

Option 1: Retention of Ownership/ Project Funded by USDA Federal Stimulus Funds

Members' Questions & Answers

Retention of ownership means that the HMC water rights, assets and all responsibilities remain with the current owner/members, under the management of the Board of Directors.

Through September 2010, the USDA Community Facilities loan program has funds available from the American Recovery and Reinvestment Act ("Stimulus") for the purposes of improving or constructing water systems. HMC had previously considered USDA funds as a source to finance water system replacement in 2007. The current loan terms are an improvement over the earlier ones.

At its December 2009 meeting, the Board of Directors authorized the Island Manager to gather information necessary to apply. The Herron Island Water System qualifies for the USDA funds, and a preapplication has been submitted so that any necessary information can be generated for USDA in a timely manner.

The following are questions and answers submitted by members of the WPC and membership at large. Questions and answers have been reviewed and approved by USDA for accuracy.

Tell Us about the Loan?

1. To what government agency are we applying?

US Department of Agriculture, Rural Development

2. What are the terms of the loan?

A maximum rate of 4.25% over the 40 year term of the loan; no prepayment penalty. This means that the loan can be paid off early or extra funds paid at any time to reduce the principal balance. Interest accrues once the interim financing is closed and loan documents signed.

For comparison purposes, we sought a quote from KeyBank regarding commercial lending availability. KeyBank is the Island's bank. The commercial lending department estimated that they would be able to provide a loan of up to \$3,000,000 for a 20-year term, at 6.35% interest. The loan would need to be renewed every five years.

3. Is the loan with the HMC or individual property owners? It is with HMC.

4. What, if any, collateral is required?

USDA will take a lien against some HMC properties. Their goal, however, in the unlikely event of default, would be to find some method by which we can repay the loan. They are not interested in owning land on Herron Island. Their last ditch effort would be to find someone to take over the system and assume the debt.

5. Will USDA fund our startup and application costs?

Yes. Certain costs associated with filing a complete application can be folded into the loan amount, such as the engineering fees required to give us a better budget estimate, environmental evaluation assistance, rate studies, and so on. To date, no HMC funds have been expended.

6. What funds are available at the beginning of the project?

HMC maintains water system reserves, currently at about \$52,000. Also, USDA can assist us in obtaining interim financing with a local bank, most likely KeyBank, which is the island's bank. The interim loan and interest would be repaid on final USDA loan approval, and folded into the USDA loan.

7. What would be the method of loan payback?

That is yet to be decided by the Board and/or members. Methods include collection via assessment, or folding capital costs into a monthly water bill. Current State law requires water metering by January 2017. USDA/RD would take an interest in real property owned by HMC, but a promissory note and assignment of income from the water revenues is really what will repay the loan. The estimated amount per assessable unit, per month, would be \$22-\$30.

8. What happens if individuals default?

If individuals default on obligations to HMC, delinquency procedures apply.

9. Does HMC Management have to have 10% (or any amount) of the loan value in reserve to qualify?

No. USDA/RD wants us to have a reserve of 25% of our annual O&M costs as reflected in our 2010 budget. Note that this is not a reserve of the capital construction budget. Our 2009-2010 budget for Water Operations & Maintenance is \$25,658 (excluding the amount budgeted for the water reserve fund). Current Water Reserves total \$51,922.74, as of December 31, 2009. RD would also like the system to have a 10% of the loan debt per year set aside for capital improvements.

10. When do we begin to pay back the USDA loan?

HMC's repayment begins six months after completion of the project. Member obligations would be repaid on a schedule to be determined after review by the Board and membership.

11. What specific project requirements are tied to this government loan? The specifics are tied to the water system, all persons should be able to hook on (no discrimination).

12. Will the construction project cost more with government financing?

No, it should not. Other large utilities also pay prevailing wages to construction workers, and right now the bidding climate is in our favor. As a smaller agency, we probably have less overhead expense than a larger utility would need to recapture.

13. What would the project timeline be with this loan?

40 years, with no prepayment penalty.

14. Are funds available at the start of the project? Or will we require some type of bridge loan?

Interim financing will be arranged with a local bank, with USDA assistance.

15. Who is our contact? Bruce Whittle, USDA Washington

What are the Schedules and Deadlines?

1. What is the final date we need to submit the application by?

No later than September 30, 2010. Best is AS SOON AS POSSIBLE, because some time is required for final review in the other Washington (30-45 days). USDA/RD has stimulus funds but they will expire 9/30/2010 and so *as soon as possible* for obligating funds. After obligation we would go to bid, then award contract, then set up a time to start and finish and have the contractor start work.

2. Is there an advantage to applying early?

Yes, to get funds committed.

3. How long does the application take to complete?

The preliminary application is complete. We are now in the review phase. We will need preliminary design sometime during the application, final design can be done after obligation of funds. Final design is needed for contractors to bid.

4. What should our deadline be for starting the application process? Today. (Preliminary application was submitted January 28, 2010.)

5. After submitting our application, how long before we are notified of the result?

USDA works with us throughout the approval process to refine our application and answer any areas needing clarification.

6. If our application is approved, how long before funds are available?

Funds are available; Congress approved the American Recovery and Reinvestment Act in early 2009. These funds must be allocated by September 30, 2010.

What Does It Cost to Apply?

1. What is the application fee?

There is no fee for application.

2. What will it cost to pay a consultant to complete the application and submit?

We can complete most of the application, with some assistance from an engineering firm. USDA will advise us when we may need assistance from an engineering firm to support our application or refine construction estimates.

3. Are there any additional costs associated with this process?

Not until we begin the detailed design process with our selected water engineering firm.

4. Are any of these expenses refundable if we are rejected or withdraw? No.

Here Are Some Other Considerations...

1. If we require a consultant to complete our application, what qualifications should they have? Qualified engineering firm, with background in water project engineering.

2. How many consultants should we consider? Three to five.

3. What criteria will be used to make this selection? Scope, References, Qualifications and Cost.

4. Who will make the decision? (The Board? The Island Manager? The WPC?) The Board.

5. How much money should be spent before a community vote is appropriate?

Enough to secure good, objective information for the members.

6. Does the timing allow for an "Advisory vote" on direction before spending money? Yes.

7. Will this loan have any effect on Island insurance rates, bonding or ability to borrow in the future?

Yes. Should positively affect fire insurance rates for future; may impact ability to borrow money from other than government sources for duration of loan. HMC has no other plans to borrow, and is building reserves annually for major projects, such as the dolphin improvements.

Please contact the Island Manager at hmcmanager@herronisland.org if you have any additional questions or concerns.