report are based on current engineering estimates of capital and operating costs for \$64 million project alternative. These cost estimates may change depending on the final project facilities constructed to meet permit requirements issued by the Regional Water Quality Control Board and other factors such as the type of financing ultimately obtained. This could result in the need for higher, or lower, rate increases over the next five years. The recommended strategy of gradual annual rate adjustments preserves ISD's ability to adjust rates annually while keeping ISD on track to meet its long-term financial obligations.

Summary of Revenue Requirements, Rates, and EDUs

| | 2006/07 | 2007/08 | 2008/09 | 2009/10 | 2010/11 | 2011/12 | 2012/13 | 2013/14 | 2014/15 | 2015/16 |
|--|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|--------------|--------------|
| Service Charge Revenue Requirements | | | | | | | | | | |
| From Existing EDUs | \$5,121,000 | \$5,783,000 | \$6,542,000 | \$7,341,000 | \$8,180,000 | \$8,937,000 | \$9,344,000 | \$9,760,000 | \$10,263,000 | \$10,778,000 |
| From New EDUs ¹ | 87,000 | 113,000 | 123,000 | 133,000 | 86,000 | 92,000 | 94,000 | 96,000 | 99,000 | 102,000 |
| Total | 5,208,000 | 5,896,000 | 6,665,000 | 7,474,000 | 8,266,000 | 9,029,000 | 9,438,000 | 9,856,000 | 10,362,000 | 10,880,000 |
| Projected EDUs | | | | | | | | | | |
| Beginning of Year | 12,430 | 12,850 | 13,350 | 13,850 | 14,350 | 14,650 | 14,950 | 15,250 | 15,550 | 15,850 |
| New Connections ¹ | 420 | 500 | 500 | 500 | 300 | 300 | 300 | 300 | 300 | 300 |
| End of Year | 12,850 | 13,350 | 13,850 | 14,350 | 14,650 | 14,950 | 15,250 | 15,550 | 15,850 | 16,150 |
| Projected Rate Per EDU | | | | | | | | | | |
| Annual | \$412 | \$450 | \$490 | \$530 | \$570 | \$610 | \$625 | \$640 | \$660 | \$680 |
| Monthly Equivalent | 34.33 | 37.50 | 40.84 | 44.17 | 47.50 | 50.84 | 52.08 | 53.33 | 55.00 | 56.67 |

¹ Assumes new EDUs are connected for half of the year on average.



Rate Structure & Equitable Cost Recovery

ISD equitably recovers costs from its customer base based on the number of Equivalent Dwelling Units (EDUs) assigned to each customer. One EDU represents the wastewater flow and loadings of a typical residential customer or equivalent. For example, a laundromat with 12 washing machines would be assigned 4.2 EDUs based on a reasonable estimate of the wastewater flow and strength that would be generated. Therefore, the customer would pay a sewer service charge that is 4.2 times the base rate per EDU or single family residence. ISD's EDU assignments ensure revenues are recovered in proportion to the costs of collecting and treating each customer's estimated wastewater discharge.

ISD assigns EDUs based on the estimated flow and strength of each type of customer class according the formulas shown on the following table. EDU assignments based on units such as square footage, or seats in a restaurant, etc. are common for agencies that only provide wastewater services to their customers. The table also shows the number of accounts and EDUs by customer class.

| Accounts & EDUs | | | | |
|------------------------------|----------------------|-------------------|--------------------|-------------------|
| Customer Class | 07/01/05 Accounts | EDUs per Unit | Number of Units | 07/01/05 EDU's |
| Single Family Residential | 10,059.7 | 1 / dwelling unit | 10,059.7 | 10,059.7 |
| Church | 8.0 | each | 13.5 | 13.5 |
| Motels / Lodging | 1.0 | 1 + 0.5 / room | 80.0 | 41.0 |
| RV Connected | 12.0 | 0.40 / RV space | 380.0 | 152.2 |
| RV Unconnected | 2.0 | 0.07 / RV space | 34.0 | 2.4 |
| Laundromat | 3.0 | 0.35 / washer | 26.0 | 9.1 |
| Office | 8.0 | 0.5 / 1,000 sf | 27.0 | 13.5 |
| Retail Shop | 110.0 | 0.5 / 1,000 sf | 295.0 | 147.5 |
| Service Station w/ Rest Room | 4.0 | 0.4 / pump | 68.0 | 27.2 |
| Bar | 2.0 | 0.1 / seat | 110.0 | 11.0 |
| Restaurant - On Premises | 21.0 | 0.1 / seat | 1,306.0 | 130.6 |
| Restaurant - Fast Food | 13.0 | 4 + 0.1 / seat | 929.0 | 144.9 |
| Boat Launch Facilities | 9.0 | 2 per facility | 9.0 | 18.0 |
| Boat Berths | 27.0 | 0.04 / berths | 1,145.0 | 45.8 |
| Boat Berths - Live Aboard | 5.0 | 1 / vessel | 5.0 | 5.0 |
| Barber Shop | 3.0 | 1 + 0.5 / chair | 6.0 | 6.0 |
| Beauty Parlor | 6.0 | 1 + 1 / char | 17.0 | 23.0 |
| Dry Cleaner | 3.0 | 1 / business | 3.0 | 3.0 |
| Market | 8.0 | 1 / 1,000 sf | 95.4 | 95.4 |
| Medical/Dental | 4.0 | 1 / doctor | 7.0 | 7.0 |
| Veterinary | 2.0 | 3 / business | 2.0 | 6.0 |
| School - Primary | 6.0 | 0.067 / student | 4,087.0 | 273.8 |
| School - Secondary | 1.0 | 0.10 / student | 2,200.0 | 220.0 |
| Auto Repair Shop | 5.0 | 0.25 / 1,000 sf | 24.0 | 6.0 |
| Parks/Recreation | 4.0 | 1 / facility | 14.3 | 14.3 |
| Civic/Service | 11.0 | 0.5 / 1,000 sf | 52.4 | 26.2 |
| Total | 10,337.7 | | 20,995.3 | 11,502.1 |

ISD's EDU assignments have been reviewed for reasonableness and the EDU assignments for the various customer classes are well within industry norms and reasonably reflect the wastewater flow and strength of each customer class. Hence, ISD's system of rates and charges equitably recovers costs from the various customers classes based on a reasonable estimate of wastewater flow and strength.