

Hello Neighbor,

Attached to this email is the latest spending chart for PSWID. It is over \$450,000 and rising. Looks like the total condemnation cost will end up in the \$550,000 to \$600,000 range.

I worked through the revenue, operational costs, and loan costs based on the current publicly available information, ACC annual reports filed by Brooke, the Economists.com rate analysis, and the Coe and Van Loo reports:

- In Year 1, operations expenses exceed revenue by \$205,321. Revenue will need to be increased by 16.0% in order to be in balance.
- In Year 2, operations expenses exceed revenue by \$293,672. Revenue will need to be increased by 22.8% in order to be in balance.
- In Year 3, operations expenses exceed revenue by \$478,793. Revenue will need to be increased by 37.0% in order to be in balance.

The PSWID board continues to maintain that there will not need to be any rate increases for the next two years. Their claim does not stand up to scrutiny. It does the community a great disservice to continue to mislead the public on what the cost impacts of purchasing the water systems will be.

In the sections below I explain how the numbers were arrived at. Much of the difference between the board's estimate and mine is in the operations costs. They have used a number of \$882,000 per year versus an adjusted operations expense of \$1,179,851.47 based on actual expenses by Brooke. I think that even the PSWID board will agree that Brooke didn't spend a dollar more than they had too. If the PSWID board wants to deliver on its promise of improved service, then they will need to spend more for the operations budget than Brooke has.

1. General Approach

- The year 2006 was Brooke's best year and 2007 was their worst year. In this analysis the two years were averaged to get something closer to a typical year.
- All of the numbers discussed combine the results for Pine Water Co. (PWCo) and Strawberry Water Co (SWCo).
- Corrected for the errors in the Economists.com report that affect this analysis. Some of the errors in the Economists.com analysis affect the calculation of the added revenue from rate changes and they were not relevant here. For a refresher on the Economists.com analysis errors, you can find the analysis here: <http://www.waterforpinestrawberry.com/data%20pages/CashFlowCorrection.htm>
- The year 2007 contained some large spikes and dips in various expense categories. For those the years 2005 and 2006 were averaged together.

2. Revenue

- In 2007 there were a combined 3084 customers
- Increased the number of customers by 14 per year as was done in the Economists.com analysis:
 - Year 1: 3112

- Year 2: 3126
- Year 3: 3140
- The average water generated revenue for 2006/2007 is \$1,251,001.50. To get to the water revenue for Year 1 thru Year 3, it is scaled by the increase in customers. This implies that the new customers use on average the same amount of water as the current customers.
 - Year 1: \$1,262,359.49
 - Year 2: \$1,268,038.49
 - Year 3: \$1,291,063.83
- There are revenues that don't come from water. The 2006/2007 average is \$39,563.50. This number varies a lot year to year. The Economists.com analysis used a value of \$20,000, so that was used in the analysis as well.

3. Operations Expenses

- The unadjusted average 2006/2007 operations costs were \$1,304,186.50. The adjusted average 2006/2007 operations costs were \$967,879.50. The following adjustments were made:
 - Subtracted \$55,348.00 for property tax expenses. As a government entity the district will not have to pay these taxes. Gila County will have to make them up elsewhere.
 - Subtracted \$94,968.50 for depreciation expense. Comment: Every water system operational budget that I have seen includes depreciation. The 2003 analysis done by Economists.com includes depreciation as part of the operational budget. Mr. Haney is adamant that depreciation should not be included, and it wasn't included in the Coe and Van Loo report. Since it is a non-cash charge I'm going along with it to reduce the amount of moaning by the board.
 - PWCo saw expenditures on Purchased Power quadruple in 2007. Averaged 2005/2006 and used \$39,228.50 instead of \$79,839.00.
 - Both PWCo and SWCo had Repairs and Maintenance drop to zero in 2007. Averaged 2005/2006 and used \$47,111.50 instead of \$23,249.00.
 - PWCo saw a large spike in the cost of Outside Services because of the legal spending over K2. Averaged 2005/2006 and used \$83,642.50 instead of \$201,233.50.
 - PWCo had a large jump in Miscellaneous expenses in 2007. Averaged 2005/2006 and used \$100,012.50 instead of \$151,664.00.
- To get to the operations costs for Year 1 thru Year 3, assumed cost growth of 4% per year as is used in the Economists.com analysis. Since two years separate the 2006/2007 average and Year 1, there is 4% counted for each of those two years. For year 1 an adjustment of \$132,993 was added to account for the difference between Brooke's Wages and Salaries expense and the projected cost for the district.
 - Year 1: \$1,179,851.47
 - Year 2: \$1,227,045.53
 - Year 3: \$1,276,127.35

4. Loan Cost

- Borrowing \$5,428,000 in Year 1 and \$986,000 in Year 2

- In the local paper, Mr. Haney stated that the newly negotiated loan interest rate would be 4.75%. Assuming that it is interest only for first two years. This loan covering Year 1 and Year 2.
- Mr. Haney stated that the WIFA loan acquired in the future would at 3.5%. WIFA makes 20 year loans with no creative financing. This is the loan covering Year 3. Every 0.5% increase in the loan's percentage rate increases the yearly cost by about \$20,000.
- Loan cost:
 - Year 1: \$257,830
 - Year 2: \$304,665
 - Year 3: \$446,383
- Comment: To get the WIFA loan there is a waiting list. At this point the money for 2010 is probably already spoken for. So 2011 would be the earliest it could be acquired. The WIFA loan payment includes principal and interest, so it is significantly higher than the interest-only Compass Bank loan. Accelerating WIFA loan accelerates the revenue shortfall.

5. Contingency

- Added \$50,000 for contingencies. The Economists.com analysis has much higher numbers.