

FINAL REPORT and RECOMMENDATION

of the Columbia Ad Hoc Committee

for the

LASA Acquisition of the Columbia Sewer System

May 6, 2014

OUTLINE

1. Introduction
2. Executive Summary
3. Borough Bonds
4. Bulk Treatment Agreement
5. Schedule
6. Valuation Summary
7. Pros and Cons
8. Alternative
9. Recommendation

1. Introduction

This Final Report and Recommendation is a follow-up to the Interim Report this Ad Hoc Committee issued in December 2013. This Final Report should be read along with the Interim Report because the Interim Report contains background which will not be repeated here. This Final Report updates the Interim Report with new information, new options and a revised valuation.

2. Executive Summary

LASA has made an offer to purchase the assets of the Columbia Municipal Authority's wastewater collection and treatment system. Like many agreements, the offer is based on several contingencies and assumptions. The details of the offer are summarized as follows:

1. Cash on signing of Asset Purchase Agreement - \$8,600,000
2. LASA will assume responsibility of principal and interest payments on the Columbia Build America Bond until November 2020. Value approximately \$2,617,000 (could go as high as \$4,800,000) for interest and approximately \$1,655,000 for principal.
3. November 2020, LASA will make a lump sum payment to Columbia an amount of \$9,590,000 for purposes of paying off the Bond.
4. LASA will assume the risk of the subsidy payment being reduced up to \$4,000,000. If subsidy is reduced by more than that amount, LASA reserves the right to add a surcharge (of no more than \$4.00) to monthly sewer bills. This reduces Columbia's risk of subsidy loss by approximately \$900,000.
5. There will be a five year transition to LASA flat rates.
6. LASA will not charge a tapping fee for capacity at their WWTP.
7. LASA will pay Columbia \$87,500 per month to treat LASA sewage at the Columbia WWTP until the pump station and force main are operable.
8. LASA will offer up to 4,000 Nitrogen credits per year until the pump station and force main are operable. Approximate value for three years @ \$0.75 per credit is \$9,000.

The financial value to Columbia can be summarized as follows:

Cash on Signing	At Closing	\$ 8,600,000
Savings on Bond Interest	Now through Nov 2020	\$ 2,617,000
Savings on Bond Principal	Now through Nov 2020	\$ 1,655,000
Nitrogen Credits	First three years	\$ 9,000
Total		\$12,881,000

3. Borough Bonds

As discussed in the Interim Report, the Columbia Bond has restrictions as to when it can be paid off and the purposes for which the bond proceeds can be used. Initially, this created some concerns about the net benefit to Columbia because of the significant carrying costs until November 2020 at which time the Bonds could be called. Since the time of the Interim Report, LASA has proposed to assume the principal and interest payments on the Columbia Bond and use the proceeds to build the pump station and force main. Through a subsidy agreement, LASA will agree to make the P&I payments on the Bond through November 2020. At that time, LASA will evaluate the financial market and decide whether to keep the Bond or refinance it.

The current proceeds of the Bond are \$11.2M and the expected cost of the pump station and force main is \$9.4M. LASA has agreed to use the remaining \$1.8M for wastewater capital expenses. These capital expenses may be at the LASA WWTP which Bond Council has advised this would be in conformance with the Bond requirements. Under this arrangement, Columbia would rely on LASA to meet the financial responsibilities of the bond payments estimated to be \$2.62M (Interest) and \$1.65M (Principal) through November 2020.

4. Bulk Treatment Agreement

After the Asset Purchase Agreement is signed, LASA will immediately own and control the Columbia wastewater system. LASA will be responsible for treatment, collection system, billing, etc. Since it will take several years to design and build the pump station and force main, provisions will be needed to treat the sewage generated by Columbia. During construction of the pump station and force main, Columbia will treat sewage for LASA under a Bulk Treatment Agreement. Basically, LASA will become a bulk user of the WWTP and will pay the Borough to treat the LASA sewage generated in the Borough and portions of West Hempfield. The Bulk Treatment Agreement is an important component of the Asset Purchase Agreement in that it sets LASA's costs for the next several years.

The fee to treat the sewage was developed by reviewing the actual annual operating costs and budgets and determining which budget line items were associated with sewage treatment. Costs associated with operating and maintaining the collection system were not included since this will become a LASA responsibility. Likewise, costs for debt service and sewer bill collections were removed since LASA will be responsible for those functions. Based on this approach, the agreed upon annual fee for treating the bulk sewage from LASA is \$1,050,000 (\$87,500 per month). Any costs (except as noted for Equipment Maintenance) over the \$87,500 per month would be the financial responsibility of the Borough of Columbia. Likewise, if costs are below the \$87,500 per month, the Borough of Columbia can keep the difference.

Attachment No. 1 summarizes the method to determine the monthly operating fee and was reviewed and modified at our March 5, 2014 meeting with LASA. This estimates that the Borough

would need \$89,000 per month to operate the plant (LASA is offering \$87,500). The table included an amount of \$108,160 for Wastewater Manager to account for using ARRO to provide the manager. This cost could be significantly reduced by replacing ARRO with a part-time operator. The budget includes an Administrative fee of \$130,048 to cover ongoing costs for Ron Miller, Georgianna Schreck, etc. The budget does not include any principal or interest payments for outstanding debt other than the Build America Bond. Presumably, outstanding debt would be paid at closing.

The amount for Maintenance of Equipment is limited to \$20,000. LASA is proposing to share the cost of equipment maintenance for anything over \$20,000. A review of the operating budget for the past four years shows that we have spent on average a little less than \$50,000 per year on Maintenance of Equipment. Therefore, our risk could be projected to be half of the difference, which would be \$15,000 per year, or \$45,000 for the three-year contract. Actual maintenance costs above or below this budget would either benefit the Borough or be the responsibility of the Borough to pay.

Finally, the Borough should be aware that an asset sale to LASA will eliminate the annual administrative fee paid by the Authority to the Borough for the Borough's costs associated with operating the sewer system. Initially, during the term of the Bulk Service Agreement, this administrative fee will be partially paid. Then, when the pump station and force main are completed, the administrative fee will disappear completely. The Borough will have to determine how to manage this loss of revenue. Presumably, this will be accomplished through expected planned retirements and reassignments.

5. Schedule

LASA developed and provided a "Term Sheet" that identifies the major areas of agreement between LASA and the Ad Hoc Committee. Within the Term Sheet, LASA identified several key dates which, depending on the timing of signing of the Asset Purchase Agreement, will probably be delayed. The key dates on the Term Sheet are as follows:

Finalize Asset Purchase Agreement	July 2014
Finalize Bulk Treatment Agreement	July 2014
Finalize Construction Agreement	July 2014
Execute Agreements	September 2014
Close on Asset Purchase Agreement	December 2014

6. Valuation Summary

Given all the assumptions and variables discussed above, the current LASA valuation of the Columbia system is approximately \$12.88M. This valuation is based, in part, on the following factors:

- Discount / Borrowing rate of 4.36%
- Revenue / O&M inflation Rate of 3.0%
- LASA paying for 5% of pump station and force main (for future West Hempfield growth).
- Zero growth in Columbia Borough. LASA will make future payments of \$1,028 / EDU.
- Five year transition to LASA flat rates.
- LASA will use proceeds from Columbia Bond and enter into agreement to make Bond payments. This will save Columbia approximately \$4,272,000.
- In November 2020, when Bonds are callable, LASA will make a payment of \$9.59M.
- LASA will provide up to 4,000 nitrogen credits each year.
- Columbia does NOT have an equity position in LASA.

The financial value to Columbia can be summarized as follows:

Cash on Signing	At Closing	\$ 8,600,000
Savings on Bond Interest	Now through Nov 2020	\$ 2,617,000
Savings on Bond Principal	Now through Nov 2020	\$ 1,655,000
Nitrogen Credits	First three years	\$ 9,000
Total		\$12,881,000

Costs

Demolition of Plant	2016-2018	\$ 500,000
Equipment Maintenance Risk	Next 3 Years	\$ 45,000
Payoff existing Loans*	At Closing	\$ 753,000
Total		\$1,298,000

* Municipal Authority currently has approximately \$1,334,000 in various capital accounts. Note that in 2014, prior to settlement, the Authority will have to make principal and interest payments (net of Bond Subsidy) of approximately \$713,000.

The initial Net Cash to Columbia at closing would be as follows:

Cash in From LASA at Closing	+\$8,600,000
<u>Cash out for above Costs</u>	<u>-\$1,298,000</u>
Net Cash to Borough	+\$7,302,000

7. Pros and Cons

In addition to the apparent attributes of the financial offer, there are other non-monetary factors that should be considered.

PROS

1. Lower Rates – Overall LASA will be lowering rates within Columbia. Commercial rates will be lower which could attract industry.
2. Flat Rate – LASA is proposing a flat rate which more consistently reflects the actual cost of operating a wastewater system.
3. Stable Rates – LASA has a long history (and large customer base) of stable rates and only modest, inflationary rate increases are expected (see Attachment No. 2).
4. LASA is a highly respected sewer Authority with professional staff and reasonable rates.
5. The location of the WWTP is problematic due to flooding and the impact of trains that are increasing in length (long trains block access to WWTP).
6. Potential for excess revenue from Bulk Service Agreement if actual operating costs are less than budget.
7. Epitomizes the Borough's, DEP's, and EPA's philosophy of regionalization and all its positive aspects, particularly economies of scale.
8. Eliminates another point source of pollution to the Susquehanna River and the Chesapeake Bay.
9. All risks will shift from Columbia Borough to LASA including: compliance to DEP and EPA current and future regulations, costs for future upgrades at the plant and in the collection system, law suits, and liability due to contractor and employee health, accident, and death issues in a high risk occupation -- Public Works!
10. Capital project dollars, estimated at \$7.3 Million, become available for Borough projects.

CONS

1. Lower Rates – The rate changes will result in those customers who pay the current minimum rate will be paying a higher flat rate. This will also negatively impact the two high-rise elderly buildings.
2. Eliminates cash flow associated with sewer revenues and Administrative Fee paid by Authority.
3. During the term of the Bulk Treatment Agreement (approximately three years) risk of having to share equipment maintenance costs that are in excess of \$45,000.
4. Potential shortfall in Bulk Service Agreement in covering WWTP expenses.
5. Loss of control over rate making.
6. The deal is forever and forever eliminates the cash flow.

8. Alternative

Over the years, the Columbia Municipal Authority considered many alternatives to upgrade the WWTP. After a final review with our engineering consultant, Entech, the remaining WWTP upgrade alternatives can be summarized as follows:

1. Upgrade the plant with a 5-stage BNR process to achieve permit limits for nitrogen and phosphorus. The cost for this alternative, including engineering, finance and legal, is approximately \$11.64M (based on a construction estimate of \$9.7M + 20% soft costs).
2. Upgrade the plant to simply replace all existing equipment and maintain the same process. This will not fully treat for nitrogen so we will need to purchase nitrogen credits (range of \$5,000 to \$10,000 per year). This option, including engineering, finance and legal, will cost approximately \$ 10.32M (based on a construction estimate of \$8.6M + 20% soft costs).

The reason there is very little difference in the cost is explained by the fact the existing plant is well past its useful life and all of the equipment needs to be replaced regardless of the alternative selected. We got everything we could out of the existing plant and now must pay to replace the well-worn equipment.

9. Recommendation

The Ad Hoc Committee was formed to investigate the possibility of selling the assets of the Columbia sewer system to the Lancaster Area Sewer Authority. In order to assist our effort, we hired the services of an expert, David Busch, from Keystone Alliance Consulting to provide review and guidance through this process. David Busch recommends proceeding with the asset purchase by LASA. After considering the Terms that LASA has offered, as well as considering the pros & cons of the offer, the Ad Hoc Committee recommends moving forward with an asset purchase by LASA.

Wastewater Fund Proposed 2014 budget

ATTACHMENT NO. 1

	A	B	P	R	S	T	U	V	W	X
1	Code	DESCRIPTION	Budget		To Be Included					
2			2014		In LASA Fee	Notes from meeting with LASA 03/05/2014				
3										
34										
35		EXPENSES								
36	400.120	AUTHORITY SALARIES	5,400		5,400					
37	400.999	AUTHORITY Misc EXPENSES	2,500			Eliminated. Won't be going to any conferences, etc.				
38		INTERGOVERNMENTAL TOTAL	7,900		5,400					
39										
40	401.100	Administrative Fee	304,497		130,048					
41		Subtotal	304,497		130,048					
42										
43	407.300	Billing Fees and Costs	37,000							
44		Subtotal	37,000							
45										
46	409.352	Liability/property/auto Insurance	49,000		30,000	reduced \$10,000 arbitrarily. Boro to verify				
47		Subtotal	49,000		30,000	cost reduction with insurance carrier.				
48										
49	429.120	PW director(1/2 ww 1/2 gf)	35,816		35,816					
50	429.121	Wastewater Manager	50,000		108,160	ARRO's rate				
52	429.123	Envir. MGr (2/3 ww 1/3 gf)	30,971		30,971					
53	429.161	Payroll Taxes FICA	27,044		17,441					
54	429.180	Wastewater Plant Operators Lic	1,600		1,600					
55	429.181	Permanent Part time (1)	15,600			Eliminate Position				
56	429.184	Overtime	35,000		28,000	reduced 20% for Collection system				
57	429.185	summer help	14,000		9,380	reduced 1/3 due to less maintenance				
58	429.186	Plant Personnel- (4 FT)	165,087		123,815	reduced 25% for Collection system				
59	429.187	Biosolids Hauling	500		500					
60	429.188	Service Contract	4,900		4,900					
61	429.189	Misc. Expenses	1,500		1,500					
62	429.210	Office Supplies & Expenses	4,500		4,500					
63	429.220	Chlorine/Nacl	2,500		2,500					
64	429.221	Lime	12,500		12,500					
65	429.222	Alum	15,000		15,000					
66	429.223	Polymer	11,000		11,000					
67	429.224	Plant Supplies	4,000		4,000					
68	429.225	Lab Equipment and Supplies	3,500		3,500					
69	429.226	Outside Lab Analysis	25,000		25,000					
70	429.227	Well Water Testing	0		0					
71	429.231	Vehicles - Regular Fuel	4,000		3,000	Reduce 25% for collection system				
72	429.232	Vehicles - Diesel Fuel	5,000		3,750	Reduce 25% for collection system				
73	429.238	Uniforms	3,500		3,500					
74	429.251	Vehicles Repairs - Parts	0		0					
75	429.252	Vehicle Repairs	15,000		10,050	Reduce 1/3 for collection system				
76	429.260	Maintenance of equipment	52,000		20,000	Consider reducing by separate agreement				
77	429.311	Accounting/auditing fees	11,200		11,200	Reduce 25% in 2nd & 3rd years				
78	429.313	Consulting Engineer	25,000		10,000	Reduced since no proposed projects				
79	429.314	Legal Expenses	35,000		17,500	Reduced since this is for collecting liens.				
80	429.315	Sewage Enforcement Officer	5,000							
81	429.321	Telephone	4,500		4,500					
82	429.326	Lubricants	2,000		2,000					
83	429.340	Printing and Advertising	2,000		2,000					

Wastewater Fund Proposed 2014 budget

ATTACHMENT NO. 1

	A	B	P	R	S	T	U	V	W	X
1	Code	DESCRIPTION	Budget		To Be Included					
2			2014		In LSA Fee	Notes from meeting with LSA 03/05/2014				
85	429.361	Electricity	150,000		150,000					
86	429.362	Gas	15,000		15,000					
87	429.364	Bar Screen Removal	1,000		1,000					
88	429.365	Biosolids Management	15,000		15,000					
89	429.366	Water	3,500		3,500					
90	429.367	Grit Removal	1,000		1,000					
91	429.368	Sewer Maintenance of lines	25,000							
92	429.369	Industrial Pre-treatment	2,500		2,500					
93	429.373	Building Maintenance	2,500		2,500					
94	429.374	Maintenance of Grounds	1,000		1,000					
95	429.384	Equipment Rental	2,700		2,700					
97	429.460	Education Training	3,000		3,000					
98	429.740	Minor Equipment Purchase Capital	0		0					
99	429.750	Safety Equipment	3,000		3,000					
100	429.751	Small Equipment	2,000		2,000					
106	429.999	Miscellaneous	2,000		2,000					
107		Collections and Treatment Total	853,418		731,783					
108										
109	471.700	Debt Principle	69,370		0	Payoff with Proceeds of Asset Purchase				
110		Subtotal	69,370		0					
111										
112	472.700	Debt Interest	15,595		0	Payoff with Proceeds of Asset Purchase				
113		DEBT EXPENSE TOTAL	15,595		0					
114										
115	487.100	Insurances	118,000		118,000					
116	487.200	Worker's Compensation Insurance	30,000		27,300					
117	487.300	U/C Insurance	3,073		3,073					
118	487.400	Pension	23,371		21,362					
120	487.600	Compensated Absences	0		0					
122		TOTAL EMPLOYEE BENEFITS	174,444		169,735					
123										
124	492.090	Transfer to Mun. Auth Capital Fund	700,147							
125		Subtotal	700,147							
126										
127		Bond Principal			0	Payoff with Proceeds of Asset Purchase				
128		Lease Payments			0					
129		Recurring Bond Fees			0	Payoff with Proceeds of Asset Purchase				
130										
131										
132		TOTAL EXPENSES	2,202,371		1,066,966					
135										
136		Expense per Month=			\$88,914	Say \$89,000				
137										

Attachment No. 2

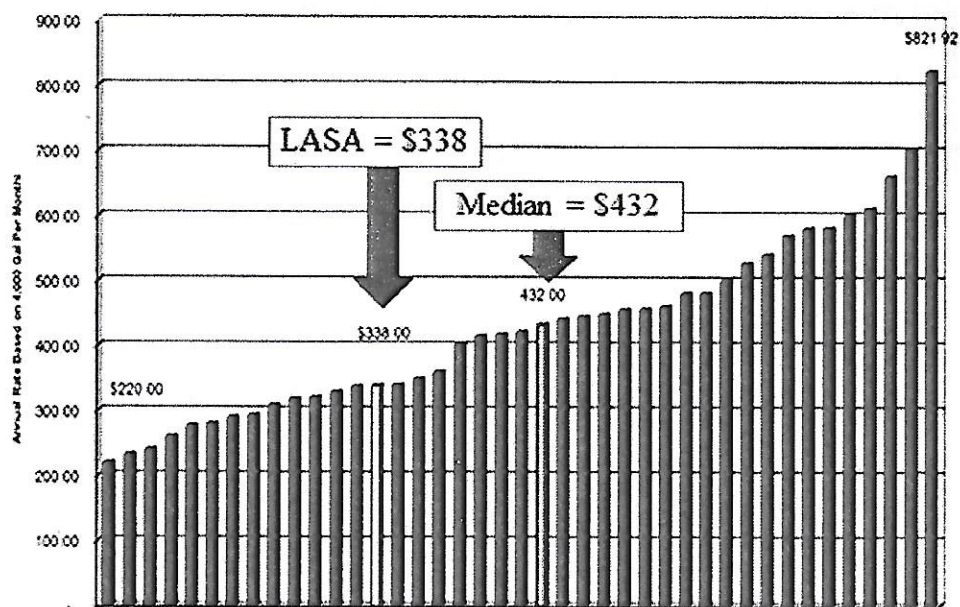
Schober, Michael A.

To: Michael Schober (schoberma@cdmsmith.com)
Subject: FW: Follow up to today's meeting

Mike,

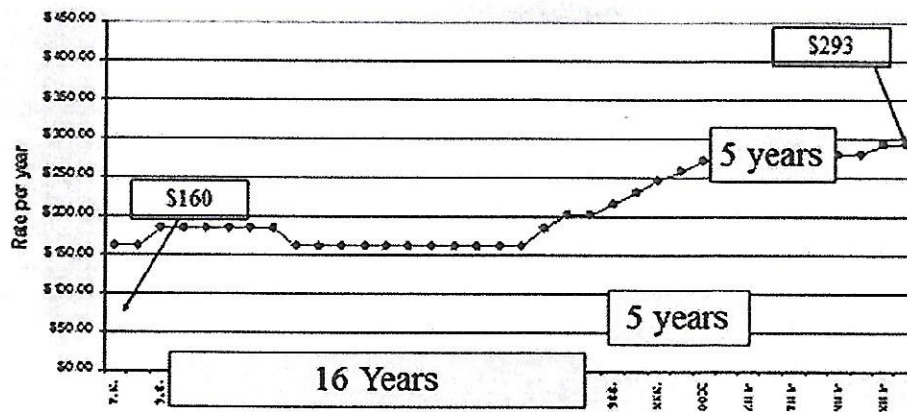
Here are the two slides you mentioned. The Rate Survey below was in the 2013 presentation, but we have not used the rate history slide since 2009, so it is not really up to date. If you need the rate history information updated, I can get that for you.

2011 RATE SURVEY - ANNUAL RATE BASED ON 4,000 GALLONS PER MONTH



Attachment No. 2

LASA Rates

**R. MICHAEL LEHMAN**

Financial Director

Lancaster Area Sewer Authority

130 Centerville Rd. Lancaster, PA 17603

717-299-4843 (Main Office)

717-344-5823 (Direct Dial)

717-277-1043 (Mobile)

717-344-5902 (Direct Dial Fax)

mlehman@lasa.org (Email)www.lasa.org (Website)

Mission - Quality Service at Reasonable Cost

Vision - Driving Decisions and Delivering Solutions