

Daniela Russell

From: GID - Moody's Investors Service [epi@moody.com]
Sent: Tuesday, September 22, 2009 4:11 PM
To: Daniela Russell
Subject: Seacoast Utility Authority, FL

MOODY'S ASSIGNS A2 RATING TO SEACOAST UTILITY AUTHORITY'S (FL) SALE OF \$78.1M WATER AND SEWER UTILITY SYSTEM REVENUE BONDS 2009 SERIES A & B

AFFIRMED A2 RATING ON \$45 MILLION IN OUTSTANDING PARITY DEBT

Seacoast Utility Authority, FL
Water/Sewer
Florida

Moody's Rating

Issue	Rating
Water and Sewer Utility System Revenue Bonds, Series 2009A	A2
Sale Amount	\$8,800,000
Expected Sale Date	09/29/09
Rating Description	Revenue
Water and Sewer Utility System Revenue Bonds, Series 2009B	A2
Sale Amount	\$69,300,000
Expected Sale Date	09/29/09
Rating Description	Revenue

NEW YORK, September 22, 2009 -- Moody's Investors Service has assigned an A2 rating to Seacoast Utility Authority's (FL) Water and Sewer Utility System Revenue Bonds Series 2009A (\$8.8 million) and B (\$69.3 million). Series B bonds will be issued as Build America Bonds. Concurrently, Moody's affirmed the A2 rating on the authority's outstanding \$45 million in parity debt. The bonds are secured by the net revenues of the system. The rating is based on satisfactory financial operations, an affluent customer base, ample capacity, elevated debt ratio and sound management team. The current issue will finance the Hood Road Membrane Conversion Project.

Adequate legal provisions include a 1.05 times rate covenant (excluding connection fees and guaranteed revenues) and 1.20 times (including connection fees and guaranteed revenues) or 1.1 times rate covenant (excluding connection fees and guaranteed revenues); a 1.05 times (excluding connection fees and guaranteed revenues) additional bonds test; and a reserve requirement equal to maximum annual debt service. About 26.6% (\$19.3 million) of utility debt is represented by two non-rated bank loans (Series 2005 and Series 2006) that are parity to Series 1989 and Series 2001 rated bonds.

AFFLUENT SERVICE AREA; SYSTEM HAS AMPLE CAPACITY

The authority provides water supply and wastewater treatment and disposal to an affluent service area in the unincorporated areas of Palm Beach County (G.O. rated Aaa), the incorporated areas of City of Palm Beach Gardens (G.O. rated Aa1), the Village of North Palm Beach and the towns of Lake Park and Juno Beach. The established water and sewer system, due to the combination of a mostly developed (84%)

service area and the severe housing market correction, experienced a significant slowdown in new meter installations from a peak of 1,441 annually in fiscal 2005 to a low of 128 in fiscal 2008- the lowest amount in at least the past eight years. The system serves approximately 47,152 water equivalent residential connections (ERC's) and 35,800 sewer ERC's, or a population of roughly about 100,000. The system is well-diversified, deriving approximately 78% of revenues from residential customers and with the top ten customers representing a minimal 5.8% of fiscal 2008 operating revenues. Facilities have reportedly been hardened against storms and have back-up generators to minimize service disruptions. Updated security measures have been implemented in accordance with a vulnerability assessment conducted at the end of 2003. Additionally, both systems are in good operating condition and are in compliance with federal and state regulations.

The authority derives its water from wells supplied by the Surficial Aquifer, with additional wells being constructed to the upper Floridan Aquifer (more brackish water requiring membrane treatment). Officials will replace the two older lime-softening treatment plants with a single membrane plant having the same (30.5 MGD) capacity by the end of 2012. The plant will have a nanofiltration train (26 MGD) that will continue to treat water from the Surficial Aquifer, and a low-pressure reverse osmosis train (4.5 MGD) to treat the more brackish Floridan Aquifer water that will be blended. The current water system can treat 30.5 MGD per day, with a fiscal 2008 average and peak daily usage of 14.2 MGD and 24.6 MGD, respectively. Officials anticipate water supply and treatment capacity to be adequate to build out. Unaccounted for water is a reportedly modest 5.4% in 2008. Officials anticipate compliance with expected DBP-Stage 2 regulations.

The sewer system can treat 12 MGD of wastewater daily, with a fiscal 2008 average and peak daily usage of 7.9 MGD and 10.1 MGD, respectively. The authority reports there are no issues related to total maximum daily loads (TMDL's). Effluent is reused (about 7 MGD to 8 MGD currently) or can also be deepwell injected (15 MGD capacity). Officials are looking to blend wastewater effluent with about 4 MGD of treated water by-product to supply about 12 MGD of reuse product. Sludge treatment levels are adequate with Class 1 landfill disposal. There are about 3,500 septic systems in the system, with mandatory tie-in required for non-residential customers only. Infiltration/inflow is reported to be a modest 7%.

WELL-MANAGED FINANCIAL OPERATIONS SUPPORTED BY SATISFACTORY DEBT SERVICE COVERAGE AND SOLID LIQUIDITY POSITION

Despite the authority's projected decline in debt service coverage due to the magnitude of the current offering, the authority's financial position is expected to remain sound given its solid liquidity position and strong management team. Net revenues in fiscal 2008 provide 2.1 times coverage (2.3 times with additionally-pledged guaranteed revenues and connection charges). A proposed 21.5% rate increase effective fiscal 2010 is intended to support upcoming debt issuance and equity contributions to the capital program. When including the proposed rate increase, debt service coverage from net revenues is still projected to decline to approximately 1.35 times in fiscal 2010 and increase to 1.49 times by fiscal 2014. Rates and charges are reportedly regionally competitive, with the monthly average residential bill estimated at \$50.03 (based on 6,000 gals. per month usage). Rates are structured for the base facility charge to cover 80% of fixed costs, lessening the impact of commodity usage on revenues.

At the end of fiscal 2008 the Authority had \$15.9 million in unrestricted cash and investments (about 306 days of cash-on-hand), which is down from the prior year at \$23.2 million (about 490 days of cash-on-hand). The authority's reduced yet solid liquidity position was a result of financing capital projects and cash funding its debt service reserve as a result of its surety provider being downgraded. Officials recently adopted a Cash Reserve Policy that states the Surplus Fund Account (unrestricted cash) will be maintained at a minimum of 90 days of budgeted operating expenses and debt service requirements. Officials

expect to maintain its unrestricted cash position at the current level (approximately \$15 million as of 8/31/2009). The authority also has \$10.6 million in its Capital Payment Account that could be used to finance capital projects and debt service related to the expansion of the system and \$5.6 million in its Renewal and Replacement Fund.

Fiscal 2008 operating and maintenance costs increased 10.3% (\$1.7 million) over the prior year due to increased fuel and chemical costs. Revenues were negatively impacted by water restrictions and the housing slump, which reduced connection fees and developer guaranteed revenues below anticipated amounts.

In response to revenue declines, officials implemented a \$5.40 surcharge and total revenues approximated the prior year. Fiscal 2009 year-end projections state that total revenues will increase by approximately 5% over the prior year, which will be offset with a 9% increases in operations and maintenance.

The rise in expenditures is due to chemical, fuel and the removal of lime sludge costs.

The authority has rather restrictive investment policies. There is currently \$6.9 million in the State Board of Administration's Local Government Investment Pool (SBA), which represents 17% of the investment portfolio.

Although \$780,000 of the total balance in the SBA is restricted, officials do not anticipate any cash flow problems related to these investments. The authority's unfunded liability related to GASB 45 (OPEB) is minimal at \$65,000.

MANAGEABLE DEBT LOAD

The debt ratio increases to 62.6% from 27.5% when incorporating the current issue. Total bond payout (including current issue) is below average at 40% paid within 10 years. The authority does not have any additional borrowing plans. System officials have entered into two similar interest rate swap agreements for a total notional amount of \$19.2 million related to the Series

2005 and Series 2006 bank loans with Bank of America, effective for the life of the loans (March 2019). Pursuant to the agreements, the authority pays 63.7% of LIBOR plus .49% and receives a variable rate based on the same index.

Simultaneously, the authority pays a fixed rate (3.93% for the Series 2005 and 3.32% for the Series 2006). Regular swap payments are on parity with bond payments and termination payments are subordinate. Except for an event of default, the authority has the only right to terminate the swap. There are no rating triggers and no collateral posting requirements. Based on a recent mark-to-market, if terminated, both swaps would require an authority payment of just over \$2 million.

KEY STATISTICS:

Number of customers: 47,152 water ERC's; 35,800 sewer ERC's

2008 Operating Ratio: 55.8%

2008 Debt Ratio: 27.5% (Pro forma 62.6%)

2008 Debt service coverage: 2.14 times (net revenue); 2.3 times (with gtd. rev. and connection charges)

Principal Payout (10 years): 40.8% (\$123.1 million rated bonds) and 49% (\$142.3 million of total debt outstanding)

1999 Per Capita Income as % State: 199.4%

1999 Median Family Income as % State: 163.4%

RATING METHODOLOGY USED AND LAST RATING ACTION TAKEN

The principal methodology used in rating Seacoast Utility Authority, FL was Moody's "Analytical Framework for Water and Sewer System Ratings", published in August 1999 and available on www.moody.com in the Rating Methodologies sub-directory under the Research & Ratings tab. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Rating Methodologies sub-directory on Moody's website.

The last rating action was on May 30, 2008, when the authority's rating was affirmed.

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