

May 29, 2014

Brad Ratliff, City Administrator
City of Peculiar, Missouri
250 S. Main
Peculiar, Missouri 64078

RE: Sewer Rate Forecast

Dear Brad,

We have completed our review and analysis of the attached Summary of Sewer Rate Scenarios covering the 6 fiscal year's ending 2014 through 2019. We were engaged to compile a forecast of rate changes necessary for certain scenarios which will be covered later in this memorandum. Our analysis is included below as well as attached to this summary.

Current Rate Structure for Sewer Customers

The City of Peculiar's rates for sewer treatment are broken down by the number of gallons of water sold to that particular customer. The charges are applied on the first 1,000 gallons then a per 1,000 gallon charge applied on each subsequent 1,000 gallons. As an example a typical household sewer charge in Peculiar is for 5,000 to 5,500 gallons. For our analysis we assumed an average household charge based on a charge for 5,000 gallons per month. Sewer rates charged during the last 5 fiscal years is summarized below:

Sewer Rates - Effective	9/30/2009		3/1/2010		9/30/2011		7/1/2012		7/1/2013	
	\$ per 1,000 gallons		\$ per 1,000 gallons		\$ per 1,000 gallons		\$ per 1,000 gallons		\$ per 1,000 gallons	
	First	Over	First	Over	First	Over	First	Over	First	Over
Within City Limits	\$12.00	\$6.35	\$15.00	\$6.85	\$15.00	\$6.85	\$15.00	\$6.85	\$15.00	\$6.85
Business-Govt.	n/a	n/a	\$20.00	\$8.35	\$20.00	\$8.35	\$20.00	\$8.35	\$20.00	\$8.35
Outside City limits	\$50.00	\$8.22	\$50.00	\$9.35	\$50.00	\$9.35	\$50.00	\$9.35	\$50.00	\$9.35
PWSD#2/10	n/a	n/a	\$15.00	\$6.85	\$15.00	\$6.85	\$15.00	\$6.85	\$15.00	\$6.85

As you can see by the table the City maintains four separate categories of rates for it's customers; 1) those within the city limits, 2) those registered as business or government entities, 3) those outside the city limits, 3) those contained with Public Water and Sewer District #'s 2 and 10 (PWSD#2/10).

Number of Active Meters	
City	1,424
Business/Government	87
Outside City Limits	20
PWSD#2/10	180
Total	1,711

In addition, the only previous change within this time frame was effective March 1, 2010 when customers within the city's limits rate on the first 1,000 gallons increased by 25% as well as those on subsequent usage by 7.87%. Business-Govt. and the PWSD#2/10 categories were added during that period as well. The rate charged on subsequent 1,000 gallon usage for customers outside the city limits increased by 13.75%. These rates are the equivalent of 5.00% and 1.57% increase, respectively and 2.75% increase for customers outside the city limits over 1,000 gallon usage.

Current Challenges

The city currently faces challenges with not only ordinary inflation of operating expenses but more so, inflation on projects as well as the constant capacity issues brought on by residential and commercial development within the city. While it was not within our scope to address the engineering of the capacity issues, we have been able to consolidate anticipated operating revenue and expense assumptions resulting in the capacity for the City's sewer system to afford the construction of capital expenses in the future to address anticipated capacity issues with its system.

Based on certain conservative assumptions we have prepared the attached summary of scenarios along with the staff recommendation going forward as it pertains to future estimated rates. The operating expenses are identical in each scenario. However, due to necessary rate structure changes in each scenario revenue as well as capital related costs differ. Each scenario began with the past two years (2012 and 2013) actual financial results and forecasts the current fiscal year through 2019.

The Sewer Rate Forecast in the attachment breaks down the rates necessary for each scenario, A1 & 2, B1 & 2 as well as the recommendation. In addition the schedule displays the impact on an average of 5,000 gallon sewer bill.

	Scenario			
	A1	A2	B1	B2
Deprec. Reserve	No	Yes	No	Yes
Capital Cost Included	No	No	Yes	Yes
Maintenance Cost	Underfunded	Underfunded	Underfunded	Underfunded
Yearly (6) Ave. Rate Incr.	1.38%	3.72%	7.97%	10.48%
Largest 1 Year Rate Incr.	\$0.75	\$1.97	\$3.00	\$4.50

Each scenario, A1 through B2, anticipates a \$0.50 mid-year increase in 2014 followed by the rates outlined within the summaries. In addition, where funded, reserves for depreciation are considered to be fully funded. Also, where applicable, funding is set aside for \$3 million in bond issuances as well as \$1 million in cash funded capital improvements from 2015 through 2019.

Scenario A1

Scenario A1 provides a starting point for our analysis. The scenario provides for neither a depreciation reserve nor a capital improvement budget. With that scenario alone the rates beginning October 1, 2014 would need to increase by 4.92% to account for principal and interest costs already committed. Both 2014 and 2015 anticipate rate increases leaving a 6 year annual rate average of 1%.

Scenario A2

Scenario A2 is a minor alteration of scenario 1 in that it adds a depreciation reserve on all assets to the rate structure. This reserve allows the City to set aside budget annually for eventual replacement of current assets. Within this scenario the first year rates would increase by 12.71% leaving a 6 year average rate increase of 4%.

Scenario B1

Scenario B1 provides funding for anticipated capacity issues by budgeting \$3.0 million in bonds as well as funding \$1million in cash funded capital needs over the 5 year window. It does not provide for a reserve for depreciation of current infrastructure assets. Within this scenario the first year rates would increase by 19.35% leaving a 6 year average rate increase of 8%. This estimates a need for additional rate increases in 2016, 2018 and 2019.

Scenario B2

Scenario B2 provides funding of a reserve for all assets within the sewer system along with the addition of capital equivalent to scenario B2 (\$3.0 million in bonds as well as funding \$1million in cash funded capital needs over the 5 year window). Within this scenario the first year rates would increase by 29.67% leaving a 6 year average rate increase of 10%. This estimates a need for additional rate increases in 2017, 2018 and 2019.

Staff feels that each of the above scenarios are relatively impractical in that they do not provide for responsible funding of current infrastructure reserves or anticipate a rate increases that are extremely volatile and unpredictable for system customers. In addition, two of the scenarios ignore anticipated growth entirely.

Recommended Approach to System Rates

Our goal in assembling a recommended scenario was a rate structure that would be:

- Predictable for our customers,
- Able to address strategic investment in the future,
- Maintain investments already made in capital assets.

A predictable rate structure would be one where our customers know future estimates of rates. Within the recommended scenario rates are estimated to increase by \$0.55 each year beginning October 1, 2014. Rate increases within each of the previously mentioned scenario's anticipate a rate increase mid year 2014 as well as, in some circumstances large, increases at October 1, 2014.

The recommended rate increase would be providing \$0.45 for operating and capital costs while approximately \$0.10 of the rate would be setting aside money to fund a depreciation reserve beginning in 2016. The \$0.10 set aside for reserve is not anticipated to be adequate to fully fund depreciation on all assets for the city.

This scenario funds the full \$3 million in bond issuance and \$1 million for cash funded capital improvements over the period between 2015 through 2019 giving the city the ability to react proactively toward strategic investment as well as invest in current capital assets.

The table below compares the staff recommendation with the scenarios previously discussed.

	Recommended	Scenario			
		A1	A2	B1	B2
Deprec. Reserve	Yes	No	Yes	No	Yes
Capital Cost Included	Yes	No	No	Yes	Yes
Maintenance Cost	Funded	Underfunded	Underfunded	Underfunded	Underfunded
Yearly (6) Ave Rate Incr.	4.96%	1.38%	3.72%	7.97%	10.48%
Largest 1 Year Rate Incr.	\$0.55	\$0.75	\$1.97	\$3.00	\$4.50

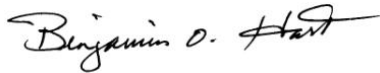
Conclusion

As with any forecast certain environmental elements exist that remain unpredictable. Utility funds are typically prone to weather conditions as well as growth in population, commercial business and inflation. None of these items can be entirely certain. However, based on relatively conservative assumptions in population and inflationary growth staff feels like the forecast that has been developed provides a substantial road map to future development.

I anticipate that staff will be available should the Board of Alderman have questions.

Respectfully,

Allen, Gibbs & Houlik, L.C.



Benjamin O. Hart
Vice President

City of Peculiar, Missouri
 Sewer Rate Forecast
 Summary Rates

	Currently	(4months)					
		2014	2015	2016	2017	2018	2019
A1 - No CIP, No Depreciation <i>Not practical</i>		\$0.50	\$0.75	\$0.00	\$0.00	\$0.00	\$0.00
City-Sewer Bill for 5,000 gallons	42.40	43.23	46.98	46.98	46.98	46.98	46.98
Bus./Govt-Sewer Bill for 5,000 gallons	53.40	54.23	57.98	57.98	57.98	57.98	57.98
Outside City Limits Sewer Bill for 5,000 gallons	87.40	88.23	91.98	91.98	91.98	91.98	91.98
PWSD#2/10 Sewer Bill for 5,000 gallons	42.40	43.23	46.98	46.98	46.98	46.98	46.98
A2 - No CIP, Full Depreciation <i>Not practical</i>		\$0.50	\$1.97	\$0.00	\$0.00	\$0.00	\$0.00
City-Sewer Bill for 5,000 gallons	42.40	43.23	53.08	53.08	53.08	53.08	53.08
Bus./Govt-Sewer Bill for 5,000 gallons	53.40	54.23	64.08	64.08	64.08	64.08	64.08
Outside City Limits Sewer Bill for 5,000 gallons	87.40	88.23	98.08	98.08	98.08	98.08	98.08
PWSD#2/10 Sewer Bill for 5,000 gallons	42.40	43.23	53.08	53.08	53.08	53.08	53.08
B1 - Full CIP, No Depreciation <i>Rates not practical</i>		\$0.50	\$3.00	\$0.50	\$0.00	\$0.65	\$0.65
City-Sewer Bill for 5,000 gallons	42.40	43.23	58.23	60.73	60.73	63.98	67.23
Bus./Govt-Sewer Bill for 5,000 gallons	53.40	54.23	69.23	71.73	71.73	74.98	78.23
Outside City Limits Sewer Bill for 5,000 gallons	87.40	88.23	103.23	105.73	105.73	108.98	112.23
PWSD#2/10 Sewer Bill for 5,000 gallons	42.40	43.23	58.23	60.73	60.73	63.98	67.23
B2 - Full CIP, Full Depreciation <i>Rates not practical</i>		\$0.50	\$4.50	\$0.00	\$0.50	\$0.80	\$0.50
City-Sewer Bill for 5,000 gallons	42.40	43.23	58.23	60.73	60.73	63.98	67.23
Bus./Govt-Sewer Bill for 5,000 gallons	53.40	54.23	69.23	71.73	71.73	74.98	78.23
Outside City Limits Sewer Bill for 5,000 gallons	87.40	88.23	103.23	105.73	105.73	108.98	112.23
PWSD#2/10 Sewer Bill for 5,000 gallons	42.40	43.23	58.23	60.73	60.73	63.98	67.23
A - Staff Recommendation		\$0.00	\$0.55	\$0.55	\$0.55	\$0.55	\$0.55
City-Sewer Bill for 5,000 gallons	42.40	42.40	45.15	47.90	50.65	53.40	56.15
Bus./Govt-Sewer Bill for 5,000 gallons	53.40	53.40	56.15	58.90	61.65	64.40	67.15
Outside City Limits Sewer Bill for 5,000 gallons	87.40	87.40	90.15	92.90	95.65	98.40	101.15
PWSD#2/10 Sewer Bill for 5,000 gallons	42.40	42.40	45.15	47.90	50.65	53.40	56.15