

January 12, 2009

26 Western Water And Sewer Issuers Are Upgraded On Revised Criteria

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Issuer Review

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Standard & Poor's Ratings Services has raised its ratings on 26 municipal waterworks, sanitary sewer, and/or drainage utility revenue bonds (see table 1). The upgrades are primarily based on our recent criteria revision (see the article, "Standard & Poor's Revises Criteria For Rating Water, Sewer, And Drainage Utility Revenue Bonds," dated Sept. 15, 2008, on RatingsDirect). In all cases, the rating outlook is stable.

In our opinion, western region utilities included in this review tend to demonstrate strong financial metrics and management practices that mitigate several regionally specific challenges. Western states face a diminishing water supply, coupled with a rising population. Drought in the Colorado River Basin and court-ordered restrictions on water deliveries from the Sacramento-San Joaquin River Delta in California to protect fish and wildlife have necessitated alternative water solutions; the construction of desalination and reclaimed water plants and water banking programs are a few of the alternatives that have gained popularity. For example, the California Department of Water Resources created a drought water bank for 2009 to facilitate the transfer of water from local water districts willing to sell excess supply to those with short supply. Despite these endeavors, we believe conservation efforts will persist and mandatory water restrictions might still be needed. We, however, believe that a well-planned rate structure can mitigate cyclical revenue trends resulting from reduced water usage. In addition, we believe that the funding of capital programs for aging infrastructures in mature areas and new infrastructure for young growing communities will require proactive long-term planning.

In our opinion, stalled housing construction has been both a blessing and a burden for some systems. Slowed new construction has provided some capital expenditure relief for growth-pressured systems. It has also resulted in declining impact fee revenues.

We believe the utilities included in this review, in general, have either sufficient operating revenues to generate adequate debt service coverage and had been using impact fees to fund capital projects that are now on hold because of reduced growth demand or responded with budget adjustments or increased user rates. Notwithstanding these challenges, these issuers, in our view, have exhibited stable credit profiles and, in general, demonstrate one or more of the following credit characteristics:

- Strong financial metrics, including debt service coverage and cash reserves;
- Good economic fundamentals, such that we expect their respective utility system(s) to be able to handle such pressures as housing market vulnerabilities, employment softness, or cost-of-service inflation; and
- Solid management, which includes a demonstrated willingness to adjust rates, long-term planning to fund key service components like water supply or regulatory-driven capital expenditures, and the ability to serve the needs of a growing community.

It should be noted that without exception, municipally owned water, sewer, and drainage systems in the United States are monopolistic service providers that enjoy local rate autonomy in the provision of a relatively price inelastic service. These are characteristics that we believe help support credit quality. Only a few states require local rate increases by a state regulator such as a public service commission.

Although we have historically incorporated factors such as the service area economy and financial performance as components of our analysis, we now believe the sector's demonstrated stability in operations and financial

performance, as well as successful management of the requirements of the federal Safe Drinking Water Act of 1974 and Clean Water Act of 1972, and all of their respective amendments and state regulations, supports these rating actions.

Our criteria revision reflects our view that for general obligation ratings, a small and/or rural issuer does not necessarily have what we consider weaker credit quality than a larger or more-urban issuer. Although we assess these factors in our credit analysis for some revenue bond ratings, we believe many municipal systems still exhibit, in our view, strong and stable credit quality despite size or location constraints. While we believe that smaller or rural utility systems may not necessarily benefit from the economies of scale that can lead to more-efficient operations or lower costs, in our view, they can still have affordable rates, even in places with less-than-favorable household income and wealth levels.

As a result of our reexamination of these credit factors, we reviewed these issuers and raised our ratings. We expect to publish additional ratings adjustments on water and sewer ratings based on our criteria revisions. All of the systems in table 1 are water and sewer service providers unless noted otherwise.

Issuer Review

Table 1

Rating Changes				
Issuer	New Rating	Previous Rating	Analyst	Comment
East Cherry Creek Wtr & San Dist, CO	A+	A	Timothy Barrett	The district continues to demonstrate what we consider good financial performance, including strong coverage of debt service and strong liquidity. This is despite a slowdown in growth and related water tap fees, which accounted for roughly 15% of total water system revenues in fiscal 2007. Within the next year, we understand that the district will likely issue additional bonds for a water treatment plant that could bring coverage close to 1.25x debt service, but we expect liquidity to remain strong at more than a year's cash on hand.
Marin Municipal Water District, CA	AA+	AA	Timothy Barrett	The district provides water to residents of the southern and central portion of Marin County, located in the North San Francisco Bay Area. The district currently serves a population of approximately 183,000 through 61,054 service connections in the cities of Belvedere, Corte Madera, Fairfax, Larkspur, Mill Valley, Ross, Sausalito, San Anselmo, San Rafael, and Tiburon, as well as a large unincorporated area. We understand that the district is currently reviewing options to expand its water supply. This could be achieved through a new 5 mgd facility or through system enhancements. Despite the potential need for additional debt to fund increased water supply, we expect financial performance to remain strong, with management annually adjusting rates and targeting at least six months' operations in cash on hand.
Montrose, CO	A+	BBB+	Timothy Barrett	The utility system serves a population of 16,070 in western Colorado. Montrose provides water and sewer service to 7,109 and 7,198 customers, respectively. We understand that water and wastewater supply and capacity are sufficient for the near future, with the utility projecting supply to meet demand for a population of 40,000 and treatment capacity to be sufficient through 2020. Liquidity and coverage remain in our view very strong, despite the system's use of operations to fund capital needs. We understand that the city does not expect to issue additional debt.
Santa Ana Financing Authority, CA	AA	AA-	Timothy Barrett	Located about 33 miles southeast of Los Angeles, Santa Ana, with a population estimate of 364,000, is both Orange County's largest city and seat. The water system provides potable water to more than 49,000 customers. The customer base is very diverse and built out. We consider the system's financial performance to be very strong, with strong liquidity and coverage of debt service.
Helix Wtr Dist, CA	AA	A+	Ian Carroll	The water district serves eastern San Diego County with retail water services and benefits from a wealthy economic base. Financial performance has been in our view strong, with 3.25x coverage of debt service and 166 days' cash on hand. Operationally, the system relies on San Diego County Water Authority for about 80% of its water supply.

Table 1

Rating Changes (cont.)				
Hillsborough, CA	AAA	AA	Ian Carroll	Hillsborough's combined water and sewer utility maintained what we consider its strong financial performance in 2008 with 2.4x coverage and 678 days' cash on hand; the underlying economy is one of the wealthiest in the U.S., with incomes at 414% of the U.S. median. We understand that there is no plan to issue any additional debt.
Imperial Irrigation District, CA	AA-	A+	Ian Carroll	The district has maintained what we consider a good debt service coverage of more than 2x, in part due to rising sales of water to San Diego County Water Authority. In our view, cash was also strong at 395 days in 2007. The system's service area is in the imperial valley, an agricultural area east of San Diego and on the U.S.-Mexico border, but sales to the water authority mitigate the local economy's agricultural concentration.
Municipality of Anchorage (Sewer), AK	AA	A+	Ian Carroll	The city's wastewater enterprise had what we consider very strong coverage of annual debt service of more than 5x in 2007, based on audited financial statements and 215 days' cash on hand, following rate increases in the past few years. We expect finances to remain strong as long as the required treatment standard is not increased, which we believe would add considerable capital pressures.
Municipality of Anchorage (Water), AK	AA	AA-	Ian Carroll	We understand that the city's water utility has virtually unlimited supply by virtue of mountain snowfall. In our view, the enterprise's finances have been strong, with 1.8x coverage and 242 days' cash on hand. Capital needs, moreover, are what we consider minimal, which should allow for stable financial performance without the need for additional rate increases.
Orange County Water Dist, CA	AAA	AA+	Ian Carroll	The water district maintained what we consider very strong coverage, more than 2x in each of the past several years, as well as exceptional cash liquidity of 590 days, in 2007. The district's economy, moreover, does not present a challenge because the district participates in the Teeter plan. Income levels are 33% above the U.S. median. The district is responsible for the long-term viability of the groundwater basin and levies an assessment on its customers who pump from the ground.
Brea Public Finance Authority, CA	A+	A	Le T. Quach	The city of Brea's water rates are adjusted annually based on inflation, which has supported what we consider good coverage of annual debt service. The city projects coverage for fiscal 2008 to be a strong 1.6x. The city has historically funded its water capital improvements with cash, but expects to issue additional parity bonds this spring. Brea receives its water supply from Southern California Metropolitan Water District and California Domestic Water Co., a private company.
Oro Loma Sanitary District, CA	AA+	AA-	Le T. Quach	This wastewater treatment system benefits from what we consider a strong collections process, which allows it to collect a majority of its fees through annual property tax billings. In our view, the system has maintained very strong financial performance, with coverage of at least 5x annual debt service from fiscals 2005-2007. Based on audited results for fiscal 2008, this Bay Area district will end with a \$28.6 million unreserved cash balance, equal to what we consider a strong 817 days' expenditures. The system projects that its capital needs will be funded by ongoing revenues.
Crescenta Vy Wtr Dist, CA	A+	A	Li Yang	Recent rate increases have contributed to what we consider the district's strong 4.3x coverage in fiscal 2008 for its outstanding water revenue debt. The first principal payments for the 2007 certificates of participation begin in fiscal 2009, and we expect coverage to be 1.5x excluding connection fees. The district currently maintains a five-year capital plan totaling roughly \$9.9 million. We understand that the district is considering issuing additional debt.
East Vy Wtr Dist, CA	AA-	A	Li Yang	The district maintains what we consider a sizable capital plan, with the majority being used for constructing new treatment plants in order to meet federal water quality standards. The most recent rate increase of 12.5% became effective in fiscal 2009. We understand that future rate are increases possible, which would enable the district to maintain what we consider good debt service coverage levels.
Goleta Wtr Dist, CA	A+	A-	Li Yang	In our opinion, the district's financial performance has improved significantly in recent years due to increased water demand. In addition, water rates were raised in fiscal 2008, which has led to what we consider strong debt service coverage of 1.53x without connection fees. We expect coverage to remain at this level as the district does not plan to issue additional debt. Currently, the district maintains a five-year capital plan of approximately \$5 million.
Lake Arrowhead Comnty Svcs Dist (water), CA	A+	A-	Matt Reining	In our opinion, the utility has shown good financial performance, while serving a mostly residential, resort community, with strong liquidity and good coverage. After a number of years of ongoing legal action regarding the district's use of water from Lake Arrowhead, the state issued a final order in 2006 allowing the district to use 1,566 acre feet per year, while also pointing to the need for outside sources given that the lake allowance supplies only 63% of recent average years' water usage. The district has met this need in the intermediate future with a 10-year contract with the Crestline-Lake Arrowhead Water Agency. Through rate increases, the district is generating revenue to cover the increase in water supply costs.

Table 1

Rating Changes (cont.)				
Los Angeles Cnty San Dist #14 (Lancaster), CA	A+	A-	Matt Reining	The district primarily serves the city of Lancaster, which has seen significant residential growth in recent years. Because of this growth, the district has a \$295 million five-year capital improvement plan that includes more routine sewer and line improvements as well as a major plant expansion and treated water storage facility. The series 2005 bonds were issued to meet these capital financing needs; the district has used and we understand will use additional state loans. Based on audited 2007 results, the district had in our view a solid 1.2x debt service coverage with a strong 1.8x coverage including connection and developer fees. Although the district projects that connection fees will fall, given the local real estate slowdown, management believes that flexibility is built into its capital improvement plan and that it can adjust expenditures through modular plant expansion and section line construction.
Los Angeles Cnty San Dists Fingc Auth, CA	AA+	AA	Matt Reining	The sanitation districts serve a large and diverse customer base of approximately 5.2 million people, or roughly all of the non-City of Los Angeles portions of Los Angeles County. Organized as a partnership among 24 individual districts (each with individual debt and tax bases), the overall district functions as a single unified operating entity with a single management structure. The overall district provides main-line conveyance, treatment, and disposal of sewage, with local collections done by individual, local agencies. For residential usage, customers pay a fixed annual service charge as well as a modest portion of property tax. These service charges ranged from \$78-\$308 in fiscal 2008 and adopted service charge increases averaged 11% for fiscal 2009. Debt service coverage by each of the member districts allows for a 20% increase in revenues as needed for the step-up charges. Coverage by what we consider the stronger districts (taking into account the step-up) ranged from a good 1.4x to a very strong 8.7x in fiscal 2007, with strong cash levels ranging from 365 days to more than 4,000 days.
Arapahoe Cnty Water & Wastewater Authority, CA	AA-	A+	Misty Newland	The authority provides service to portions of Arapahoe and Douglas counties. In our view, proximity to Denver has driven expansion in these areas. Coverage and cash balances have been historically what we consider strong. Estimated coverage for fiscal 2008 is lower but still in our view strong at 3.4x due to a decline in tap fees and added debt service for series 2007 revenue bonds. We understand that future capital projects will include expansion of its water treatment plant and water acquisition, a portion of which would be funded with additional debt. The authority's additional bonds coverage test is 1.25x maximum annual debt service.
Olivenhain Mun Wtr Dist, CA	AA	AA-	Misty Newland	The district serves an affluent area in San Diego County, including part of the city of Encinitas. Financial management includes a 10-year operating and capital spending forecast. In addition, the district is proposing a rate structure that includes step-ups during drought conditions to offset revenue losses due to decreased consumption. The district has reserve targets for the operating, capital, and rate stabilization funds. The district is about 74% built-out and we expect will require additional capacity in the future, which we understand it plans to fund with system revenues and debt financing.
Manteca, CA	A+	A-	Shannon Groff	The city is located in the northern portion of the San Joaquin Valley between the cities of Stockton and Modesto and approximately 75 miles east of San Francisco. The city is located in the agriculturally rich San Joaquin Valley between Interstate 5 and State Highway 99. After determining that it was over-drafting its ground water resources, the city entered into an agreement with South San Joaquin Irrigation District for the provision of surface water. The city's current usage is 44% surface water and 56% ground water and future usage is projected at 53% surface water and 47% ground water. A recent rate study led the city to adopt rate increases of 5% each year from 2009-2013; the adopted plan will decrease fixed rates and increase water use charges.
Susanville, CA	A	BBB-	Lisa Schroeer	The moderately small system serves roughly 18,600 people in the seat of Lassen County. In our view, finances are good, and coverage has not fallen below the 1.25x target. We believe cash is very strong, with \$2.2 million in fiscal 2007, and management has indicated that it intends to keep cash at this level. Finances should stay at what we consider good given the system's relatively small capital needs and recent rate increases. Management intends a recent rate increase to fund the system's capital needs, with an estimated revenue of \$400,000 annually.
Los Angeles Cnty San Dist #20, CA	A	A-	Lisa Schroeer	The system serves the city of Palmdale and surrounding areas with roughly 110,000 people. In 2007, the district issued bonds to address environmental compliance issues. Management expects the project to be completed on time. Coverage was more than 2.0x with connection fee revenue and what we consider a still good 1.2x without it in 2007. Management indicated that approved rate increases are anticipated to be sufficient to cover any decline in connection fee revenue and expects 2008 coverage to be similarly strong. The district does have about \$200 million in additional capital needs through 2014. Management anticipates using state loans in the upcoming year to address some of these needs and that it will meet all bond covenants. In our view, the district's strong cash position, with cash held in restricted funds but available for operations, mitigates some concerns over additional capital needs.

Table 1

Rating Changes (cont.)				
Clovis, CA	A+	A-	Lisa Schroeer	The system serves a population of roughly 90,000 in the city of Clovis. Previously a rapidly growing area, the city has had to curb its expectation for one-time revenues, but lower construction costs have provided additional financial flexibility not previously anticipated. Coverage is more than 1x without growth-related revenues, and management expects cash to stay strong. The city's capital plans are, in our view, minimal, but management noted that the city may need to contribute to projects necessary for the Fresno system, which the city currently uses for its treatment. Management indicated a willingness to raise rates to ensure a target level of coverage of 1.2x. Additionally, the city has a rate stabilization fund that can stabilize revenues as growth-related revenues drop off. The new rating reflects our expectation that the city will take into account the decrease in growth-related revenues and adjust its finances.
Weber Basin Wtr Conservancy Dist, UT	AA	AA-	Lisa Schroeer	This wholesale and retail utility, covering Weber and Davis counties, has customer cities that, in our opinion, are of strong credit quality. In addition, the district benefits from property tax revenues and a strong water supply. The district provides water to what we consider a strong economic area that ties into the broader Salt Lake economy.
Valley Sanitary District, CA	A+	A-	Lisa Schroeer	The district serves the city of Indio and surrounding areas. Coverage is more than 4x, even when excluding one-time development-generated revenue. User rates are rising to address additional costs and should help as connection fee revenue decreases. In our view, the district holds strong cash that it may partially use to address some treatment plan needs, but it has a policy to maintain at least six months' operations in cash on hand, which it is well above. Additional capital projects are related to growth, and we understand that the district is evaluating whether or not it is a prudent time, financially, to move forward. These are not currently need-based projects, which gives the district flexibility.

mgd--Million gallons per day. MSA--Metropolitan statistical area. MHEBI--Median household effective buying income.

Table 2

Selected Credit Ratios				
Issuer	DSC (x)	Days' Cash	MHEBI (% of U.S.)	Debt to Plant (%)
East Cherry Creek Valley Water and Sanitation District, CO	2.4	537	104	33
Marin Municipal Water District, CA	2.0	238	156	19
Montrose, CO	4.3	876	83	21
Santa Ana Financing Authority, CA	3.9	187	101	30
Helix Wtr Dist, CA	3.3	166	114	11
Hillsborough, CA	2.4	678	414	85
Imperial Irrigation District, CA	2.1	395	75	39
Municipality of Anchorage (Sewer), AK	5.4	215	132	24
Municipality of Anchorage (Water), AK	1.8	242	132	35
Orange County Water Dist, CA	2.3	590	130	73
Brea Public Finance Authority, CA	1.7	212	132	30
Oro Loma Sanitary District, CA	6.4	935	128	8
Crescenta Vy Wtr Dist, CA	4.3	312	133	23
East Vy Wtr Dist, CA	1.7	339	97	24
Goleta Wtr Dist, CA	2.0	112	139	53
Lake Arrowhead Comnty Svcs Dist (water), CA	1.8	397	146	28
Los Angeles Cnty San Dist #14 (Lancaster), CA	1.2	2,493	96	134
Los Angeles Cnty San Dists Fincg Auth, CA	1.4 to 8.7	365 to 4,000	101	38
Arapahoe Cnty Water & Wastewater Authority, CO	7.9	799	127	69
Olivenhain Mun Wtr Dist, CA	4.0	399	145	20
Manteca, CA	5.46	1,977	109	71
Susanville, CA	1.3	289	85	123

Table 2

Selected Credit Ratios (cont.)				
Los Angeles Cnty San Dist #20, CA	1.2	833	101	303
Clovis, CA	2.2	1,000	100	154
Weber Basin Wtr Conservancy Dist, UT	3.2	696	122/104	31
Valley Sanitary District, CA	6.5	2,120	90	20

MHEBI--Median household effective buying income. DSC--Debt service coverage.

Table 3

Contact Information			
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