

Hello Neighbor,

Reminder: The setting of the budget for 2009-2010 will be at 7:00 PM on Thursday July 16th at the Pine Cultural Center.

This email looks at the Compass Bank loan commitment. Parts of the commitment letter's Term Sheet have been blacked out, however, much of that information was revealed by Mr. Haney at the April 16th PSWID meeting. I have included that information in the description of the loan terms.

The Compass Bank commitment expires July 31st. Whether they can get an extension on that is unclear. So the terms and conditions described below may never come to pass since the sale of the water companies can't close by then. However, it does provide a view into what the board is willing to agree to and what the market is willing to provide.

1. Compass Bank Loan Terms

A. Amounts

- \$5,428,000 in 2009 and \$986,000 in 2010, for total of \$6,414,000
- Comment: Given the conditions in the loan and the other things they need to do to establish the District as an operator of a water system, I think that this gives them enough for a purchase price of \$3.5 million.

B. Pricing/Payment Structure

- 65% of the 30 Day LIBOR plus 300 basis points with a floor rate of 4%.
- Interest monthly for first 24 months. Interest plus principal monthly in months 25 through 119 with the principal divided by 240. Unpaid interest and principal due at the end of 10 years.
- Comment: Use of this creative financing increases the overall cost of the loan. The two years of interest only payments will increase the total cost of the loan by \$473,680, if the interest rate stays at the floor of 4%. Is it worth increasing the total cost of the loan so that raising rates can be avoided the first two years?
- Doesn't address it specifically, but the implication is that the interest rate would adjust monthly.
- 30 Day LIBOR is currently at 0.60%, so the interest rate would calculate to 3.39%. Since this is less than the floor interest rate of 4%, the 4% number would be used. The high for the 30 Day LIBOR in the last year was 4.55%. That would have produced an interest rate on the loan of 5.96%.
- Comment: Variable rate loans can come back and bite the borrower if interest rates don't cooperate. The federal government is suppressing interest rates right now, but when inflation kicks up they may not be able to sustain this. There is no cap rate on this loan.

C. Fees

- Commitment Fee: The board paid Compass Bank \$37,020 to obtain the commitment for the loan. This money is NOT refundable if the loan doesn't go through.

- Issuance Fee: This is blacked out and not known at this time. The board refused to provide this information when asked at the July 7th meeting. A fee of 1% would be about \$64,000.
- Refinancing Fee: This is blacked out and not known at this time. The board refused to provide this information when asked at the July 7th meeting. States that the refinancing fee applies up until the time that principle repayment starts after the first two years. Since it is the board's stated intent to refinance the loan through WIFA (and a condition of the Compass Bank loan) as soon as possible it is very likely that this fee will be paid.
- Comment: The board said that the information blacked out in the terms sheet was to keep Brooke from knowing information that might help them in the negotiations. It is hard to understand how hiding the interest rate being paid, the percentage to be paid as a refinancing fee fall into that category. Now that the cat is out of the bag on the loan amount, the board should provide the public with all of the information that was blacked out. There is no logical reason why this information should be withheld by the board. The only reason is that they don't want questions from the public about it.
- Brokerage Commission: This is outside of the Compass Bank loan. At the July 7th meeting Mr. Haney said that Stone & Youngberg were not involved in the Compass Bank loan. Mr. Haney said that they would collect a fee when the WIFA money is obtained.

D. Dates

- Loan closing deadline of July 31, 2009

2. Compass Bank Loan Closing Conditions

A. Acquisition of the Pugel/Randall Well

- Condition: "In connection with the closing of the loan, Borrower shall also acquire the Pugel/Randall Well in Pine, Arizona, which will improve the capacity of the project."
- Comment: This a most interesting condition. The board has been silent on their plans for purchasing the Milk Ranch well. Certainly they have not talked about the purchase of it as being required. They are currently "evaluating" the well, although it is hard to imagine any condition of the well that would keep them from buying it. It would be interesting to know whether the board had this condition added in order to provide them cover for purchasing the well.
- Comment: This is the kind of "stealth" maneuver that the board should avoid. If the Milk Ranch well is going to be purchased, it should be discussed in public, the valuation of the well should be public, and the performance of the well should be public. The board should have a specific vote on that purchase. It does the public a disservice to try and slide it in as a condition of a loan.

B. Purchase Agreement

- Condition: "Fully executed purchase and sale agreement (the "Purchase Agreement"), between Borrower and the proposed seller, together with all schedules, exhibits, amendments, and modifications thereto."
- Comment: From this and other language in the commitment letter, it is clear that this never covered funding immediate possession. The board still has not

addressed why they went ahead with the immediate possession when they didn't have the money.

C. WIFA Refinancing

- Condition: “the District agrees to actively apply for and attempt to obtain a loan from the Water Infrastructure Financing Authority of the State of Arizona in sufficient amount to pay off all amounts owing and due to Compass in a reasonable and timely manner.”
- Condition: “Confirmation by Compass that WIFA has the legal authority to refinance and fully repay the Loan such that no legal restrictions or impediments exist as to such refinancing by WIFA.”
- Comment: At an earlier PSWID meeting the board stated that WIFA is requiring a written opinion from the State that PSWID is a Domestic Water Improvement District (DWID). At the time Mr. Haney said that it would be nine months before the written statement was provided. Not clear how Compass Bank was going to get confirmation from WIFA prior to that.

F. CAP Allocation

- Condition: “The Purchase Agreement shall include the CAP Allocation held by the proposed seller such that the entire allocation held by the proposed seller shall be included in the Project in amount of no less than [161 feet per acre].”
- Comment: The CAP allocation has always been interesting. There isn't an official market for pricing/selling water allocations. None of the valuations that have been done include the value of the CAP allocation. Yet everyone seems to want to make sure that it is included in the sale. Depending on who you talk to, this allocation could add significantly to the cost of the water systems.

3. Compass Bank Operations Conditions

- Condition: “prior written bank approval of all capital expenditures in excess of \$100,000”
- Condition: “prior written bank approval of borrowings from any other entity”
- Condition: “prior written bank approval of all guarantees”
- Condition: “monthly balance sheet, profit and loss statement, and accounts receivable aging”
- Condition “annual internally prepared operating and capital expenditure budget
- Condition: “annual audited financial statements by a CPA firm approved by the Bank”
- Comment: It looks like Compass Bank plans to take an active hand in the running of the water system. Since the rate analysis that the board is relying on overstates revenue and understates operational costs, it will be interesting to see how long it takes before Compass Bank tells them to raise rates.