

# Hilton Head No.1 Public Service District Comprehensive Annual Financial Report



Fiscal Year Ending  
June 30, 2010

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# INTRODUCTION

## Board of Commissioners

The Hilton Head No.1 Public Service District (the “PSD” or the “District”) is governed by a seven-member Board of Commissioners (the “Commission”). Commissioners are elected to four-year terms by registered voters during general elections. Commissioners represent four different sub districts within the PSD service area.



**W. Robert “Bob” Manne, Chairman, District 4**  
Current Term: 2008-2012



**Robert “Bob” Gentzler, Vice Chairman, District 3**  
Chairman, Planning & Operations Committee  
Current Term: 2010-2014



**Gary Kratz, Treasurer, District 4**  
Current Term: 2008-2012



**John Geisler, Secretary, District 3**  
Chairman, Finance Committee  
Current Term: 2008-2012



**Jack Burke, District 2**  
Current Term: 2008-2012



## Board of Commissioners (continued)



**Frank Drehwing, District 4**

Chairman, Long-Range Water Supply Committee

Current Term: 2010-2014



**Dorothy "Dot" Law, District 1**

Chairperson, Community & Personnel Relations Committee

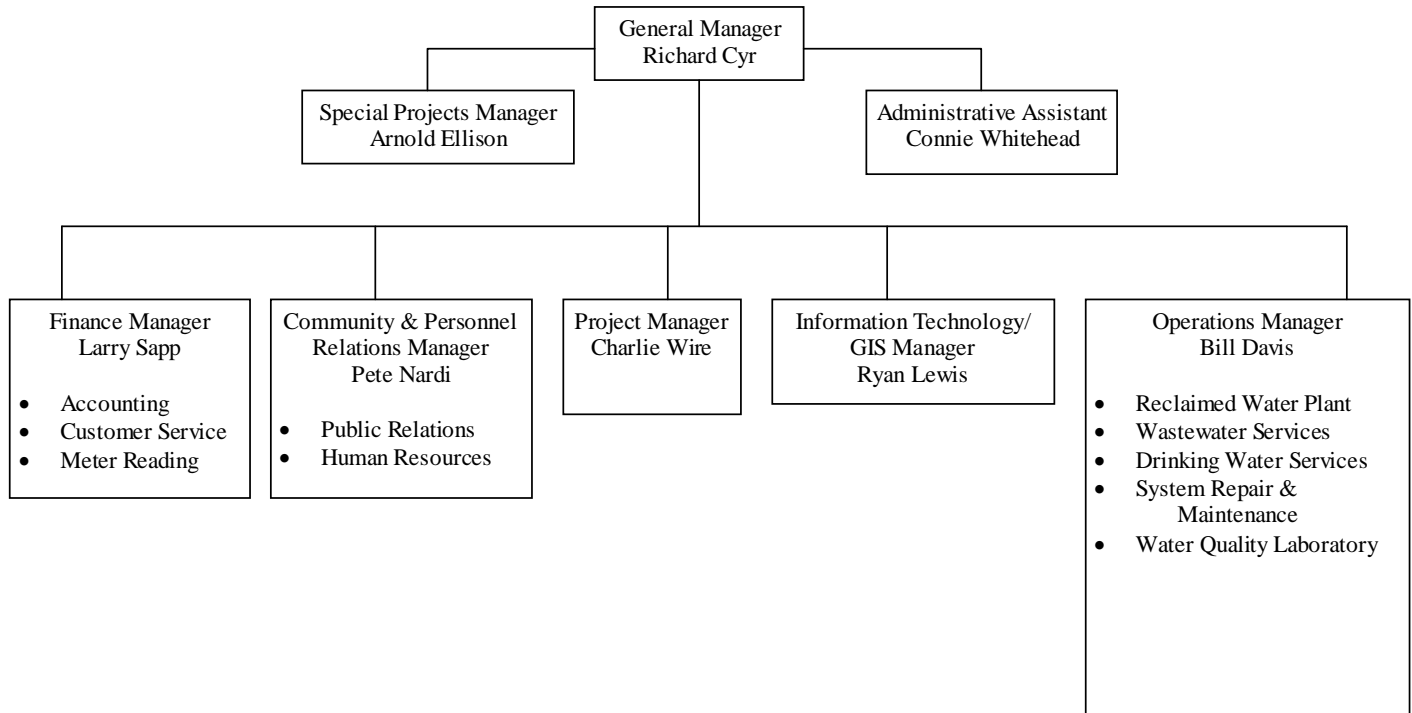
Current Term: 2005-2010

The PSD's Customer Service Center is located at 21 Oak Park Drive off Mathews Drive on Hilton Head Island. The Commission meets there on the fourth Tuesday of each month.



## Administrative Team

Below is an organizational chart of the District's administrative team.



## A Message from the General Manager

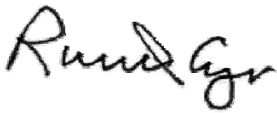
Hilton Head PSD views the protection of public health and the stewardship of our most precious natural resource – water – as our top priorities. The men and women of the PSD take seriously the vital role our utility plays in the sustainability and enhancement of our quality of life here on beautiful Hilton Head Island.

We are a drinking water, wastewater treatment, and reclaimed water public utility serving 18,000 customers in the north- and mid-island areas of Hilton Head Island. We provide an average of 6 million gallons of drinking water a day, peaking up to 11 million gallons a day in the summer. We treat an average of 3 million gallons of wastewater a day and recycle it into reclaimed water. The PSD annually recycles nearly 1 billion gallons of wastewater, with the reclaimed water being sold to 11 different golf courses for irrigation, and sent to four different wetlands as part of a state-monitored wetlands nourishment program. Our wastewater is never discharged into any bodies of water on or around the island. It is always recycled for irrigation and wetlands nourishment.

In this report's Priorities and Projects section, you will read about two of the most pressing issues facing Hilton Head PSD and Hilton Head Island itself – ensuring a clean and long-term drinking water supply in the face of continued saltwater intrusion into our traditional source of drinking water and the extension of our public sewer system to properties within our service area that still rely upon septic systems to treat their household wastewater.

The PSD is a small but state-of-the-art utility and we view ourselves as a local leader in the critically-important areas of public health and environmental protection, and natural resource management. We are honored to be stewards of this special place – Hilton Head Island.

Best Regards,



General Manager  
Hilton Head PSD

Aerial view of the PSD  
Reclaimed Water Plant and  
Customer Service Center



## **Vision Statement**

Our vision is to be a state of the art public utility, operated by an excellent, highly trained staff, providing the best practical levels of water and sewer customer service and satisfaction.

## **Mission Statement**

Hilton Head Public Service District is a public utility chartered by the General Assembly of South Carolina and owned by the people of the State. Its mission is to provide high quality water and sewer service to all properties within the district, and to deliver that service at a reasonable cost and in a timely manner, with sensitivity to the needs of the community and commitment to improving the environment of the island.

## **Strategic goals**

The PSD Commission conducts an annual Strategic Planning Session and conducts ongoing strategic planning activities throughout the year. Each Strategic Goal is accompanied by specific directives and staff work plan items. The directives and staff work plan also are updated annually. Below are the current Strategic Goals for the PSD as adopted by the PSD Commission.

### **The District's Strategic Goals**

Revised November 17, 2009

Goal No. 1 – Water Services: Meet all of our customers' water supply needs with the highest quality water possible at a reasonable cost.

Goal No. 2 - Wastewater Services: Meet all of the District's wastewater collection and treatment needs at a reasonable cost while enhancing and protecting the Island's environment.

Goal No. 3 – Environmental: Operate with the highest regard for protecting and improving the environment.

Goal No. 4 – Customer Satisfaction: Achieve a consistently high level of customer satisfaction.

Goal No. 5 – Financial Responsibility: Conduct all District activity in a fiscally responsible manner.

Goal No. 6 – Organizational Excellence and Leadership: Achieve organizational excellence and leadership through careful strategic planning, environmental initiatives and personnel excellence in all District activities.

Goal No. 7 – Asset Management: Improve, maintain and secure the District's property, plant and equipment assets.

Goal No. 8 – External Relations: Develop and expand the District's positive relationships with external organizations, utilities and governments.



## The PSD At-a-Glance

- Provides drinking water, wastewater treatment, and reclaimed water services for approximately 18,000 residential and commercial customers in the north and mid-island areas of Hilton Head Island, SC.
- Drinking water sources are: groundwater from the 600-foot-deep Middle Floridan Aquifer treated in Reverse Osmosis Plant that began operations in April 2009, groundwater from the 150-to-300-foot-deep Upper Floridan Aquifer, and treated Savannah River surface water purchased wholesale from the Beaufort-Jasper Water & Sewer Authority.
- Provides customers with an average of 6 million gallons of drinking water a day.
- Has the capacity to provide approximately 3.8 billion gallons of drinking water a year.
- Uses five elevated water storage tanks with a total capacity of approximately 1.4 million gallons, and three ground-level storage tanks with a capacity of 7 million gallons.
- Maintains 220 miles of drinking water lines throughout our service area.
- Operates a Reclaimed Water Plant with a capacity to treat 6.4 million gallons of wastewater a day.
- Maintains a public sewer system with more than 100 lift stations, including 133 miles of gravity sewer lines and 69 miles of force main.
- Has the capacity to store 45 million gallons of reclaimed water, using two storage tanks and two different lagoon systems.
- Provides reclaimed water to 11 golf courses on the island for use in irrigation. Also provides reclaimed water to four wetlands in Hilton Head Plantation and Palmetto Hall as part of a state-monitored wetlands nourishment program. The PSD annually recycles nearly 1 billion gallons of reclaimed water for golf course irrigation and wetlands nourishment.



PSD Reclaimed Water nourishes wetlands in Hilton Head Plantation and Palmetto Hall.

## Priorities and Projects

### *Combating Saltwater Intrusion*

The PSD historically relied upon the 150-foot-deep Upper Floridan groundwater aquifer for its primary water supply. Freshwater in the Upper Floridan is very pure and requires a minimal amount of treatment, making it a cost-effective supply. However, this natural resource is being destroyed by the over pumping of the aquifer in the Savannah, Ga. region. A phenomenon known as a cone of depression has been created in the aquifer under Savannah as a result of that area's over pumping. Hilton Head, sitting on the outer edge of the cone, has seen saltwater from Port Royal Sound brought into the aquifer where it is tapped by our drinking water wells. The PSD has lost six wells as a result of the saltwater intrusion since 2000, and it anticipates losing six of its remaining seven Upper Floridan wells by the year 2020. The loss of these wells represents a loss of 6.3 million gallons a day of drinking water capacity for the utility.

Studies conducted by the State of South Carolina and the PSD have shown that the saltwater intrusion is advancing from Port Royal Sound through the PSD's service area at a rate of more than 300 feet a year. There is no action Hilton Head can take to stop the intrusion. But the PSD has not simply stood by while our drinking water resource is being destroyed. Instead, we have developed new resources and are preparing to employ a new storage technique to ensure a high-quality and long-term supply of drinking water for generations to come.

### *The Reverse Osmosis Drinking Water Treatment Facility*

In the spring of 2009, the PSD began treating drinking water in our state-of-the-art Reverse Osmosis (RO) plant. We have developed a groundwater source never before used on Hilton Head Island – the 600-foot-deep Middle Floridan Aquifer – and are treating that water in the RO plant. Groundwater in the Middle Floridan is brackish and requires the removal of salt and other minerals in order to be distributed to customers. The RO plant is filtration-based treatment. It filters 3 million gallons of drinking water a day, about half of our average demand for water. Three wells into the Middle Floridan feed the RO plant.

Reverse Osmosis is a filtration treatment for drinking water. Specifically, it is a pressure-driven membrane separation process that removes ions, salts, and other dissolved solids. As such, RO is filtration on a molecular level. This filtering action is capable of removing 99 percent of the dissolved solids, 95 to 97 percent of most dissolved organics, and more than 98 percent of biological and other small particles from water. These high degrees of separation are made possible by the use of a semi-permeable membrane. This membrane permits certain substances, such as water, to pass through easily, while the passage of other items, such as dissolved salt, is impeded.

At the PSD's Reverse Osmosis plant, located on Jenkins Island across U.S. 278 from Windmill Harbour, raw water from the Middle Floridan Aquifer is pumped into tubes containing the semi-permeable membranes. The filtered drinking water is pulled through the system, while the dissolved solids are rejected by the membranes and continuously flushed from the system. The RO plant produces 3 million gallons of fresh drinking water for every 1 million gallons of dissolved solids, which is called the "concentrate stream" after being flushed through the RO system. The drinking water is sent into the PSD's water distribution system for delivery to customers, while the concentrate stream is blended into the saltwater of nearby Skull Creek. The PSD's water quality monitoring for the RO plant includes testing both the drinking water produced and the water quality of Skull Creek where the concentrate is blended.

### *Aquifer Storage and Recovery (ASR) Well*

As a result of the continued saltwater intrusion and its impact on drinking water supply, the PSD is preparing to use a new technique to store drinking water for the high-demand summer months – an Aquifer Storage & Recovery (ASR) drinking water supply well. ASR is a technique that seasonally stores surplus drinking water in the underground aquifer during times of low demand, and pumps into the water distribution system during times of high, or peak, demand.

The ASR well will provide 2 million gallons a day of drinking water during times of peak demand, and will replace part of the drinking water supply necessary to meet the PSD's daily peak water demand projection of 12 million gallons a day. The PSD will construct the ASR well at the utility's Royal James Drive property in Hilton Head Plantation.

The PSD and the Beaufort-Jasper Water & Sewer Authority have agreed upon a long-term, off-peak wholesale water rate that is less expensive than the normal rate (\$0.75 per 1,000 gallons, versus \$1.58 per 1,000 gallons). The PSD will inject the off-peak water into the ASR well during the winter months, and withdraw from the ASR well during the summer months of higher demand.

As part of the project, the PSD also will install a new 16-inch water transmission main into Hilton Head Plantation, and will pressurize a 24-inch water main jointly owned by the Broad Creek and Hilton Head PSDs. These main improvements are a crucial transmission and storage component of the PSD's efforts to combat the impacts of saltwater intrusion.

The PSD Commission has chosen to pay for the \$4-million ASR well and main improvement project using general obligation bonds that will be repaid by the utility's property tax rate. The project will add less than \$4.00 to the PSD taxes on a home valued at \$100,000. Construction of the ASR Well and main improvements is underway, and the well will begin replacing lost drinking water supply by the summer of 2013. More detail for the ASR Project and funding source is covered in the Financial Highlights section of the Management's Discussion and Analysis.

### *Future Water Supply Projects*

The PSD also must continue to plan for future projects to replace lost water supply. Below is a list of anticipated water supply projects the PSD faces:

- 2013 – First ASR well needed to replace three Upper Floridan wells, as discussed above.
- 2017 – Second ASR well needed to replace one Upper Floridan well.
- 2020 – Third ASR well needed to replace two Upper Floridan wells.
- 2020 – Reverse Osmosis plant expansion may be needed to add another one million gallons a day of supply.

The construction of additional ASR wells and expansion of the Reverse Osmosis plant are options currently at the forefront of the PSD's future water supply planning.

### *The Sewer Extension Effort*

In 2003, approximately 80 percent of all properties in the District's service area (Jenkins Island to the Hilton Head Resort) were connected to the public sewer system. Today, approximately 92 percent of all properties in the PSD service area are connected to the public sewer system. That leaves about 1,000 properties that remain unconnected to sewer.

The progress we have made has been the result of:

- Taking a systematic approach to extending the sewer system into previously unserved areas whenever the opportunity arises as a result of development or neighborhood initiative. For instance, neighborhoods such as Oak Marsh and Blue Heron Point chose to install sewer service and end their use of septic tanks.
- Contributions of Hilton Head and Broad Creek PSD customers to Project SAFE (Sewer Access for Everyone), which has provided more than \$150,000.00 in sewer connection grants for low-income property owners. Hilton Head PSD customers contribute more than \$35,000.00 annually to Project SAFE to help their neighbors meet the cost of sewer connection and end their use of septic systems. Project SAFE is a fund of the Community Foundation of the Lowcountry, a 501(c)(3) nonprofit. The PSD and the Foundation work closely together to assist SAFE applicants in the grant process. The Foundation makes the final determination on grant awards.
- Leadership on the part of the PSD Commission and former Hilton Head Mayor Tom Peebles to hold joint meetings of the Commission and Town Council on the topic of sewer access. These "Sewer Summits" paved the way for a set of Town Council goals that included prohibiting new septic tanks from being installed when sewer is available.
- Cooperation between the staff of the PSD and the Town led to the formation of a "Sewer Working Group" to work together on the common goal of providing sewer access.
- Cooperation between the PSD and the Town has resulted in reducing the cost of installing sewer by identifying Town lands where sewer infrastructure, such as pump stations, can be located. It also led to Town projects to install sewer for public park facilities that had been unserved by the sewer system.

Neighborhoods such as Spanish Wells, Chaplin, Baygall, and Stoney, comprise the bulk of the areas still in need of sewer access. The PSD is prioritizing projects based on public health, environmental impact, customer interest, and cost, among other factors.

The PSD in 2009 completed several public sewer projects that helped further our goal of providing sewer access to all properties in the PSD service area. It partnered with the Town of Hilton Head Island to complete a project that extended sewer service along part of Squire Pope Road to the Town's Green's Shell Park.

## **Management Letter of Transmittal**

The Commission and staff of the District are pleased to present the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2010. This is the PSD's first-ever CAFR. This report will be made available to the general public via the [www.hhpsd.com](http://www.hhpsd.com) web site. It also can be viewed in person at the PSD's Customer Service Center at 21 Oak Park Drive off Mathews Drive, on Hilton Head Island.

Management is responsible, in all material respects, for both the accuracy of the data included herein, and for the comprehensiveness of the presentation, including all disclosures. The data contained herein is being presented to fairly disclose the financial position and the results of operations of the PSD. All disclosures necessary to provide the reader with an understanding of the PSD's financial and operational activities have been included.

The CAFR is presented in three sections: Introduction; Financial; and Statistical. The Introduction contains an overview of the PSD's mission and its operations, including management transmittal letters. The Financial section has a report of the independent auditor, management's discussion and analysis, the PSD's financial statements, and supplemental financial data. The Statistical section includes select financial and demographic information, generally presented on a multi-year basis.

### ***Profile of the Government***

The PSD was created by Act No. 596 of the Acts and Joint Resolutions of the General Assembly of the State of South Carolina for the year 1969, and certain amendments thereto, as a Special Purpose District of perpetual succession. The purpose of the PSD is to provide for a publicly owned and operated waterworks and sewage disposal system within its service area on Hilton Head Island.

Citizens of Hilton Head Island relied on private wells for their drinking water needs until 1957. At that time, a local development firm by the name of the Hilton Head Water Company introduced a community waterworks system, installing water lines and drilling wells throughout the island.

As the community expanded and development progressed Hilton Head citizens became increasingly aware of the need for enhanced services, a need especially apparent in fire protection, water flow and sewer services.

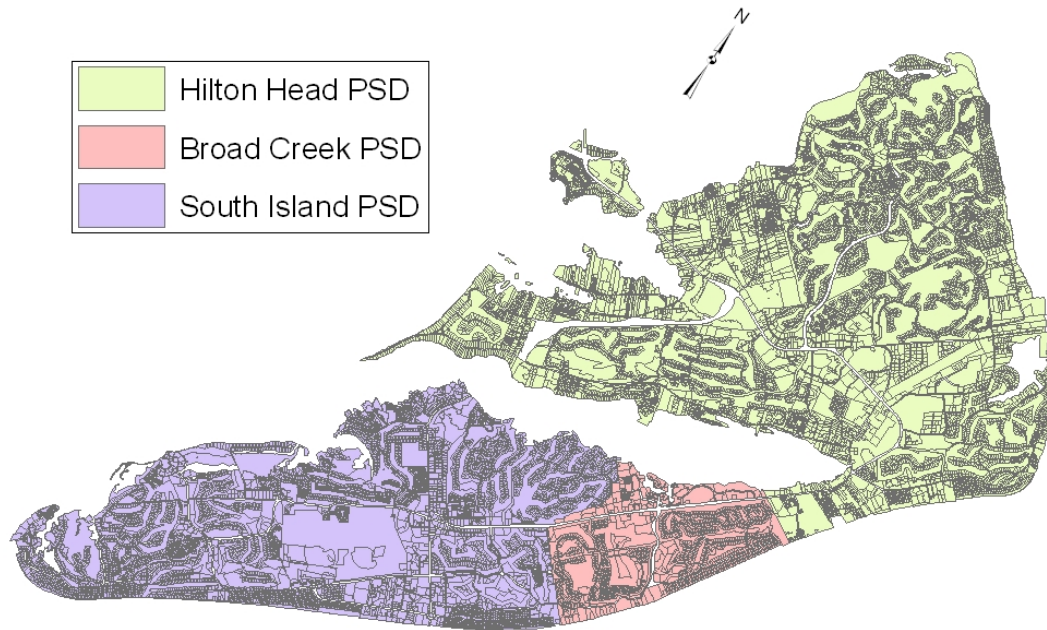
Ten separate utilities developed, both public and private, providing water and wastewater services to the residents of the island. Beginning in 1995, the District acquired the four utilities that now encompass its current service district, including Hilton Head Plantation Utilities, Hilton Head Island Rural Water District, Coastal Utilities and Hilton Head Water Company. In addition, the District acquired two small systems on the island previously served by the Beaufort-Jasper Water & Sewer Authority. Consolidation of the remaining island utilities formed the three public service districts currently serving Hilton Head Island.

Today, the PSD serves more than 18,000 customers in the north- and mid-island areas of Hilton Head Island, from Jenkins Island to the Hilton Head Resort.

The remainder of Hilton Head Island is served by either the Broad Creek PSD, which serves the Palmetto Dunes and Shelter Cove areas, or the South Island PSD, which serves all areas of the island south of Palmetto Dunes. The three island public service districts work together on an array of issues, from hurricane operations and recovery to future water supply planning.



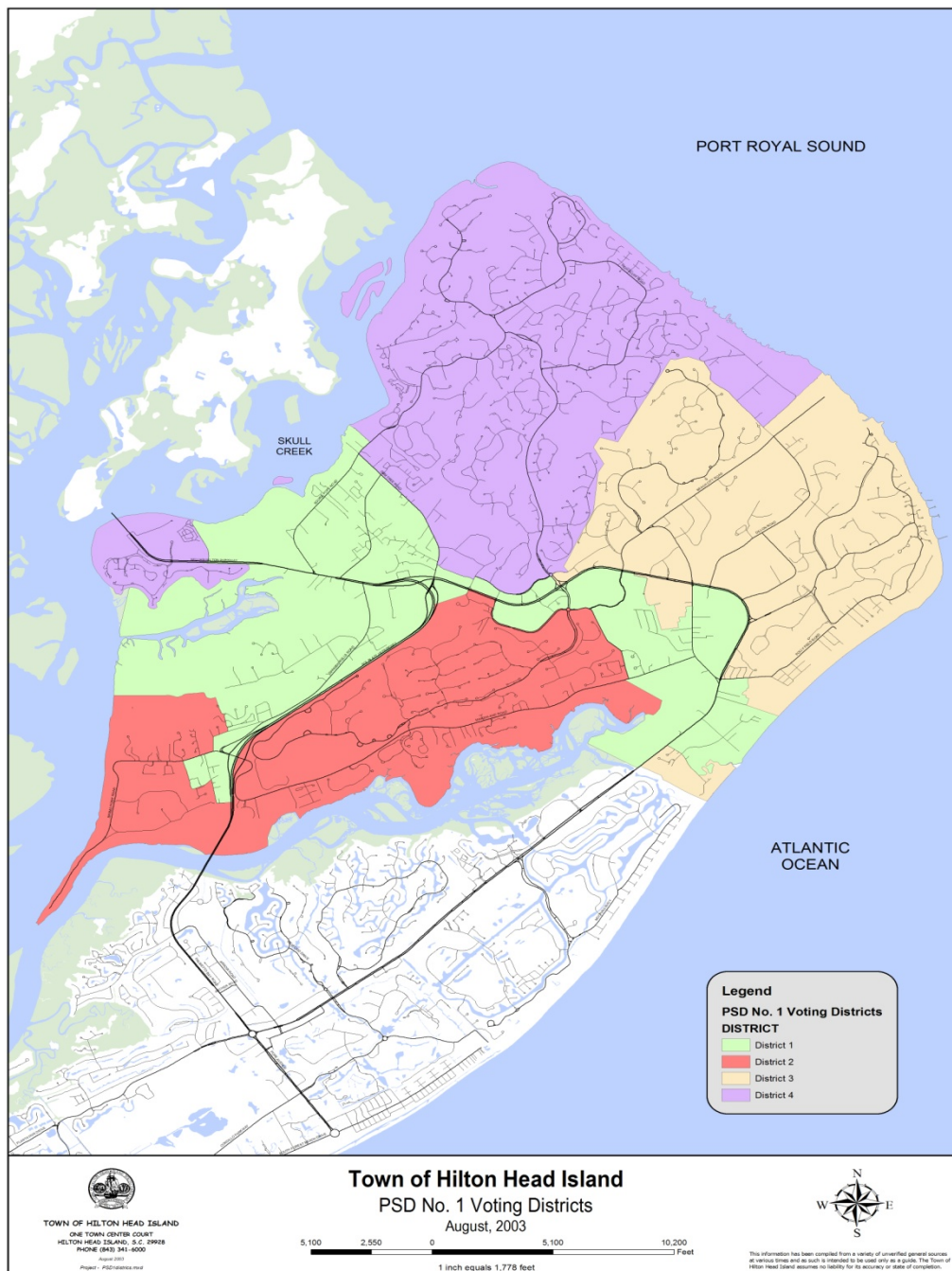
The following map shows each of the three PSDs' service areas:



Members of the Hilton Head PSD Board of Commissioners were nominated by the Beaufort County Legislative Delegation and appointed by the Governor of South Carolina, until 2003, at which time legislation was passed to have Commission members be elected by registered voters within the PSD service area.

Commissioners are elected to four-year terms. Commissioner elections are held during general election years. Commissioners represent four different voting districts within the PSD service area. Three Commissioners represent Voting District 4, and two Commissioners represent Voting District 3. All other Voting Districts are represented by one PSD Commissioner.

The map below shows the PSD Voting Districts within the utility's service area:



The Commission establishes policy for the PSD and employs the General Manager. The Commission reviews and adopts the utility's annual operating budget and conducts an annual Cost of Service Analysis in order to determine the utility's consumption rates and user fees.

The Commission normally meets on the fourth Tuesday of each month in the PSD Community Room at 21 Oak Park Drive off Mathews Drive on Hilton Head Island. Public comment is welcome at all Commission meetings.

## *Waterworks System*

The District's waterworks system currently consists of the following components: (a) six wells with treatment described in the following paragraph, (b) five elevated storage tanks with a total capacity of 1,350,000 gallons; (c) one 2,000,000 gallon ground storage tank; (d) three booster pump stations; (e) approximately 1,268,678 linear feet of water line ranging in size from 2 inches to 20 inches in diameter; and (f) a 3.0 MGD capacity reverse osmosis water treatment facility (the "RO Facility"). All wells are equipped with emergency generators. In addition, two ground storage tanks located within the District, with capacity of 3.0 and 2.0 million gallons, and 40,500 linear feet of 24 inch transmission mains are jointly owned with the Broad Creek PSD.

The District's water supply comes from three primary sources. The first source for potable and irrigation water is six wells drilled into the Upper Floridan Aquifer at approximately 150 to 200 feet below sea level. The water meets all drinking water standards and is chlorinated for disinfection as required by South Carolina Department of Health and Environmental Control ("DHEC") regulations. Under current operating conditions, the wells have a total annual permitted withdrawal capacity of approximately 1.31 billion gallons. The wells are not subject to a daily withdrawal limitation, provided that the amounts withdrawn in a given year or month may not exceed the annual or monthly permits, respectively.

The second source for potable and irrigation water is the Savannah River. The District obtains a portion of its water supply from the Savannah River and entered into a contract to purchase that water from the Beaufort-Jasper Water and Sewer Authority (BJWSA). The District has the right to draw up to 4 million gallons per day ("MGD") under the Contract. In addition, in September 2009, the District entered into an off-peak water purchasing contract with BJWSA. The Off-Peak Contract was initially for a five-year term commencing in November 2009, and provides for the purchase of water in the months of November through February at Off-Peak Rates. The term of the Off-Peak Contract was extended to 10 years in January 2010. The Off-Peak Rate is \$0.75 per 1,000 gallons for all water purchased above the District's 1 MGD minimum established under the Contract. The Off-Peak Rate is adjusted annually based on the July Consumer Price Index. There is no cap on the amount of water available for purchase and no minimum purchase amount. The Contract is discussed further in the Financial Highlights section of the Management's Discussion and Analysis.

The third source for potable and irrigation water is the Reverse Osmosis Drinking Water Treatment Facility, which treats brackish groundwater from the 600-foot-deep Middle Floridan Aquifer, a new source for Hilton Head Island. The RO Facility became operational in mid-April 2009. It provides 3 MGD of drinking water, which is about half of the District's average daily demand, and is expandable to provide 6 MGD.

With few exceptions, water services are available to all parcels of property presently located within the boundaries of the District. The number of customers has grown from 4,059 water taps (3,833 residential and 226 commercial) in 1988 to 17,316 water taps (comprising 10,415 residential taps, 4,843 master metered residential and 2,058 commercial water taps) in 2010. More information on water customer counts and growth can be found in the Financial Highlights section of the Management's Discussion and Analysis.

## *Wastewater and Reclaimed Water System*

The wastewater system is presently comprised of a wastewater collection system and treatment plant. Approximately 40% of the wastewater system infrastructure is less than ten years old, another 40% is ten to twenty years old, and the remaining twenty 20% is 20 to 30 years old. At present, the wastewater system is comprised of approximately 110 lift stations, 709,870 linear feet of gravity sewer lines (ranging in size from 4

inches to 42 inches in diameter), and 434,972 linear feet of force main, including effluent force mains ranging in size from 1-1/4 inches to 16 inches in diameter. The wastewater treatment plant is a 6.4 MGD complete mix activated sludge treatment plant with aerobic digestion and sludge dewatering. The wastewater treatment plant produces an effluent of less than 5 parts per million (ppm) of biological oxygen demand, 5 ppm of suspended solids, and 5 ppm of ammonia-nitrogen, as required by its National Pollutant Discharge Elimination System permit. Most of the effluent – also known as reclaimed water – produced by the wastewater treatment plant is distributed to eleven (11) golf courses within the District’s service area for disposal by spray irrigation. A smaller amount of effluent is distributed to four (4) conservancy wetlands within the District’s service area. The District also has four lined storage lagoons capable of storing up to 42 million gallons of reclaimed water and two ground level storage tanks capable of storing 3 million gallons of reclaimed water.

The number of sewer customers has grown from 3,310 customers (3,210 residential and 100 commercial) in 1988 to 14,891 customers (comprising 8,653 residential, 4,843 master metered residential, and 1,395 commercial) at June 30, 2010. More information on water and sewer customer counts and growth can be found in the Financial Highlights Section of the Management’s Discussion and Analysis.

## ***Financial Information***

The Management’s Discussion and Analysis (“MD&A”) is intended to serve as an introduction to the District’s financial statements and should be read in conjunction with the supplementary information and this portion of the management transmittal letter. The MD&A is found in the Financial Section of this report.

### *Accounting System and Budgetary Control*

The District’s financial accounting system is based on the full accrual basis in accordance with generally accepted accounting principles in the United States of America (GAAP). The accounts of the District are organized on the basis of a proprietary fund type enterprise fund. The fund is accounted for by a set of self-balancing accounts that comprise its assets, liabilities, net assets, and revenues and expenses. The fund is established to account for water and sewer operations that are financed and operated in a manner similar to private business enterprises, where the intent is to provide goods and services to the general public on a continuing basis recovered primarily through user charges.

The District is required by State law to adopt a balanced budget by June 30 of each year. District staff begins preparation of a draft budget in January, which is presented to the Commission in April and approved prior to June 30 of each year. The budget may be amended from time to time within the fiscal year. As required by the laws of the State of South Carolina, the District will adopt a balanced Operating Budget and provide full disclosure when a deviation from a balanced Operating Budget is planned or when it occurs. This balanced budget will ensure that all operating expenses will not exceed operating revenues at adoption and at year-end. Any increase in expenses, decrease in revenues, or combination of the two that would result in a material budget imbalance may require a budget revision upon the Commission’s approval.

The District operates on a current funding basis. Expenditures are budgeted and controlled so as not to exceed current revenues plus the planned use of Fund Balances accumulated through prior years.

### *Internal Accounting Controls*

The District has developed and adopted a comprehensive set of financial policies that are consistent with the District's goals and objectives. Financial policies are an integral part of the development of service, providing of capital, and establishing of financial plans and the annual budget. They provide the basis for decision-making and ensure the District's ongoing financial stability. The financial policies of the District provide the structure and direction for financial reporting, planning, and decision making by management and the Board. Additionally, they are designed to ensure the financial integrity of the District. Policies are documented and periodically reviewed to reflect changes in Board policy, legal and professional requirements, and changes in accepted industry practices. Internal accounting controls are designed to provide reasonable assurance that assets are safeguarded from unauthorized use or disposition, and that records used for preparing financial reports and maintaining asset accountability are reliable. A system of internal controls is established and monitored by management. The Finance Manager reviews controls and procedures on a continuing basis and immediately reports any concerns to the General Manager / Finance Committee for resolution. As part of this initiative, the Finance Manager oversees the documentation and periodic review of financial standard operating procedures to ensure that internal audit functions and professional skepticism are incorporated as part of the analytical and reporting function. Management of the District is further charged, through personnel policies, with providing the leadership that promotes ethical behavior within the control environment.

The Finance Committee of the Board of Directors serves as the Audit Committee of the District. It is composed of two members of the Board. Generally, this Committee meets with management on a monthly basis to review the financial status of the District. Additionally, the Committee meets with management and the independent external auditors to ensure that both parties are fulfilling their obligations with regard to auditing, controls, and other financial reporting factors.

### *Rates and Charges*

The District maintains and administers a revenue system that assures a reliable, equitable and sufficient revenue stream to support the District services. Since the principal revenue stream for the District is composed of the fees and charges established by the Commission, the governing body of the District, it is important that the District adopts policies that identify the manner in which fees and charges are set and the extent to which they cover the cost of the service provided.

The District establishes all user charges and fees at levels related to the costs (operating, direct, indirect and capital) of providing its services. The District reviews these fees and charges annually during the budget process and target rates that are expected to produce revenues sufficient to fully fund the costs of providing services – particularly in the District's key businesses (water and wastewater).

Costs of service includes direct and indirect costs such as operating and maintenance costs, overhead, and charges for use of capital. The District may choose not to recover all costs, but it must identify such costs. Reasons for not recovering full costs are identified and explained.

The District also examines rates and charges levied by other water and sewer systems for like services in establishing rates, fees and charges. These fees (water and sewer user fees, capacity fees, tap fees, tower revenues, etc.) are reviewed through the District's annual cost of service process. An aggressive policy of seeking the collection of delinquent utility accounts is maintained and is outlined by specific procedures. In projecting revenues - and where judgment is required - conservatism is the rule.



The District tries to minimize water and sewer rate increases whenever possible. On August 1, 2008, it was necessary to raise water rates for the first time since July 1, 1999. Effective October 1, 2009, it was again necessary to raise water rates. For a summary of the District's historical and present water and sewer rates, please reference the Water Rates Comparison Table in the Statistical Section.

Sewer rates were restructured for fiscal year 2006 to incorporate a 10,000-gallon monthly cap for residential users (previously the cap was 32,000 gallons) with residential consumption rates being increased from \$1.25 to \$1.65 per thousand gallons and commercial consumption rates being increased from \$1.25 to \$1.50 with no cap. It was then necessary to raise sewer rates again for fiscal year 2007 for residential customers up to \$1.90 per thousand gallons. The last sewer rate increase was put into effect October 1, 2009 increasing both residential and commercial consumption rates by \$0.10 per thousand gallons.

### *Millage*

Pursuant to Act No. 596, the District is authorized to impose ad valorem property taxes not to exceed ten mills to defray a portion of its operational costs. The District's operational ad valorem tax millage is fixed at 3 mills. As of July 1, 2007, millage rates for operations may increase only at a rate equal to the sum of (a) the increase in the consumer price index, plus (b) the rate of population growth of the political subdivision or school district. This limitation may be overridden by a vote of two-thirds of the governing body of the political subdivision, but only for the following purposes and only in a year in which such condition exists:

1. a deficiency of the preceding year;
2. any catastrophic event outside the control of the governing body such as a natural disaster, severe weather event, act of God, or act of terrorism, fire, war, or riot;
3. compliance with a court order or decree;
4. taxpayer closure due to circumstances outside the control of the governing body that decreases by ten percent or more the amount of revenue payable to the taxing jurisdiction in the preceding year;
5. compliance with a regulation promulgated or statute enacted by the federal or state government after the ratification date of this section for which an appropriation or a method for obtaining an appropriation is not provided by the federal or state government;
6. purchase by the local governing body of undeveloped real property or of the residential development rights in undeveloped real property near an operating United States military base which property has been identified as suitable for residential development but which residential development would constitute undesirable residential encroachment upon the United States military base as determined by the local governing body. The local governing body shall enact an ordinance authorizing such purchase and the ordinance must state the nature and extent of the potential residential encroachment, how the purchased property or development rights would be used and specifically how and why this use would be beneficial to the United States military base, and what the impact would be to the United States military base if such purchase were not made. Millage rate increases for the purpose of such purchase must be separately stated on each tax bill and must specify the property, or the development rights to be purchased, the amount to be collected for such purchase, and the length of time

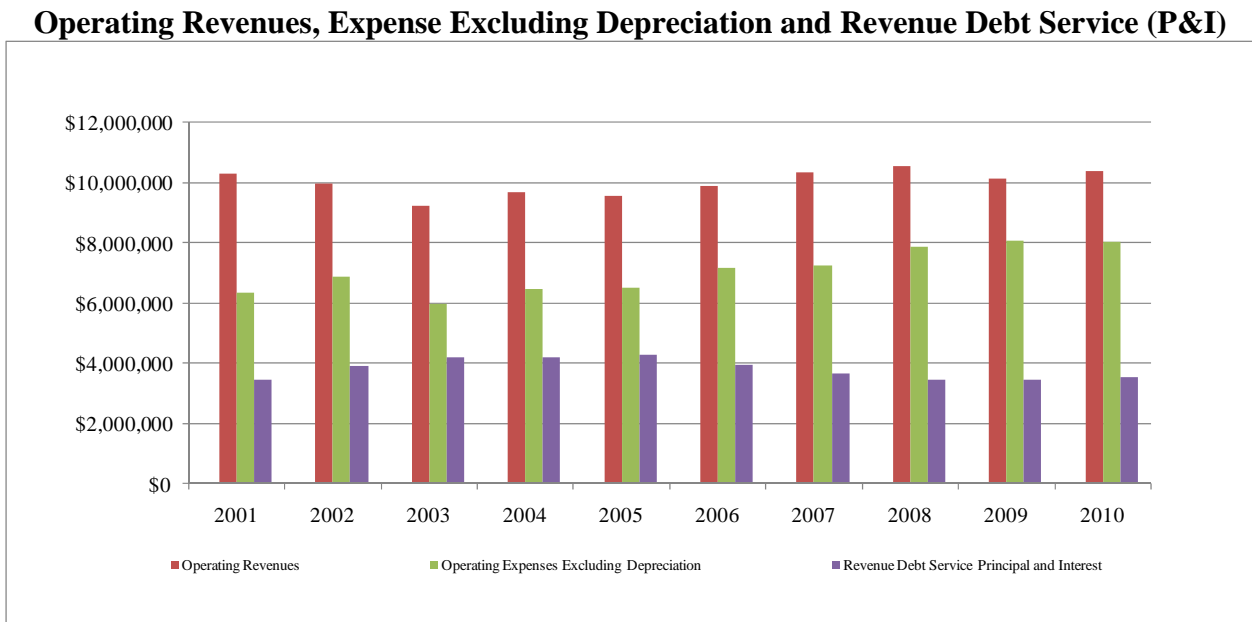
that the millage rate increase will be in effect. The millage rate increase must reasonably relate to the purchase price and must be rescinded five years after it was placed in effect or when the amount specified to be collected is collected, whichever occurs first. The millage rate increase for such purchase may not be reinstated unless approved by a majority of the qualified voters of the governmental entity voting in a referendum. The cost of holding the referendum must be paid from the taxes collected due to the increased millage rate; or

7. to purchase capital equipment and make expenditures related to the installation, operation, and purchase of the capital equipment including, but not limited to, taxes, duty, transportation, delivery, and transit insurance, in a county having a population of less than one hundred thousand persons and having at least forty thousand acres of state forest land. For purposes of this section, “capital equipment” means an article of nonexpendable, tangible, personal property, to include communication software when purchased with a computer, having a useful life of more than one year and an acquisition cost of fifty thousand dollars or more for each unit.

The limitations described above do not apply to the levy of debt service millage. Therefore, the District is also authorized to impose ad valorem property taxes, without limit, to defray the debt service on general obligation bonds of the District. All of such general obligation bonds are approved by the Beaufort County Council pursuant to South Carolina general law.

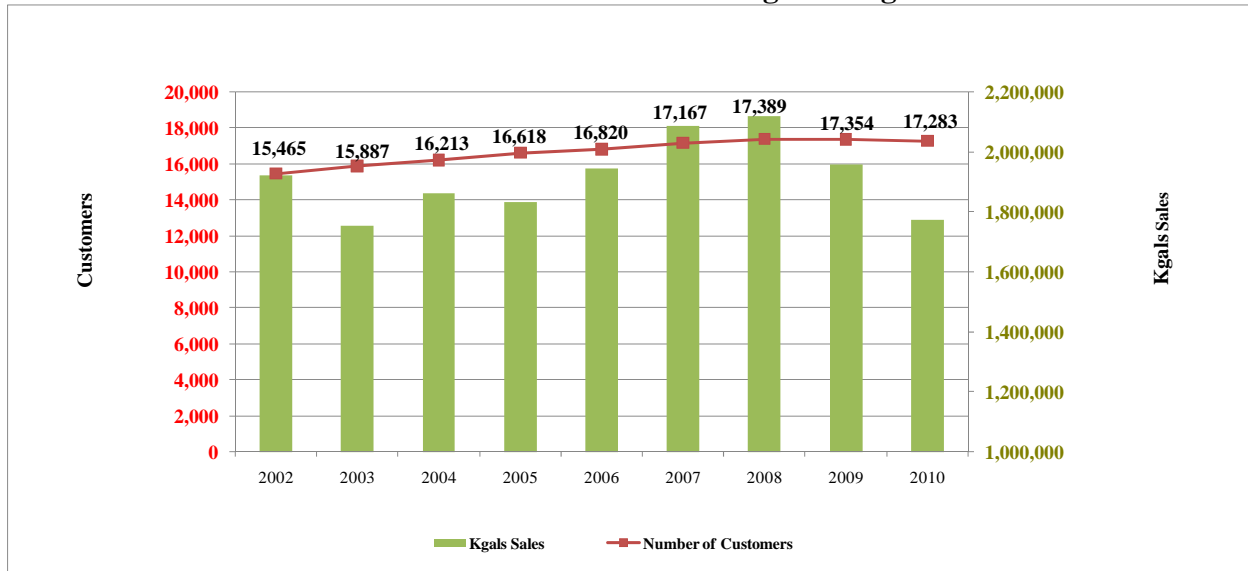
#### *Financial Condition*

Despite very low water consumption levels and corresponding decreased revenues for both fiscal years 2009 and 2010, the District’s financial condition remains sound. This is due in part to proactive fiscal management of customer rates, operating expenses and capital expenditures. Operating revenues, operating expenses (excluding depreciation), and revenue related debt service payments for the past ten fiscal years are summarized in the following graph.



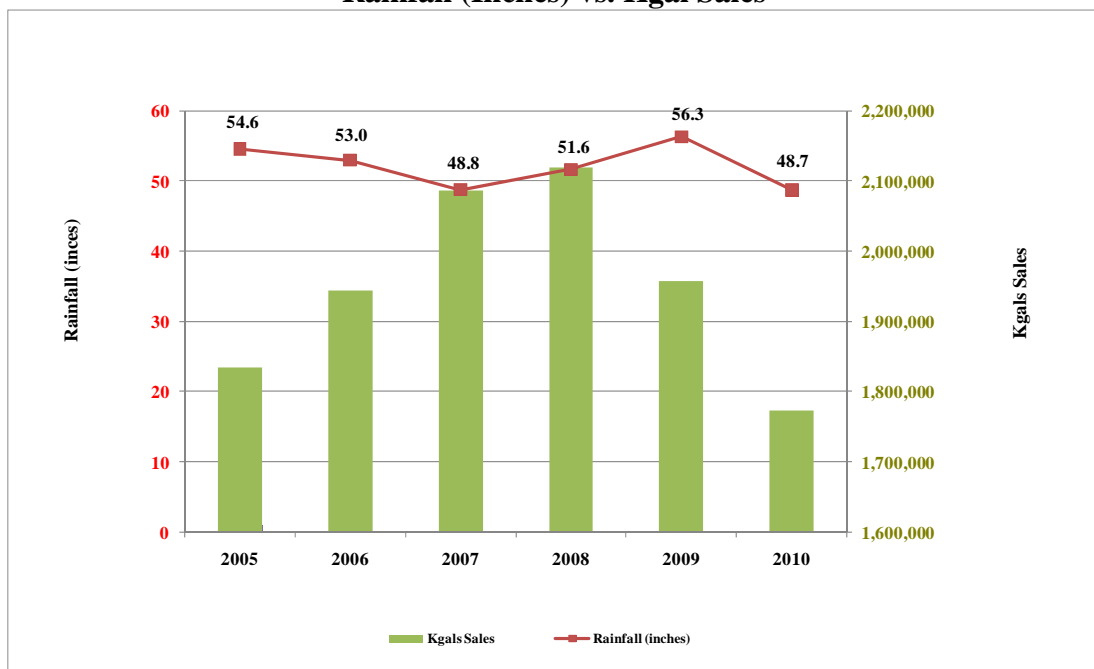
For both fiscal years 2009 and 2010, there was a sharp decrease in customer water consumption levels and related revenues. While a small percentage of this decrease is attributable to decreased customer counts, it is more likely that low consumption levels are mainly due to the economic downturn and a combination of increased rainfall (fiscal year 2009) and cooler weather (fiscal year 2010).

**Customers vs. Water/Irrigation Kgal Sales**



As shown in the following chart, rainfall amounts typically have a direct inverse relationship<sup>1</sup> to customer consumption levels with the exception of fiscal year 2010. Despite a comparatively lower rainfall amount for fiscal year 2010, water consumption levels were at their lowest since fiscal year 2003 due to unseasonably cooler weather and lower tourist occupancy rates associated with the economic downturn.

**Rainfall (Inches) vs. Kgal Sales**



<sup>1</sup> Inverse Relationship – Higher Rainfall causing Lower Consumption Levels.

The fiscal year 2009 water/irrigation consumption level dropped 8% or 161 million gallons from the prior year. For fiscal year 2010, there was a decrease of 10% or almost 185 million gallons from the already low 2009 water/irrigation consumption level. Despite lower consumption levels, water and sewer revenues have remained adequate due in part to a water rate increase implemented in fiscal year 2009 and both a water and sewer rate increase implemented in fiscal year 2010.

### *Cash Management*

Cash management activities are conducted in full compliance with prevailing state and federal regulations. Furthermore, such activities are designed to adhere to guidelines and standards promulgated by such professional organizations as the American Institute of Certified Public Accountants (AICPA), the Governmental Accounting Standards Board (GASB), and the Government Finance Officers Association (GFOA). Investments of the District must comply with Section 6-5-10 of the Code. The provisions of South Carolina Code Section 6-5-10 do not impair the power of the District to hold funds in deposit accounts with banking institutions as otherwise authorized by law. Investments have maturities consistent with the time or times when the invested monies will be needed in cash.

The District's cash management program seeks to achieve three objectives with regards to investments: safety of principal, adequate liquidity to meet daily cash needs, and a reasonable yield commensurate with the preservation of principal and liquidity.

The Finance Manager institutes and administers specific procedures and criteria relating to cash management issues in pursuit of ensuring the absolute safety and integrity of the District's financial assets, while optimizing financial return of those assets. Additionally, the Finance Manager, with the assistance of the Commission and General Manager of the District, is responsible for oversight and will regularly examine and evaluate the District's Cash and Investment Management Policy (the "Policy") and investment activities, and will recommend revisions to the Policy and operational rules and regulations as circumstances dictate.

### *Risk Management*

The District has policies in place to guide the financial actions it will take in the event of emergencies, natural disasters, or other unexpected events. Further, the District purchases insurance for general and automobile liability and participates with the State Accident Fund providing workers' compensation coverage to limit the exposure to risk.

The District also has implemented policies regarding insurance coverage on various assets. These policies ensure that assets at risk are properly identified and sufficiently insured, while also tracking those assets should be removed from the insurable assets list.

### *Independent Audit*

The accompanying financial statements have been audited by the District's independent auditors, Robinson Grant & Co., P.A., and their report on the financial statements resulting from their audit is included in the Financial Section of this report.

# FINANCIAL



## **INDEPENDENT AUDITORS' REPORT**

December 2, 2010

The Commissioners  
Hilton Head No. 1 Public Service District  
Hilton Head Island,  
Beaufort County, South Carolina

We have audited the accompanying balance sheets of Hilton Head No. 1 Public Service District as of June 30, 2010 and 2009, and the related statements of revenues, expenses and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Hilton Head No. 1 Public Service District as of June 30, 2010 and 2009, and the results of its operations, and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements of Hilton Head No. 1 Public Service District taken as a whole. The introductory section, supplementary information, and statistical section, as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplementary information has been subjected to the auditing procedures applied to the audits of the basic financial statements and, in our opinion, is fairly

stated in all material respects in relation to the basic financial statements. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

## Management's Discussion and Analysis

This section of the Hilton Head No. 1 Public Service District (the "District") annual financial statements presents our analysis of the District's financial performance during the fiscal years ending June 30, 2010, 2009 and 2008. Please read it in conjunction with the financial statements following this section.

### *Financial Highlights*

- Total assets at the end of the fiscal year 2010 were approximately \$92.29 million, exceeding liabilities by \$38.56 million (See Table A-1, Page 29).
- The District's General Obligation (GO) Bond Rating: On October 5, 2009, Moody's Investor Service upgraded the District's GO bond rating to Aa2. Prior to this date, the District's GO bond rating was Aa3. According to Moody's, the upgrade was the result of ongoing economic growth in the District's tax base, proactive management practices, and strong fiscal policies. That rating was then recalibrated to Aa1 on May 1, 2010. See the subsequent events section on page 6 for further information on the District's GO bond rating upgrades which occurred after fiscal year 2010.
- During September 2009 the District and the Broad Creek Public Service District entered into an off peak water purchasing contract with Beaufort Jasper Water and Sewer Authority (BJWSA). The key conditions of the original contract executed September 22, 2009 are outlined below:
  - ✓ The contract term is for five years starting in November 2009.
  - ✓ Off peak is defined as November through February.
  - ✓ The off peak rate charged by BJWSA will be \$0.75 per 1,000 gallons for all water purchased above the 1 million gallon per day underlying contract minimum.
  - ✓ The rate will be adjusted annually based on the July Consumer Price Index (CPI) and BJWSA will provide 60 days notice of their intent to adjust the rates.
  - ✓ There is no cap on the amount of off peak water available for purchase.
  - ✓ There is no additional minimum purchase amount. As such, the District can terminate the contract by discontinuing further water purchases.

Amended Off Peak Contract: During January 2010, BJWSA agreed to extend the term of the off peak rate agreement from five years to 10 years. At the end of the initial 5 year period, BJWSA will recalculate the off peak rate based on current costs and then adjust it annually during the remaining 5 years based on the CPI. In addition, BJWSA will consider extending off peak pricing making the off peak rate effective October 1 through March 31 on a case by case basis.

- Water Customer Growth: Although the District has added 37 new water/irrigation taps to the system in fiscal year 2010 the net effect has been a reduction of 38 water service equivalent dwelling units (EDUs) due to water services being terminated due to foreclosures and economic factors. As of June 30, 2010, the District has a total of 17,316 EDUs. This is a 0.2% decrease for FY'10. For FY'09 there was also a 0.2% decrease in total EDUs as compared to the FY'08 growth of 94 new EDUs or 0.5%. The current EDUs consist of 16,270 water service units, 995 irrigation service units, and 51 miscellaneous water units such as dock meters, hydrants, pool meters, and golf course water coolers.

Water & Irrigation Customers					
<u>Fiscal Year</u>	<u>Residential</u>	<u>Master Metered Residential</u>	<u>Commercial</u>	<u>Total</u>	<u>% Growth</u>
<b>2010</b>	<b>10,415</b>	<b>4,843</b>	<b>2,058</b>	<b>17,316</b>	-0.2%
2009	10,440	4,843	2,071	17,354	-0.2%
2008	10,525	4,834	2,030	17,389	0.5%
2007	10,463	4,822	2,010	17,295	1.1%

- Sewer Customer Growth: Similarly, sewer system growth has slowed due to water services being terminated that have related sewer services. Total sewer service EDUs have only increased by 11 for a total of 14,891 EDUs. This is a 0.1% increase for FY'10 as compared to FY'09 growth of 45 new EDUs or 0.3%.

Sewer Customers					
<u>Fiscal Year</u>	<u>Residential</u>	<u>Master Metered Residential</u>	<u>Commercial</u>	<u>Total</u>	<u>% Growth</u>
<b>2010</b>	<b>8,653</b>	<b>4,843</b>	<b>1,395</b>	<b>14,891</b>	0.1%
2009	8,635	4,843	1,402	14,880	0.3%
2008	8,603	4,834	1,398	14,835	1.2%
2007	8,467	4,822	1,369	14,658	2.0%

As shown in the table below, the sewer to water customer percentage has increased to 91.52% percent since the beginning of fiscal year 2010.<sup>2</sup>

Sewer Connection Growth 06/30/10						
<u>Date</u>	<u>All Water/Irrigation EDU's</u>	<u>Water EDU's</u>	<u>Change in Water EDU's</u>	<u>Sewer EDU's</u>	<u>Change in Sewer EDU's</u>	<u>% Water to Sewer EDU's</u>
06/30/09	17,354	16,304	N/A	14,880	N/A	91.27%
09/30/09	17,334	16,281	-23	14,882	2	91.41%
12/31/09	17,280	16,233	-48	14,845	-37	91.45%
03/31/10	17,264	16,220	-13	14,841	-4	91.50%
06/30/10	17,316	16,270	<u>50</u>	14,891	<u>50</u>	91.52%
<b>Total EDU's Added</b>			<b>-34</b>		<b>11</b>	

- The following rate changes were approved at the July 28, 2009 Commission Meeting:
  - ✓ Effective August 1, 2009, water meter construction fees were increased to reflect recent meter cost and overhead increases.
  - ✓ Effective October 1, 2009, volumetric water rates were increased to affect an overall 3.4% increase in revenues as compared to the fiscal year 2010 budget. In addition, the volumetric sewer rate has been adjusted, raising the residential volumetric sewer charge from \$1.90 to \$2.00 per thousand gallons and the commercial volumetric sewer charge from \$1.50 to \$1.60 per thousand gallons.

<sup>2</sup> This percentage is based solely on water customers and does not include irrigation, dock meters, hydrants, pool meters, and golf course water coolers etc.

- During July 2009, the District issued two forms of debt; the Series 2009 GO Debt in the amount of \$1,781,694 and the Series 2009B Front Foot Assessment (FFA) Revenue Debt in the amount of \$355,902. These issues closed on July 31, 2009 which allowed the District to reimburse its operating account for funds expended in conjunction with construction of the RO Plant and installation of gravity and low pressure sewer.
- On April 27, 2010, the Commission adopted a resolution authorizing a petition to the County Council of Beaufort County (the “County Council”) regarding the issuance of the District’s general obligation bonds in an amount not exceeding \$4,000,000. On June 14, 2010, the County Council approved the issuance of the District’s general obligation bonds. Then, on June 15, 2010, the Commission enacted a resolution authorizing the issuance of the general obligation bonds in an amount not exceeding \$4,000,000. The bonds were issued to construct and equip a new aquifer storage and recovery (ASR) well to service the residential and commercial establishments located within the District. The bonds closed September 28, 2010 (see Subsequent Events, pages 28 and 29, for details), and were issued in the principal amount of \$3,970,000.
- On June 15, 2010, the Commission adopted a series resolution providing for the issuance and sale of its Waterworks and Sewer System Refunding Revenue Bond, Series 2010A. Pursuant to such authorization, on June 15, 2010, the District issued its Series 2010A Bond in the principal amount of \$190,721.78 in order to affect the redemption of its outstanding Series 2000B Revenue Bond and to pay certain costs and expenses associated therewith.
- On June 15, 2010, the Commission adopted a series resolution providing for the issuance and sale of its Waterworks and Sewer System Improvement Revenue Bonds, Series 2010B, in the principal amount of not exceeding four million dollars (\$4,000,000) of Hilton Head No. 1 Public Service District, South Carolina. The Series 2010B Bonds were issued (1) to defray the costs of certain improvements to the System, consisting of (i) various improvements and repairs to the District’s wastewater treatment plant, including the addition of a new influent screen, replacement of the third screw pump, replacement of a pond liner, replacement of a centrifuge, replacement of a grit removal system, repairs and replacement to the gravity line from U.S. Highway 278 to the wastewater treatment plant, and replacement of the chlorination system, and (ii) installation of the Stoney lift station and (2) to pay certain costs and expenses relating to the issuance of the Series 2010B Bonds. The Bonds closed August 24, 2010 (see the following Subsequent Events section for details) and were issued in the principal amount of \$3,400,000.

## ***Subsequent Events***

### *Standard and Poor's Revenue Bond Rating*

District's Revenue Bond Rating: On July 29, 2010, Standard and Poor's (S&P) assigned its AA long term rating to the District's \$3,400,000 Series 2010B waterworks and sewer system improvement revenue bonds and affirmed its AA underlying rating on the District's previously rated parity bonds. According to S&P the rating affirmation issued reflects the District's:<sup>3</sup>

- Diverse Customer Base;
- Good debt service coverage and liquidity; and
- Well-developed infrastructure with manageable future capital needs.

### *Series 2010B Revenue Bond Closing Details*

The Series 2010B Revenue Bonds closed on August 24, 2010 and were issued in the principal/par amount of \$3,400,000. The all inclusive cost/interest rate is 4.084%.

### *Standard and Poor's 2010 General Obligation Bond Rating*

District's General Obligation Bond Rating: On August 31, 2010, S&P raised its rating on the District's general obligation debt two notches to AA+ from AA- based on the District's strong financial operations and stable local economy. S&P also assigned its AA+ rating and stable outlook to the District's series 2010 GO bonds. This bond issue is to be used to fund the District's Aquifer Storage and Recovery (ASR) Project. According to S&P the rating issued further reflects the District's:<sup>4</sup>

- Affluent community in northern Hilton Head Island, South Carolina;
- Well established, tourism-centered local economy with below average unemployment;
- Large and growing property tax base; and
- Strong financial position, supported by healthy fund balance reserves.

### *Moody's General Obligation Bond Rating*

During August 2010, Moody's again assigned a Aa1 rating to the District's Series 2010 GO bonds. Positive factors which were cited by Moody's included the following:

- Wealthy tax base with seasonal component experiencing moderate growth;
- Modestly growing customer base; Modest growth expected in near-term;
- Satisfactory financial operations and liquidity position guided by formal fiscal policies; and
- Debt burden expected to remain modest.

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<sup>3</sup> Source: Standard and Poor's, Global Credit Portal Ratings Direct, [www.standardandpoors.com/ratingsdirect](http://www.standardandpoors.com/ratingsdirect), July 29, 2010.

<sup>4</sup> Source: Standard and Poor's, Global Credit Portal Ratings Direct, [www.standardandpoors.com/ratingsdirect](http://www.standardandpoors.com/ratingsdirect), August 31, 2010.

## Series 2010 GO Bond Closing Details

The Series 2010 GO Bond closed on September 28, 2010 and were issued in the principal/par amount of \$3,970,000. The all inclusive cost/interest rate is 3.301%.

## Financial Analysis of the District

The Balance Sheets and the Statements of Revenues, Expenses and Changes in Net Assets report information about the District's activities in a way that shows the District's financial position as a result of this year's operations. These two statements report the net assets of the District and changes in them. The District's net assets and the difference between assets and liabilities is one way to measure financial health or financial position. Over time, increases or decreases in net assets are indicators of whether the District's financial health is improving or deteriorating. However, one must also consider other non-financial factors such as changes in economic conditions, population growth, annexation and new or changed legislation.

### Balance Sheets

The following comparative condensed balance sheets show changes in financial position from previous fiscal years:

**TABLE A-1**  
**Hilton Head Public Service District**  
**Condensed Balance Sheets as of June 30, 2010, 2009, and 2008**

Year Ended June 30,	2010	2009	2008	2010 to 2009	%
<b>Assets</b>				Increase (decrease)	
Current assets	\$ 5,118,206	\$ 4,330,719	\$ 6,728,842	\$ 787,487	18.2%
Restricted assets	2,378,848	2,684,128	6,656,444	(305,280)	-11.4%
Net Property Plant & Equipment	80,515,057	81,439,611	75,400,516	(924,554)	-1.1%
Sewer Assessments, Long-term	3,329,883	3,284,197	3,659,584	45,686	1.4%
Other	946,120	993,225	1,073,899	(47,105)	-4.7%
<b>Total Assets</b>	<b>92,288,114</b>	<b>92,731,880</b>	<b>93,519,285</b>	<b>(443,766)</b>	<b>-0.5%</b>
<b>Liabilities</b>					
Current Liabilities	4,577,296	4,021,429	3,462,428	555,867	13.8%
Noncurrent Liabilities, net of amortization	49,147,698	49,445,029	49,553,374	(297,331)	-0.6%
<b>Total Liabilities</b>	<b>53,724,994</b>	<b>53,466,458</b>	<b>53,015,802</b>	<b>258,536</b>	<b>0.5%</b>
<b>Net Assets</b>					
Invested in capital assets, net	29,464,863	30,467,552	29,167,977	(1,002,689)	-3.3%
Restricted for capital activity/debt service	2,378,848	2,446,988	2,334,594	(68,140)	-2.8%
Unrestricted	6,719,409	6,350,882	9,000,912	368,527	5.8%
<b>Total Net Assets</b>	<b>38,563,120</b>	<b>39,265,422</b>	<b>40,503,483</b>	<b>(702,302)</b>	<b>-1.8%</b>
<b>Total Liabilities and Net Assets</b>	<b>\$ 92,288,114</b>	<b>\$ 92,731,880</b>	<b>\$ 93,519,285</b>	<b>\$ (443,766)</b>	<b>-0.5%</b>



## Net Assets

Changes in net assets result from operating and non-operating revenues, expenses and contributions of capital. Net assets are classified in the following three components: *invested in capital assets, net of related debt*; *restricted for capital activity and debt service*; and *unrestricted net assets*.

*Invested in capital assets, net of related debt*, consists of all capital assets, net of accumulated depreciation and reduced by outstanding debt that is attributable to the acquisition, construction and improvement of those assets; debt related to unspent proceeds of other restricted cash and investments is excluded from the determination.

*Restricted for capital activity and debt service* consists of net assets for which constraints are placed thereon by external parties, such as lenders, grantors, contributors, laws, regulations and enabling legislation, including self-imposed legal mandates, less any related liabilities.

*Unrestricted* consists of all other net assets not included in the above categories.

Total net assets as of June 30, 2010 were \$38,563,120, representing a \$702,302 or 1.8% decrease from the prior year. Fiscal year 2009 had a decrease in total net assets from fiscal year 2008 of \$1,238,061 or 3.1% due to decreased capital contributions.

Change in Net Assets			
Year Ended June 30,	2010	2009	2008
Invested in Capital assets, net	\$ 29,464,863	\$ 30,467,552	\$ 29,167,977
Restricted for capital activity and debt service	2,378,848	2,446,988	2,334,594
Unrestricted	6,719,409	6,350,882	9,000,912
Total Net Assets	<u>\$ 38,563,120</u>	<u>\$ 39,265,422</u>	<u>\$ 40,503,483</u>

Of the total net assets, \$5,118,206 million are current non-restricted assets available to support short-term operations (Table A-1, page 29). This current asset balance is \$787,487 higher than on June 30, 2009.

## Capital Assets

As of June 30, 2010, the District has invested \$80,515,057 (net of accumulated depreciation) in water and sewer equipment and a broad range of infrastructure as shown in Table A-2 below. Net Property Plant & Equipment has decreased \$924,554 during fiscal 2010.

**TABLE A-2**  
**Capital Assets**

<b>Year Ended June 30,</b>	<b>2010</b>	<b>2009</b>	<b>2008</b>
Land	\$ 1,326,629	\$ 1,266,629	\$ 1,141,629
Wetlands discharge system	996,653	996,653	996,653
Waterworks system	50,684,177	49,500,248	37,260,024
Shop furniture and equipment	98,412	98,412	98,412
Sewage disposal system	26,949,588	21,137,894	23,979,989
Buildings	4,289,335	4,289,335	4,269,460
Sewage treatment facilities	36,638,501	40,919,514	36,640,901
Transportation equipment	687,913	715,655	765,596
Water and sewer equipment	1,751,913	1,768,627	1,754,861
Orthophotography mapping	11,175	11,175	11,175
Office equipment	<u>580,797</u>	<u>605,663</u>	<u>621,157</u>
Sub Total	124,015,092	121,309,803	107,539,856
Accumulated depreciation	<u>(44,736,214)</u>	<u>(40,512,172)</u>	<u>(36,681,713)</u>
Property Plant & Equipment	79,278,877	80,797,631	70,858,144
Construction in Progress	<u>1,236,180</u>	<u>641,980</u>	<u>4,542,372</u>
Net Property Plant & Equipment	<u>\$ 80,515,057</u>	<u>\$ 81,439,611</u>	<u>\$ 75,400,516</u>

### *Non-current Liabilities and Debt Administration*

As of June 30, 2010, (see Table A-1, page 29) the District had \$49,147,698 in non-current liabilities as compared to fiscal year end 2009 of \$49,445,029.

Bond covenants require that the District maintain and collect rates and charges which together with income are reasonably expected to yield annual net earnings equal to at least the sum of one hundred twenty percent (120%) of annual principal and interest requirements for all revenue bonds outstanding. As shown in the following table, the District is in compliance with the necessary requirements at 140%.

**TABLE A-3**  
**Coverage of Debt Service**

<b>Year Ended June 30,</b>	<b>2010</b>	<b>2009</b>	<b>2008</b>
Net Income(loss) before capital contributions per Financial Statements	(\$1,681,923)	(\$1,439,634)	(\$700,741)
Capacity Fees	242,308	109,037	985,723
Add: Depreciation	4,405,077	3,965,632	3,720,333
Amortization	202,112	206,685	204,689
Interest Expense (Bonds)	2,208,372	1,911,438	1,860,432
Assessments - Debt Service	537,759	508,381	419,060
Less: Property Taxes – Debt Service	(967,418)	(817,751)	(409,292)
Net Earnings Available for Debt Service	\$4,946,286	\$4,443,788	\$6,080,204
Debt Service on Revenue Bonds	3,523,871	\$3,438,347	\$3,441,126
<b>Coverage of Debt Service by Net Earnings</b>	<b>140%</b>	<b>129%</b>	<b>177%</b>
<b>Debt Coverage without Capacity Fees</b>	<b>133%</b>	<b>126%</b>	<b>148%</b>

## Statements of Revenues, Expenses and Changes in Net Assets

While the Balance Sheet shows the change in financial position of net assets, the Statement of Revenues, Expenses, and Changes in Net Assets provides information regarding the nature and source of these changes as presented below:

<b>TABLE A-4</b>							
<b>Hilton Head PSD</b>							
<b>Statement of Revenues, Expenses and Changes in Net Assets and Comparison Schedule</b>							
<b>Year Ended June 30,</b>	<b>2010</b>	<b>2009</b>	<b>2008</b>	<b>2010 to</b>		<b>2009 to</b>	
	<b>Actual</b>	<b>Actual</b>	<b>Actual</b>	<b>2009 Actual</b>	<b>%</b>	<b>2008 Actual</b>	<b>%</b>
				<b>Favorable (Unfavorable)</b>			
Operating Revenues	\$ 10,362,778	\$ 10,144,750	\$ 10,541,875	\$ 218,029	2.1%	\$ (397,125)	-3.8%
Total Non-operating Revenues	<u>2,819,445</u>	<u>2,589,355</u>	<u>2,414,268</u>	<u>230,090</u>	<u>8.9%</u>	<u>175,087</u>	<u>7.3%</u>
Total Revenues	<b>13,182,223</b>	12,734,105	12,956,143	448,119	3.5%	(222,039)	-1.7%
Departmental Expenses	<b>8,048,586</b>	8,089,984	7,871,429	41,397	0.5%	(218,555)	-2.8%
Depreciation	<b>4,405,077</b>	3,965,632	3,720,333	(439,445)	-11.1%	(245,299)	-6.6%
Total Non-operating Expenses	<u>2,410,484</u>	<u>2,118,123</u>	<u>2,065,122</u>	<u>(292,360)</u>	<u>-13.8%</u>	<u>(53,002)</u>	<u>-2.6%</u>
Total Expenses	<u><b>14,864,147</b></u>	<u>14,173,739</u>	<u>13,656,884</u>	<u>(690,407)</u>	<u>-4.9%</u>	<u>(516,856)</u>	<u>-3.8%</u>
Increase (decrease) in net assets before capital contributions	<b>(1,681,923)</b>	(1,439,634)	(700,741)	(242,289)	-16.8%	(738,894)	-105.4%
Capital Contributions:							
Water Capacity Fee	<b>34,512</b>	63,437	434,600	(28,925)	-45.6%	(371,163)	-85.4%
Sewer Capacity Fee	<b>207,796</b>	45,600	551,123	162,196	355.7%	(505,523)	-91.7%
Developer Contributions of Systems	<b>416,411</b>	92,536	1,569,363	323,875	350.0%	(1,476,827)	-94.1%
Sewer Assessments	<u><b>320,902</b></u>	-	-	<u>320,902</u>	<u>N/A</u>	<u>-</u>	<u>N/A</u>
Total Capital Contributions	<u><b>979,621</b></u>	<u>201,573</u>	<u>2,555,086</u>	<u>778,047</u>	<u>386.0%</u>	<u>(2,353,512)</u>	<u>-92.1%</u>
Increase (decrease) in net assets	\$ <b>(702,302)</b>	\$ (1,238,061)	\$ 1,854,345	\$ 535,759	-43.3%	\$ (3,092,406)	-166.8%
Net Assets at the beginning of the year	<u><b>39,265,422</b></u>	<u>40,503,483</u>	<u>38,649,138</u>				
Net Assets at end of year	<u><b>\$ 38,563,120</b></u>	<u><b>\$ 39,265,422</b></u>	<u><b>\$ 40,503,483</b></u>				

## Revenues (Fiscal Year to Year Comparisons)

Operating revenues for fiscal year 2010 total \$10,362,778 which is approximately 79% of total revenues (operating and non-operating) for the year. Total operating revenues have increased 2.1% or \$218,029 compared to last year's revenues mainly due to increased sewer connection fees which were \$115,037 higher than in fiscal year 2009.<sup>5</sup> Total operating revenues decreased 3.8% or \$397,125 from fiscal year 2008 to fiscal year 2009 mainly due to reduced customer growth, increased rainfall and cooler weather.

In addition to higher sewer connection fees, other line items that have contributed to this year's \$218,029 operating revenue increase include the following (see Table A-5, Page 36):

<sup>5</sup> Higher sewer connections fees were caused by Low Pressure connections installed and paid for by grants from Project SAFE and are offset by related higher sewer connection expenses.

- Despite the aforementioned water rate increase, water service revenues have remained relatively flat increasing only \$1,537 due to decreased water/irrigation consumption. The fiscal year 2010 water and irrigation consumption level was nearly 185 million gallons less for commercial and residential customers when compared to fiscal year 2009;
- Sewer service revenues have increased 1.9% or \$74,981;
- Service fees have increased 40% or \$20,178;
- Availability fees have increased 4.2% or \$22,815.

The previously discussed line items that increased operating revenues were partially offset by decreased water tap in fees and decreased golf course irrigation revenue.

Total non-operating revenues were equal to \$2,819,445. The non-operating revenues received by the District were derived primarily from ad valorem property taxes, interest earnings, and tower leases. The District imposed an ad valorem tax of 3.0 mills for operational purposes and 2.82 mills for debt service. The Commission has the authority to set the rates charged for water and sewer services without approval of any other authority, although such rate-setting ability is subject to certain procedural requirements including the holding of public hearings and the posting of public notices.

#### *Departmental Expenses (Fiscal Year to Year Comparisons)*

Total departmental expenses have decreased \$41,399 or 0.5% compared to fiscal year 2009 (See Table A-5, page 36). For fiscal year 2009, departmental expenses increased \$218,555 or 2.8% from fiscal year 2008. The 2009 increase was mainly due to increased payroll and related expenses, administrative costs related to bank/bond administration fees, and rising costs for bio-solids disposal, and fuel and power expenses. The following factors have contributed to this year's decrease:

Purchased water expense decreased \$610,232 or 45% compared to last fiscal year. The main contributing factor to reduced purchased water expense is the RO plant's production of potable water and off-peak rates for BJWSA purchased water.<sup>6</sup> As of June 30, 2010, the O&M expense associated with the RO plant is \$674,039.<sup>7</sup> The following departmental expense items were also reduced when compared to the same period last year.

- Administrative expenses have decreased 0.7% or \$5,141.
- Maintenance expenses have decreased 4.0% or \$32,345.
- Professional fees decreased 34% or \$141,529.
- Vehicle expenses decreased 18% or \$24,087.

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<sup>6</sup> For FY'10, the BJWSA off-peak purchased water price is \$0.75 per 1,000 over the minimum allocation for the months of October through March. The peak rate is \$1.58 for remaining months.

<sup>7</sup> The RO plant became operational in mid-April 2009; therefore it is not practical to compare RO fiscal year 2009 expenses to fiscal year 2010.

These decreased expenses were partially offset by higher operations and water tap in/sewer connection expense items. Operations expense increased 7.9% or \$103,621 mainly due to increased fuel and power expenses. Water tap in/sewer connection expense increased \$120,737 due to higher sewer connection expenses for installations funded via grants through Project SAFE. As previously discussed, these sewer connection expenses are offset by associated sewer connection fee revenue.

TABLE A-5							
Hilton Head PSD							
Statement of Revenues, Expenses and Changes in Net Assets and Budgetary Comparison Schedule							
Year to Date as of June 30, 2010							
(With comparative amounts for the same period in prior fiscal year)				Variance of FY 2010 Actual Data to			
	Fiscal Year 2010		FY 2009	Budget		FY 2009 Actual	
	Actual	Budget	Actual	Dollars	%	Dollars	%
<b>Operating Revenues</b>					<b>Favorable (Unfavorable)</b>		
Water Service	\$ 5,308,798	\$ 5,755,800	\$ 5,307,261	\$ (447,002)	-7.8%	\$ 1,537	0.0%
Sewer Service	4,034,068	4,118,300	3,959,087	(84,232)	-2.0%	74,981	1.9%
Tap In Fees - Water	31,305	30,000	35,133	1,305	4.4%	(3,828)	-10.9%
Connection Fees - Sewer	117,367	2,000	2,330	115,367	N/A	115,037	N/A
Service Fees	70,488	50,000	50,311	20,488	41.0%	20,178	40.1%
Golf Course Irrigation	230,583	325,600	243,274	(95,017)	-29.2%	(12,691)	-5.2%
Availability Fees	570,169	568,700	547,354	1,469	0.3%	22,815	4.2%
<b>Total Operating Revenues</b>	<b>10,362,778</b>	<b>10,850,400</b>	<b>10,144,750</b>	<b>(487,622)</b>	<b>-4.5%</b>	<b>218,028</b>	<b>2.1%</b>
<b>Departmental Expenses</b>							
Payroll & Related	3,166,896	3,083,500	3,165,506	(83,396)	-2.7%	(1,390)	0.0%
Administrative Expenses	754,453	733,100	759,594	(21,353)	-2.9%	5,141	0.7%
Operations	1,410,295	1,324,200	1,306,674	(86,095)	-6.5%	(103,621)	-7.9%
Maintenance	768,575	692,500	800,920	(76,075)	-11.0%	32,345	4.0%
Water Tap In / Sewer Connection Expenses	151,257	25,000	30,520	(126,257)	N/A	(120,737)	N/A
Purchased Water	746,571	600,000	1,356,803	(146,571)	-24.4%	610,232	45.0%
RO Plant O&M	674,039	664,000	127,852	(10,039)	-1.5%	(546,187)	N/A
Professional Fees	269,207	345,000	410,736	75,793	22.0%	141,529	34.5%
Vehicle	107,292	144,500	131,379	37,208	25.7%	24,087	18.3%
<b>Total Departmental Expenses</b>	<b>8,048,585</b>	<b>7,611,800</b>	<b>8,089,984</b>	<b>(436,785)</b>	<b>-5.7%</b>	<b>41,399</b>	<b>0.5%</b>
Depreciation	4,405,077	4,337,000	3,965,632	(68,077)	-1.6%	(439,445)	-11.1%
<b>Total Operating Expenses</b>	<b>12,453,662</b>	<b>11,948,800</b>	<b>12,055,616</b>	<b>(504,862)</b>	<b>-4.2%</b>	<b>(398,046)</b>	<b>-3.3%</b>
<b>Operating income (loss)</b>	<b>(2,090,883)</b>	<b>(1,098,400)</b>	<b>(1,910,866)</b>	<b>(992,483)</b>	<b>-90.4%</b>	<b>(180,018)</b>	<b>-9.4%</b>
<b>Non-operating revenues</b>							
Property taxes-G.O. Debt Levy	967,418	947,400	817,751	20,018	2.1%	149,667	18.3%
Property taxes-Operations Levy	1,028,416	1,010,000	924,702	18,416	1.8%	103,713	11.2%
Rental Income	82,150	95,500	84,496	(13,350)	-14.0%	(2,345)	-2.8%
Interest earned	256,948	310,600	269,950	(53,652)	-17.3%	(13,002)	-4.8%
Tower lease	448,673	451,800	471,303	(3,127)	-0.7%	(22,630)	-4.8%
Other	35,840	17,200	21,153	18,640	108.4%	14,687	69.4%
<b>Total Non-operating Revenues</b>	<b>2,819,445</b>	<b>2,832,500</b>	<b>2,589,355</b>	<b>(13,055)</b>	<b>-0.5%</b>	<b>230,090</b>	<b>8.9%</b>
<b>Non-operating Expenses</b>							
Interest expense-Bonds	2,208,372	2,134,215	1,911,438	(74,157)	-3.5%	(296,933)	-15.5%
Bond Defeasance Amortization	231,716	231,100	231,716	(616)	-0.3%	-	0.0%
Amortization of Debt Expenses	77,093	84,722	81,666	7,629	9.0%	4,573	5.6%
Bond Premium Amortization	(106,697)	(104,100)	(106,698)	2,597	2.5%	(0)	0.0%
<b>Total Non-operating Expenses</b>	<b>2,410,484</b>	<b>2,345,937</b>	<b>2,118,123</b>	<b>(64,547)</b>	<b>-2.8%</b>	<b>(292,361)</b>	<b>-13.8%</b>
<b>Total Non-operating Revenues/Exp.</b>	<b>408,961</b>	<b>486,563</b>	<b>471,232</b>	<b>(77,602)</b>	<b>-15.9%</b>	<b>(62,270)</b>	<b>-13.2%</b>
<b>Increase (decrease) in net assets, before capital contributions</b>	<b>(1,681,923)</b>	<b>(611,837)</b>	<b>(1,439,634)</b>	<b>(1,070,086)</b>	<b>174.9%</b>	<b>(242,289)</b>	<b>-16.8%</b>
Water Capacity Fee	34,512	50,000	63,437	(15,488)	-31.0%	(28,925)	-45.6%
Sewer Capacity Fee	207,796	230,700	45,600	(22,904)	-9.9%	162,196	N/A
Developer Contributions of Systems	416,411	-	92,536	N/A	N/A	323,875	350.0%
Assessments	320,902	-	-	N/A	N/A	N/A	N/A
<b>Total Capital Contributions</b>	<b>979,621</b>	<b>280,700</b>	<b>201,573</b>	<b>698,921</b>	<b>249.0%</b>	<b>457,145</b>	<b>226.8%</b>
<b>Increase (decrease) in net assets</b>	<b>\$ (702,302)</b>	<b>\$ (331,137)</b>	<b>\$ (1,238,061)</b>	<b>\$ (371,165)</b>	<b>-112.1%</b>	<b>\$ 535,759</b>	<b>-43.3%</b>
<b>Net Assets at the beginning of the year</b>	<b>\$ 39,265,422</b>						
<b>Net Assets Year-To-Date</b>	<b>\$ 38,563,120</b>						



*Water and Sewer Revenues/Expenses: Fiscal Year 2010 vs. Fiscal Year 2009.*  
(Please reference Table A-6, Page 38)

**Water Revenues and Related Expenses:**

- For FY'10, total water operating revenues have increased 0.2% or \$9,321 compared to FY'09. As discussed, fiscal year 2010 experienced much lower water consumption levels which resulted in flat revenue growth despite a water rate increase effective October 1, 2009.
- Water departmental expenses decreased 1.9% or \$87,830.
- Water operating loss for fiscal year 2010 is \$1,124,267 and is \$107,630 or 11% lower than fiscal year 2009. This increased loss is due to higher water related depreciation expense.

**Sewer Revenues and Related Expenses:**

- Total sewer and related operating revenues have increased 4.5% or \$208,707 from last fiscal year despite lower sewer related water consumption. This is due to the sewer rate increase which was effective October 1, 2009.
- Sewer departmental expenses increased just 1.3% or \$46,431 compared to last fiscal year.
- Sewer operating loss for fiscal year 2010 is \$966,617, an increased loss of \$72,388 as compared to last fiscal year. This increased loss is due to higher sewer related depreciation expense.

TABLE A-6							
Hilton Head PSD							
Water vs. Sewer Budgetary Comparison Schedule							
Year to Date as of June 30, 2010							
(With comparative amounts for the same period in prior fiscal year)				Variance of FY 2010 Actual Data to			
	Fiscal Year 2010		FY 2009	Budget		FY 2009 Actual	
	Actual	Budget	Actual	Dollars	%	Dollars	%
<b>Operating Revenues</b>							
<b>Water</b>					Favorable	(Unfavorable)	
Service	\$ 5,308,798	\$ 5,755,800	\$ 5,307,261	\$ (447,002)	-7.8%	\$ 1,537	0.0%
Tap In Fees	31,305	30,000	35,133	1,305	4.4%	(3,828)	-10.9%
Service Fees	35,244	25,000	25,156	10,244	41.0%	10,088	40.1%
Availability Fees	107,530	107,200	106,006	330	0.3%	1,524	1.4%
<b>Total Water Operating Revenues</b>	<b>5,482,877</b>	<b>5,918,000</b>	<b>5,473,556</b>	<b>(435,123)</b>	<b>-7.4%</b>	<b>9,321</b>	<b>0.2%</b>
<b>Sewer</b>							
Service	4,034,068	4,118,300	3,959,087	(84,232)	-2.0%	74,981	1.9%
Connection Fees	117,367	2,000	2,330	115,367	N/A	115,037	N/A
Service Fees	35,244	25,000	25,155	10,244	41.0%	10,089	40.1%
Availability Fees	462,639	461,500	441,348	1,139	0.2%	21,291	4.8%
Golf Course Irrigation	230,583	325,600	243,274	(95,017)	-29.2%	(12,691)	-5.2%
<b>Total Sewer Operating Revenues</b>	<b>4,879,901</b>	<b>4,932,400</b>	<b>4,671,194</b>	<b>(52,499)</b>	<b>-1.1%</b>	<b>208,707</b>	<b>4.5%</b>
<b>Total Operating Revenues</b>	<b>10,362,778</b>	<b>10,850,400</b>	<b>10,144,750</b>	<b>(487,622)</b>	<b>-4.5%</b>	<b>218,028</b>	<b>2.1%</b>
<b>Departmental Expenses</b>							
<b>Water</b>							
Payroll & Related	1,456,772	1,480,080	1,456,133	23,308	1.6%	(639)	0.0%
Administrative Expenses	437,583	425,198	440,564	(12,385)	-2.9%	2,982	0.7%
Operations	606,427	569,406	561,870	(37,021)	-6.5%	(44,557)	-7.9%
Maintenance	464,481	358,880	414,043	(105,601)	-29.4%	(50,438)	-12.2%
Water Tap in Expense	23,030	21,395	26,620	(1,635)	-7.6%	3,590	13.5%
Purchased Water	746,571	600,000	1,356,803	(146,571)	-24.4%	610,232	45.0%
RO Plant O&M	674,039	664,000	127,852	(10,039)	-1.5%	(546,187)	N/A
Professional Fees	96,121	141,450	197,889	45,329	32.0%	101,768	51.4%
Vehicle	49,354	66,470	60,434	17,116	25.7%	11,080	18.3%
<b>Total Water Departmental Expenses</b>	<b>4,554,379</b>	<b>4,326,879</b>	<b>4,642,209</b>	<b>(227,500)</b>	<b>-5.3%</b>	<b>87,830</b>	<b>1.9%</b>
<b>Sewer</b>							
Payroll & Related	1,710,124	1,603,420	1,709,373	(106,704)	-6.7%	(750)	0.0%
Administrative	316,870	307,902	319,030	(8,968)	-2.9%	2,160	0.7%
Operations	803,868	754,794	744,804	(49,074)	-6.5%	(59,064)	-7.9%
Maintenance	304,094	333,620	386,877	29,526	8.9%	82,783	21.4%
Sewer Connection Expense	128,227	3,605	3,900	(124,622)	N/A	(124,327)	N/A
Professional Fees	173,086	203,550	212,847	30,464	15.0%	39,761	18.7%
Vehicle	57,938	78,030	70,945	20,092	25.7%	13,007	18.3%
<b>Total Sewer Departmental Expense</b>	<b>3,494,207</b>	<b>3,284,921</b>	<b>3,447,776</b>	<b>(209,286)</b>	<b>-6.4%</b>	<b>(46,431)</b>	<b>-1.3%</b>
<b>Operating Expenses before depreciation</b>	<b>8,048,585</b>	<b>7,611,800</b>	<b>8,089,984</b>	<b>(436,785)</b>	<b>-5.7%</b>	<b>41,399</b>	<b>0.5%</b>
Depreciation - Water	2,052,766	2,021,042	1,847,984	(31,724)	-1.6%	(204,781)	-11.1%
Depreciation - Sewer	2,352,311	2,315,958	2,117,647	(36,353)	-1.6%	(234,664)	-11.1%
<b>Total Operating Expenses</b>	<b>12,453,662</b>	<b>11,948,800</b>	<b>12,055,616</b>	<b>(504,862)</b>	<b>-4.2%</b>	<b>(439,445)</b>	<b>-3.6%</b>
<b>Water Operating income (loss)</b>	<b>(1,124,267)</b>	<b>(429,921)</b>	<b>(1,016,637)</b>	<b>(694,346)</b>	<b>N/A</b>	<b>(107,630)</b>	<b>-10.6%</b>
<b>Sewer Operating income (loss)</b>	<b>(966,617)</b>	<b>(668,479)</b>	<b>(894,229)</b>	<b>(298,138)</b>	<b>-44.6%</b>	<b>(72,388)</b>	<b>-8.1%</b>
<b>Total Operating income (loss)</b>	<b>(2,090,884)</b>	<b>(1,098,400)</b>	<b>(1,910,866)</b>	<b>(992,484)</b>	<b>-90.4%</b>	<b>(180,018)</b>	<b>-9.4%</b>
Non-operating revenues (expenses), net	408,962	486,563	471,232	(77,601)	-15.9%	(62,270)	13.2%
<b>Increase (decrease) in net assets,</b>							
<b>before capital contributions</b>	<b>(1,681,923)</b>	<b>(611,837)</b>	<b>(1,439,634)</b>	<b>(1,070,086)</b>	<b>-174.9%</b>	<b>(242,288)</b>	<b>-16.8%</b>
<b>Capital Contributions</b>	<b>979,621</b>	<b>280,700</b>	<b>201,573</b>	<b>698,921</b>	<b>249.0%</b>	<b>778,047</b>	<b>386.0%</b>
<b>Increase (decrease) in net assets</b>	<b>\$ (702,302)</b>	<b>\$ (331,137)</b>	<b>\$ (1,238,061)</b>	<b>\$ (371,165)</b>	<b>-112.1%</b>	<b>\$ 535,759</b>	<b>-43.3%</b>

## ***Budgetary Highlights***

The District operates on a fiscal year (July 1 – June 30). The budget must be adopted prior to the start of its Fiscal Year. The capital and operating budgets are prepared together and adopted at the same time.

- Operating Revenues: Actual of \$10,362,778 vs. FY'10 Budget of \$10,850,400 represents a variance of \$487,622 or 4.5% less than budget despite an effective 4% water rate increase on water consumed after October 1, 2009. (Refer to page 36, Table A-5) Lower operating revenues are mainly due to lower than average temperatures and the poor economy which has resulted in lower than expected water service revenues and service revenues. As previously discussed, the fiscal year 2010 water and irrigation consumption level was nearly 185 million gallons less for commercial and residential customers when compared to fiscal year 2009.

The District's operating expenses encompass ten (10) separate categories. Departmental expenses account for approximately 65% of the total operating expense budget, with depreciation accounting for the remaining 35%. By category, payroll and related cost accounted for 25%, administration accounted for 6%, operations for 11%, maintenance for 6%, water tap in/sewer connection for 1%, RO operating & maintenance for 5%, purchased water for 6%, and professional fees and vehicles for 3%, for the total of 65% (rounded). Total operating expenses were over budget by 4.2%. The factors contributing to this overage are discussion in more detail below.

- Payroll and Related Expenses: Actual of \$3,166,896 vs. FY'10 Budget of \$3,083,500 is \$83,396 or 2.7% above budget and is mainly due to higher than expected salary and training/education expense. Staffing was budgeted for 38.5 full-time employees.
- Administration Expenses: Actual of \$754,453 vs. FY'10 Budget of \$733,100 is \$21,353 or 2.9% above budget. This variance is mainly due to increased bank and bond administration fees.
- Operations Expenses: Actual of \$1,410,295 vs. FY'10 Budget of \$1,324,200 is \$86,095 or 6.5% greater than budget. This is mainly due to higher than expected costs for operation's power and chemical expenses.
- Maintenance Expenses: Actual of \$768,575 vs. FY'10 Budget of \$692,500 is \$76,075 or 11% higher than budget. Other maintenance expense items that increased include higher SCADA, plant, and hydrant expenses.
- Water Tap in / Sewer Connection Expenses: Actual of \$151,257 vs. FY'10 Budget of \$25,000 is \$126,257 higher than budget. This variance is mainly due to the previously discussed higher sewer connection expenses for installations funded via grants through Project SAFE. These sewer connection expenses are offset by associated sewer connection fee revenue.
- Purchased Water: Actual of \$746,571 vs. FY'10 Budget of \$600,000 is \$146,571 or 24% above budget.
- RO Plant Operation & Maintenance: Actual of \$674,039 vs. FY'10 Budget of \$664,000 represents a variance of \$10,039 or 1.5% above budget. Higher than expected plant and well maintenance expenses were partially offset by lower chemical, power, and quality analysis expenses.

- Professional Fees: Actual of \$269,207 vs. FY'10 Budget of \$345,000 represents a variance of \$75,793 or 22% below than budget.
- Vehicle Expenses: Actual of \$107,292 vs. FY'10 Budget of \$144,500 is \$37,208 or 26% lower than budget. This variance is due to decreased vehicle fuel expense, lower maintenance costs, and lower insurance costs.
- Total Departmental Expenses (excluding depreciation): Actual of \$8,048,585 vs. FY'10 Budget of \$7,611,800 represents a variance of \$436,785 or 5.7% above budget. As discussed, this variance is due to higher than expected increases in payroll, administrative expenses, operations expenses, maintenance expenses, water tap in/sewer connection expenses, purchased water expenses and the RO Plant and maintenance expense line items. The overages for these line items were partially offset by lower than budgeted professional fees and vehicle expense line items.
- Total Non-Operating Revenue: Actual of \$2,819,445 vs. FY'10 Budget of \$2,832,500 represents a variance of \$13,055 or 0.5% under budget. This shortfall is mainly due to lower than expected interest income due to the market turmoil on the United States economy during fiscal year 2010 and lower than expected tower lease and rental income. While these items fell short of budget projections, they were for the mostly offset by higher than expected GO Debt and Operations Levy revenues and other miscellaneous revenue items.
- Total Non-Operating Expenses: Actual of \$2,410,484 vs. FY'10 Budget of \$2,345,937 represents a variance of \$64,547 or 2.8% above budget. This is due to increased bond interest expense.
- Capacity Fees: Actual of \$242,308 vs. FY'10 Budget of \$280,700 represents a variance of \$38,392 below budget. The sewer capacity fee budget was amended to reflect \$130,000 fees financed and collected via Front Foot Assessment and those fees collected for Low Pressure Sewer installed and paid by Project SAFE.
- Developer Contributions of Systems/Assessments: Both developer contributions of systems and assessments are non-budgeted items. The assessments line item has been added due to the new front foot assessment projects in the amount of \$320,902.
- Total Capital Contributions: Actual of \$979,621 vs. FY'10 Budget of \$280,700 represents a variance of \$698,921 above budget. Note: Exclusion of the previously mentioned non-budgeted items results in Actual of \$242,308 vs. Budget of \$280,700 as discussed above under the Capacity Fees' comparison.
- Bond Disclosure: As discussed on page 30, the District is in compliance with necessary requirements.

Fiscal year 2010's decrease in net assets was \$(702,302) which was \$371,165 under the projected decrease in net assets of \$(331,137). This shortfall is mainly attributable to less than expected operating revenues as well as increased operating expenses and non-operating expenses.

## **CONTACTING THE DISTRICT'S FINANCE MANAGER**

This financial report is designed to provide our citizens, customers and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District's Finance Manager, P.O. Box 21264, Hilton Head Island, SC 29925.

## **AUDITED FINANCIAL STATEMENTS**

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT									
BALANCE SHEETS									
AS OF JUNE 30, 2010 AND 2009									
ASSETS						2010		2009	
Current assets									
Cash available for operations						\$ 2,554,900		\$ 2,101,978	
Accounts receivable - trade, net						1,936,011		1,611,742	
Accounts receivable - tower leases						8,820		-	
Sewer assessments, due within one year						335,220		309,916	
Inventory						236,835		221,923	
Prepaid expenses						46,420		85,160	
Total current assets						5,118,206		4,330,719	
Restricted assets									
Cash in banks						1,804,778		1,935,465	
Cash held by Beaufort County Treasurer						574,070		511,523	
Cash held for construction by Beaufort County Treasurer						-		237,140	
Total restricted assets						2,378,848		2,684,128	
Net Property plant and equipment									
Non-depreciable assets						2,323,281		2,263,282	
Depreciable assets, net						78,191,776		79,176,329	
Total property, plant and equipment						80,515,057		81,439,611	
Other assets									
Sewer assessments, due after one year						3,329,883		3,284,197	
Bond and note issuance costs, net						921,962		960,765	
Prepaid expenses, non-current						24,158		32,460	
Total other assets						4,276,003		4,277,422	
Total assets						\$ 92,288,114		\$ 92,731,880	

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HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT									
BALANCE SHEETS									
AS OF JUNE 30, 2010 AND 2009									
LIABILITES AND NET ASSETS							2010		2009
Current liabilities									
Payable from current assets:									
	Accounts payable - trade					\$	534,074	\$	213,002
	Accounts payable - construction						548,353		625,310
	Notes payable, due within one year						18,000		18,000
	Customer deposits						135,010		136,072
	Deferred revenue						143,536		153,522
	Other accrued expenses						409,349		278,763
	Total current liabilities payable from current assets						1,788,322		1,424,669
Payable from restricted assets:									
	Interest payable						530,869		515,135
	Bonds payable, due within one year						1,640,578		1,484,706
	Notes payable, due within one year						617,527		596,919
	Total current liabilities payable from restricted assets						2,788,974		2,596,760
	Total current liabilities						4,577,296		4,021,429
Noncurrent liabilities									
	Bonds payable, due after one year						41,218,772		40,988,459
	Notes payable, due after one year						9,325,117		9,960,643
	Bond discount/premium, net of amortization						956,624		1,063,321
	Deferred loss on early retirement of debt, net of amortization						(2,352,815)		(2,567,394)
	Total noncurrent liabilities						49,147,698		49,445,029
	Total liabilities						53,724,994		53,466,458
Net assets									
	Invested in capital assets, net of related liabilities						29,464,863		30,467,552
	Restricted for capital activity and debt service						2,378,848		2,446,988
	Unrestricted						6,719,409		6,350,882
	Total net assets						38,563,120		39,265,422
	Total liabilities & net assets					\$	92,288,114	\$	92,731,880

The accompanying notes are an integral part of these financial statements

<b>HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT</b>			
<b>STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS</b>			
<b>FOR THE YEARS ENDED JUNE 30, 2010 AND 2009</b>			
	<b><u>2010</u></b>		<b><u>2009</u></b>
<b>Revenues</b>			
Water Service	\$ 5,308,798	\$	5,307,261
Sewer Service	4,034,068		3,959,087
Tap In Fees - water	31,305		35,133
Tap in fees - Sewer	117,367		2,330
Availability charges	570,169		547,354
Service fees and penalties	70,488		50,311
Golf course irrigation	<u>230,583</u>		<u>243,274</u>
Total revenues	10,362,778		10,144,750
<b>Departmental Expenses</b>			
Payroll and related expenses	3,166,896		3,165,506
Administrative expenses	754,453		759,594
Operations expenses	1,410,295		1,306,674
Maintenance expenses	768,576		800,920
RO plant expenses	674,039		127,852
Tap in expenses	151,257		30,520
Purchased water	746,571		1,356,803
Professional fees	269,207		410,736
Vehicle expenses	107,292		131,379
Depreciation	<u>4,405,077</u>		<u>3,965,632</u>
Total departmental expenses	<u>12,453,662</u>		<u>12,055,616</u>
Loss from operations	<u>(2,090,884)</u>		<u>(1,910,866)</u>
<b>Non-operating revenues (expenses)</b>			
Property taxes-debt service	967,418		817,751
Property taxes-operations	1,028,416		924,702
Rental Income	82,150		84,496
Interest earned	256,948		269,950
Tower lease	448,673		471,303
Other revenues	35,679		19,153
Gain on disposal of edquipment	161		2,000
Amortization of bond and note costs	(202,112)		(206,685)
Interest expense	<u>(2,208,372)</u>		<u>(1,911,438)</u>
Total net non-operations loss	408,961		471,232
<b>Decrease) in net assets before capital contriburtions</b>	<b>(1,681,923)</b>		<b>(1,439,634)</b>

The accompanying notes are an integral part of these financial statements

<b>HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT</b>		
<b>STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS</b>		
<b>FOR THE YEARS ENDED JUNE 30, 2010 AND 2009</b>		
	<b><u>2010</u></b>	<b><u>2009</u></b>
<b>Capital contributions</b>		
Assessments	\$ 320,902	\$ -
Capacity fees	242,308	109,037
Developer contributions of systems	<u>416,411</u>	<u>92,536</u>
Total capital contributions	979,621	201,573
Change in net assets	(702,302)	(1,238,061)
Net Assets at the beginning of the year	<u>39,265,422</u>	<u>40,503,483</u>
Net Assets Year-To-Date	<u>\$38,563,120</u>	<u>\$39,265,422</u>

The accompanying notes are an integral part of these financial statements

<b>HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT</b>			
<b>STATEMENTS OF CASH FLOWS</b>			
<b>FOR THE YEARS ENDED JUNE 30, 2010 AND 2009</b>			
	<b><u>2010</u></b>		<b><u>2009</u></b>
<b>Cash flows from operating activities:</b>			
Cash received from customers	\$ 10,025,448		\$ 10,260,090
Cash paid to suppliers and employees	<u>(7,561,099)</u>		<u>(8,118,838)</u>
Net cash provided from operating activities	2,464,349		2,141,252
<b>Cash flows from investing activities</b>			
Change in restricted cash	305,194		3,972,316
Interest earned	<u>256,948</u>		<u>269,950</u>
Net cash provided by investing activities	562,142		4,242,266
<b>Cash flow from noncapital financing activities:</b>			
Property taxes collected - operations	1,028,416		924,702
Tower Lease	442,827		522,515
Sewer Assessment	249,912		364,143
Other nonoperating revenues, net of expenses	<u>113,253</u>		<u>110,961</u>
Net cash provided by noncapital financing activities	1,834,408		1,922,321
<b>Cash flow from capital and related financing activities:</b>			
Capacity fees	242,308		109,037
Property taxes collected - bond sinking fund	967,418		817,751
Interest expense	(2,192,638)		(1,899,159)
Proceeds from revenue bonds	2,328,318		1,958,930
Bond issuance and other capitalized costs	(55,427)		-
Principal payments on bonds and notes	(2,557,050)		(1,995,929)
Proceeds from sale of capital assets	161		2,000
Purchases of property, plant and equipment	<u>(3,141,069)</u>		<u>(9,427,067)</u>
Net cash used by capital and related financing activities	(4,407,978)		(10,434,437)
<b>Net increase in cash</b>	452,922		(2,128,598)
Cash and cash equivalents at beginning of year	<u>2,101,978</u>		<u>4,230,576</u>
Cash and cash equivalents at year end	<u>\$ 2,554,900</u>		<u>\$ 2,101,978</u>

The accompanying notes are an integral part of these financial statements

<b>HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT</b>							
STATEMENTS OF CASH FLOWS							
FOR THE YEARS ENDED JUNE 30, 2010 AND 2009							
					<b><u>2010</u></b>		<b><u>2009</u></b>
<b>Reconciliation of Operating loss to net cash provided by operating activities:</b>							
Operating loss					\$(2,090,884)		\$(1,910,866)
<b>Adjustments to reconcile operating loss to net cash provided by operating activities</b>							
Depreciation					4,405,077		3,965,632
Increase in allowance for doubtful accounts					-		12,000
Write-down of obsolete inventory					-		15,000
Changes in assets and liabilities							
Accounts receivable - trade					(324,269)		107,900
Inventories					(14,912)		72,284
Prepaid assets					38,740		16,138
Accounts payable - trade					321,072		(147,196)
Customer deposits					(1,062)		(4,560)
Other accrued liabilities					130,586		14,920
Net cash provided by operating activities					<u>2,464,349</u>		<u>2,141,252</u>
<u>Schedule of cash and cash equivalents</u>							
Available for operations							
Demand deposits (interest and non-interest bearing)					\$ 2,385,606		\$ 2,065,165
Held by Beaufort County Treasurer					169,294		36,813
					<u>\$ 2,554,900</u>		<u>\$ 2,101,978</u>
<u>Supplemental Disclosures</u>							
Noncash financing activities:							
Developer contribution of systems					\$ 416,411		\$ 92,536

The accompanying notes are an integral part of these financial statements

## **NOTES TO FINANCIAL STATEMENTS**

## **Note 1 - Summary of significant accounting policies**

### **General**

The Hilton Head No. 1 Public Service District was established in November of 1969. Its purpose is to provide water and sewer services to the public within designated boundaries.

The financial statements of the District have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The more significant of the government's accounting policies are described below:

The District applies all relevant GASB pronouncements. The District applied all relevant Financial Accounting Standards Board (FASB) Statements and Interpretations and Accounting Principles Board (APB) Opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. Based on provisions in GASB Statement 20, the District has elected to apply all FASB Statements and Interpretations issued after November 30, 1989, except those that conflict with or contradict GASB pronouncements.

These GASB statements require the presentation of Management's Discussion and Analysis which precedes the financial statements, in addition to several changes to the financial statements such as: 1) the classification of the Equity section of the balance sheet into Net Assets with categories of Invested in Capital Assets net of related debt, Restricted, and Unrestricted; 2) the statement of revenues, expenses and changes in net assets formatted to report changes in net assets in lieu of changes in retained earnings; and 3) additional note disclosures to the financial statements.

### **Fund accounting**

The accounts of the District are organized on the basis of a proprietary fund type - enterprise fund. The fund is accounted for by a set of self-balancing accounts that comprise its assets, liabilities, net assets, and revenues and expenses. The fund is established to account for water and sewer operations that are financed and operated in a manner similar to private business enterprises, where the intent is to provide goods and services to the general public on a continuing basis financed and recovered primarily through user charges.

### **Net assets**

Net assets comprise the various net earnings from operating and non-operating revenues, expenses and contributions of capital. Net assets are classified in the following three components: invested in capital assets, net of related debt; restricted for capital activity and debt service; and unrestricted net assets.

Invested in capital assets, net of related debt, consists of all capital assets, net of accumulated depreciation and reduced by outstanding debt that is attributable to the acquisition, construction and improvement of those assets; debt related to unspent proceeds of other restricted cash and investments is excluded from the determination. Restricted for capital activity and debt service consists of net



## **Note 1 - Summary of significant accounting policies (continued)**

### **Net assets (continued)**

assets for which constraints are placed thereon by external parties, such as lenders, grantors, contributors, laws, regulations and enabling legislation, including self-imposed legal mandates, less any related liabilities. Unrestricted consists of all other net assets not included in the above categories.

### **Basis of accounting**

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. The proprietary fund type is reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when the related liabilities are incurred.

Property taxes and availability charges are recognized when collected by the Beaufort County Treasurer.

Fees and payments due under developer contracts are treated as capital contributions and are recognized in the period received. Tap fees and connection fees are recognized as income in the period the customer connects to the system.

### **Cash and cash equivalents**

The District considers both restricted and unrestricted demand deposits and money market accounts to be cash equivalents. In addition, all highly liquid investments, including repurchase agreements, with original maturities of three months or less from the date of purchase are considered to be cash equivalents.

### **Accounts receivable, allowance for doubtful accounts and bad debt expense**

The District carries accounts receivable at cost less an allowance for doubtful accounts. Management charges off to expense any balances that are determined to be uncollectible. At June 30, 2009 and 2010, the balance of the allowance for doubtful accounts was \$12,000. Bad debt expense for the years ended June 30, 2010 and 2009 were \$55,989 and \$35,512, respectively.

### **Inventory**

Inventory is recorded at the lower of cost or market on a weighted average cost basis.

### **Property, plant and equipment**

Property, plant and equipment are recorded at cost when constructed or purchased. Assets contributed to the District by developers are capitalized at the developers' cost to construct the water and sewer system. Betterments and improvements over \$1,000 which extend the useful life of an asset are capitalized and depreciated over their estimated useful life.

Repairs and maintenance are charged to expense as incurred. During the period of construction, construction period interest in excess of the interest earned on bond proceeds is capitalized into the

## **Note 1 - Summary of significant accounting policies (continued)**

### **Property, plant and equipment (continued)**

project which is being financed from the bond proceeds. For the year ended June 30, 2009, \$364,670 of interest was capitalized. No interest was capitalized for the year ended June 30, 2010.

Depreciation of all property, plant and equipment is provided by the straight-line method and estimated useful lives of assets in service are as follows:

Description	Estimated life (in years)
Waterworks system	5-40
Shop furniture and equipment	5-7
Sewage disposal system	5-33
Building	40
Sewage treatment facilities	3-40
Transportation equipment	5
Water and sewer equipment	3-7
Orthophotography mapping	5
Office equipment	4-10

### **Bond issuance cost**

Bond issuance costs are amortized using the straight-line method over the life of the bonds commencing at the date of issuance. Amortization expense on bond issuance costs was \$77,093 and \$81,666 for the years ended June 30, 2010 and 2009, respectively.

### **Bond discount and premium**

The issue price of the 2004 revenue bonds exceeded its par value resulting in a bond premium of \$1,669,539. The bond premium is being amortized over the 17-year life of the 2004 revenue bonds. The 2006 revenue bonds included two series of bonds, one issued at a premium of \$40,990 and one issued at a discount of \$197,849. The 2007 general obligation bonds included two series of bonds, one issued at a premium of \$108,661 and one issued at a discount of \$8,471. The net unamortized bond premium as of June 30, 2010 and 2009, was \$956,624 and \$1,063,321, respectively.

### **Use of estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

## **Note 1 - Summary of significant accounting policies (continued)**

### **Compensated absences**

The District accounts for compensated absences by accruing a liability for future absences according to the guidelines of GASB Statement No. 16, Accounting for Compensated Absences, which amounted to \$210,919 and \$187,611 at June 30, 2010 and 2009, respectively.

### **Reclassification**

Certain accounts and amounts in the June 30, 2009 financial statements have been reclassified in order to conform to the June 30, 2010 presentation.

### **Date of Management's Review**

In preparing the financial statements, the District has evaluated events and transactions for potential recognition or disclosure through December 2, 2010, the date that the financial statements were available to be issued.

## **Note 2 – Cash, cash equivalents and investments**

At June 30, 2010, the bank balances of unrestricted and restricted accounts totaled \$4,135,867 and had a carrying balance totaling \$4,190,184. A sum of \$200 is held in petty cash funds of the District.

Custodial credit risk is the risk that, in the event of failure of a financial institution, the District will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. As of June 30, 2010, none of the District's deposits or investments were exposed to custodial credit risk. The amounts covered by federal depository insurance (FDIC), invested in money market accounts and collateralized were as follows:

	Unrestricted	Restricted under bond covenants	Total
FDIC insured	\$ 250,000	\$ -	\$ 250,000
Collateralized	2,081,089	1,804,778	3,885,867
Balance per bank at 6/30/2010	<u>\$ 2,331,089</u>	<u>\$ 1,804,778</u>	<u>\$4,135,867</u>

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The District's investment policy limits investments to those that are very creditworthy. At June 30, 2010, the District's investments were all in a Standard and Poor's AAAM rated money market account that is collateralized by U.S. Treasury obligations. As of June 30, 2010 and 2009 all investments of the District were redeemable on demand without penalty and are, therefore, classified as cash and cash equivalents.

Concentration of credit risk is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. The district's investment policy does not address this risk.

## **Note 2 – Cash, cash equivalents and investments (continued)**

### **Investment Policy**

The District's cash management program seeks to achieve three objectives with regards to investments: safety of principal, adequate liquidity to meet daily cash needs, and a reasonable yield commensurate with the preservation of principal and liquidity. The following investment strategy has been designed to accomplish these objectives:

1. The District will invest in very creditworthy, highly liquid investments with maturities of one year or less and in intermediate-term securities of high credit quality with maturities no greater than five years. The District will only invest in those securities specified under South Carolina Code Section 6-5-10. These include collateralized money market accounts and certificates of deposits, U.S. Treasury Bills and Notes, high quality obligations of certain U.S. agencies and instrumentalities, and the local government investment pool.
2. The primary objective of all District investment activity is the preservation of capital and safety of principal. Each investment transaction shall ensure that capital losses are avoided, whether from security default, sale of instruments prior to maturity or erosion of market value.
3. At all times, the District shall remain sufficiently liquid to meet cash flow requirements by matching investment maturities with forecasted cash flow requirements, investing in securities with active secondary markets, and maintaining appropriate portfolio diversification.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of investments. There may be times when the District has more or less of its funds in particular investment vehicles due to cash flow needs, prevailing market conditions, and other factors. Analyzing monthly financial reports in conjunction with prevailing market conditions serve as a general guideline for making investment decisions. In this way, the portfolio will be able to take advantage of rising interest rates by re-investing maturing securities at higher yields. In falling rate environments, it will profit from having investments that were made at higher rates. Following this discipline ensures that the District will always have sufficient cash available for daily needs, preserve its principal, and earn a competitive yield without assuming unacceptable risks.

### **Note 3 - Cash held by the Beaufort County Treasurer**

Cash held by the Beaufort County Treasurer includes the remaining proceeds of the general obligation bond issues, property tax collections and interest earned on monies held by the Treasurer.

The funds will be used as follows:

	As of June 30,	
	2010	2009
Unrestricted cash - Available for general operating purposes	\$ 169,294	\$ 36,813
Restricted cash - Available for construction	-	237,140
Restricted cash - Bond principal retirement and interest payments	574,070	511,523
Total	<u>\$ 743,364</u>	<u>\$ 785,476</u>

The deposits are a pool of funds invested by the pool for the entities which receive property taxes from the County Treasurer. As such, collateral is not identified for each deposit, but rather for the fund as a whole. These deposits are collateralized by cash or governmental agency securities, which are fully guaranteed as to principal and interest by the federal government.

### **Note 4 - Accounts receivable-trade**

Accounts receivable include the following:

	As of June 30,	
	2010	2009
Receivable from customers	\$ 1,011,987	\$ 811,094
Unbilled receivables from customers	889,397	761,886
Other receivables	34,627	38,762
Total	<u>\$ 1,936,011</u>	<u>\$ 1,611,742</u>

### **Note 5 - Property, plant, equipment and depreciation**

Capital asset activity during the year ended June 30, 2010 and 2009 was as follows:

	June 2009	Additions	Disposals	Transfers	June 2010
<u>Nondepreciable capital assets</u>					
Land	1,266,629	60,000	\$ -	\$ -	1,326,629
Wetlands discharge system	996,653	-	-	-	996,653
	2,263,282	60,000	-	-	2,323,282
<u>Depreciable capital assets:</u>				-	
Waterworks system	49,500,248	3,850	-	1,180,079	50,684,177
Shop furniture and equipment	98,412			-	98,412
Sewage disposal system	25,416,505	416,411	-	1,116,670	26,949,586
Buildings	4,289,335	-	-	-	4,289,335
Sewage treatment facilities	36,640,901	-	(2,400)	-	36,638,501
Transportation equipment	715,655	33,324	(61,066)	-	687,913
Water and sewer equipment	1,768,627	62,634	(79,348)	-	1,751,913
Orthophotography mapping	11,175	-	-	-	11,175
Office equipment	605,663	13,355	(38,220)	-	580,798
	119,046,521	529,574	(181,034)	2,296,749	121,691,810
Accumulated depreciation	(40,512,172)	(4,405,077)	181,034		(44,736,215)
Construction in progress	641,980	2,890,949	-	(2,296,749)	1,236,180
Sub Total	79,176,329	(984,554)	-	-	78,191,775
	-				-
Year End Totals	81,439,611	\$ (924,554)	\$ -	\$ -	80,515,057
	June 2008	Additions	Disposals	Transfers	June 2009
<u>Nondepreciable capital assets</u>					
Land	1,141,629	125,000	\$ -	\$ -	1,266,629
Wetlands discharge system	996,653	-	-	-	996,653
	2,138,282	125,000	-	-	2,263,282
<u>Depreciable capital assets:</u>				-	
Waterworks system	37,260,024	42,537	-	12,197,687	49,500,248
Shop furniture and equipment	98,412			-	98,412
Sewage disposal system	23,979,989	50,000	-	1,386,516	25,416,505
Buildings	4,269,460	-	-	19,875	4,289,335
Sewage treatment facilities	36,640,901	-	-	-	36,640,901
Transportation equipment	765,596	59,263	(109,204)	-	715,655
Water and sewer equipment	1,754,861	16,287	(2,521)	-	1,768,627
Orthophotography mapping	11,175	-	-	-	11,175
Office equipment	621,157	7,954	(23,448)	-	605,663
	105,401,575	176,041	(135,173)	13,604,078	119,046,521
Accumulated depreciation	(36,681,713)	(3,965,632)	135,173		(40,512,172)
Construction in progress	4,542,372	9,703,686	-	(13,604,078)	641,980
Sub Total	73,262,234	5,914,095	-	-	79,176,329
					-
Year End Totals	75,400,516	\$ 6,039,095	\$ -	\$ -	81,439,611

#### **Note 5 - Property, plant, equipment and depreciation (continued)**

Depreciation expense for the years ended June 30, 2010 and 2009 was \$4,405,077 and \$3,965,632, respectively. Transfers relate to construction in progress completed during the year.

#### **Note 6 – Long-term obligations**

The District has financed its acquisitions of property, plant and equipment through bond issuances and notes payable as follows:

##### **Notes payable**

The District is obligated under a note dated November 30, 1988, with a balance of \$223,939 and \$241,969 at June 30, 2010 and 2009, respectively, payable to the South Carolina Jobs-Economic Authority (Authority). The proceeds of the note were for expansion of water lines within the District. The note is without interest, payable at \$1,500 per month. Since this obligation was acquired pursuant to the purchase of an existing utility system, the Authority may have the right to renegotiate the terms of the note, including the interest rate and maturity date.

On May 26, 2000, the district entered into a loan agreement with the South Carolina Water Quality Revolving Fund Authority in the amount of \$10,194,238 for the purpose of expanding the wastewater treatment plant capacity by 3,200,000 gallons per day. The note is an obligation of the District, bears interest at the rate of 3.50 percent, and is payable quarterly through September 2021 in the amount of \$177,724, which includes interest, from revenues derived from operation of the District's system, and is secured by a lien upon these revenues. The balance of this note payable was \$6,587,376 and \$7,057,386 at June 30, 2010 and 2009, respectively.

On April 14, 2008 the District executed a loan with the South Carolina State Infrastructure Revolving Loan Fund (SIRF) in the amount of \$481,080 at an interest rate of 3.50% per annum. The proceeds of this loan were used only to pay the costs of constructing new water wells. Principal and interest of \$8,387 are payable quarterly beginning January 1, 2009 through October 1, 2028. The SIRF loan balance outstanding at June 30, 2010 and 2009 amounted to \$451,058 and \$468,437, respectively.

On October 3, 2008, the District finalized a State Revolving Fund (SRF) loan in the amount of \$2,887,826 at an interest rate of 3.99% per annum. (See note 7) These funds were used as part of the financing for the new reverse osmosis plant. Principal and interest of \$48,135 are payable quarterly beginning January 1, 2009 through October 1, 2028. The SRF loan balance outstanding at June 30, 2010 and 2009 amounted to \$2,698,270 and \$2,807,800, respectively.

## **Note 6 – Long-term obligations (continued)**

### **Bonds payable**

In May 2000, the District issued \$530,000 of Series 2000B revenue bonds for purposes of funding certain improvements within the District. The bonds were an obligation of the District, bore interest at the rate of 6.172% and were payable annually through May, 2020 in the amount of \$46,856, which included interest. The bonds will be repaid by annual assessments to the owners in the Burkes Beach area over a 20 year period and will be collected by the county treasurer. The 2000B revenue bonds outstanding at June 30, 2009 amounted to \$366,316. In June 2010, the District made a \$342,069 payment to pay off these bonds. After the pay off, \$190,722 of these bonds were refinanced as series 2010A revenue bonds. The series 2010A bonds bear interest at a rate of 3.85% per annum. The first payment of principal and interest in the amount of \$23,219 is due March 26, 2011. Nine additional payments of principal and interest of \$23,301 are payable on March 26<sup>th</sup> of each year beginning in 2012 and continuing until 2020. The 2010A revenue bonds outstanding amounted to \$190,722 at June 30, 2010.

In April 2004, the District determined that a debt service savings could be achieved by issuing a series of 2004 revenue bonds in the amount of \$17,575,000 and applying the proceeds thereof to refund a portion of the callable maturities of the 1995 revenue bonds and all of the callable maturities of the 1996 revenue bonds. The 2004 revenue bonds bear varying interest rates of between 2% to 5%, and are payable semi-annually beginning August 1, 2004 through August 1, 2021. The 2004 revenue bonds outstanding amounted to \$14,640,000 and \$15,350,000 at June 30, 2010 and 2009, respectively.

In August 2004, the District completed the issuance of series 2004B revenue bonds for \$430,000. The proceeds of the bonds are to be used first for funding the debt service requirement and the issuance costs of the bond. Proceeds are then to be used to reimburse the District for the cost of system improvements. A one time principal payment was made in September 2004 of \$103,978. Beginning May 2, 2005, the remaining balance of \$326,022 will be paid with 19 annual payments of \$26,275 which includes interest at a rate of 5.19% per annum. A final payment of \$26,126, including interest, is due on May 2, 2024. The bonds are payable from revenues derived from operation of the District's system, and are secured by a lien upon these revenues. The 2004B bonds outstanding amounted to \$256,883 and \$269,186 at June 30, 2010 and 2009, respectively.

On February 2, 2006 the District issued \$18,770,000 of Series 2006 revenue bonds to refund the series 1998 revenue bonds in order to achieve savings on debt service. Interest on the bonds is payable semi-annually at varying interest rates of between 3.50% and 4.125% per annum. Principal payments are due annually on December 1<sup>st</sup> of each year beginning in 2006 and continuing until 2023. The bonds are payable from revenues derived from operation of the District's system, and are secured by a lien upon these revenues. The 2006 bonds outstanding amounted to \$18,105,000 and \$18,535,000 at June 30, 2010 and 2009, respectively.



## **Note 6 – Long-term obligations (continued)**

### **Bonds payable (continued)**

In June 2007, the District issued \$930,000 of series 2007 revenue bonds. Proceeds are to be used to defray the costs of system improvements. The series 2007 bond bears interest at a rate of 4.22% per annum. Principal and interest of \$69,771 are payable on June 20<sup>th</sup> of each year beginning in 2008 and continuing until 2027. The bonds are payable from revenues derived from operation of the District's system, and are secured by a lien upon these revenues. The 2007 revenue bonds outstanding amounted to \$834,507 and \$867,663 at June 30, 2010 and 2009, respectively.

On October 3, 2007 the District issued \$7,350,000 of general obligation bonds. Proceeds are to be used to defray the cost of constructing, furnishing and equipping a new water well and reverse osmosis plant. Interest on the bonds is payable semi-annually beginning March 1, 2008 at varying interest rates of between 4.50% and 4.00% per annum. Principal payments on the bonds are due annually beginning March 1, 2009 through March 1, 2027. The 2007 general obligation bonds outstanding amounted to \$6,810,000 and \$7,085,000 at June 30, 2010 and 2009, respectively.

In July 2009, the District issued \$335,902 of series 2009A revenue bonds. Proceeds are to be used to defray the costs of system improvements. The series 2009A bond bears interest at a rate of 4.55% per annum. Principal and interest of \$33,254 are payable on June 30<sup>th</sup> of each year beginning in 2010 and continuing until 2024. The bonds are payable from revenues derived from operation of the District's system, and are secured by a lien upon these revenues. The 2009A revenue bonds outstanding amounted to \$355,902 at June 30, 2010.

In July 2009, the District issued \$1,781,694 of general obligation bonds. Proceeds are to be used to defray the cost of constructing, furnishing and equipping a new water well and reverse osmosis plant. The bonds bear interest at a rate of 4.219% per annum. The first payment of principal and interest in the amount of \$159,413 was due March 1, 2010. Fourteen additional payments of principal and interest of \$160,040 are payable on March 1<sup>st</sup> of each year beginning in 2011 and continuing until 2024. The 2009 general obligation bonds outstanding amounted to \$1,666,338 at June 30, 2010.

Maturities and debt service costs of bonds and notes payable are as follows:

Years ended June 30,	Principal	Interest	Total
2011	\$ 2,276,105	\$ 2,139,884	\$ 4,415,989
2012	2,369,418	2,052,716	4,422,134
2013	3,039,099	1,949,478	4,988,577
2014	3,169,873	1,823,091	4,992,964
2015	3,306,782	1,685,182	4,991,964
2016 - 2020	19,235,269	6,107,741	25,343,010
2021 - 2025	17,535,534	1,907,002	19,442,536
2026 - 2027	1,887,914	110,413	1,998,327
	<u>\$ 52,819,994</u>	<u>\$ 17,775,507</u>	<u>\$ 70,595,501</u>

**Note 6 – Long-term obligations (continued)**

Bonds with varying interest rates at June 30, 2010 are as follows:

For those bonds due June 30,	Revenue bonds dated April 13, 2004	Revenue bonds dated Feb. 2, 2006	General Obligation bonds dated Oct. 3, 2007
2011	4.00%	3.50%	4.375%
2012	4.00%	3.50%	4.125%
2013	4.25%	3.50%	4.00%
2014	5.00%	3.625%	4.00%
2015	5.00%	3.625%	4.00%
2016	5.00%	3.75% - 4.00%	4.00%
2017 - 21	5.00%	4.00%	4.00%
2022	-	4.00%	4.00%
2023	-	4.10%	4.00%
2024	-	4.125%	4.00%
2025 - 27	-	-	4.00%

## **Note 7 – Non-current liabilities**

The non-current liability activity during fiscal years 2010 and 2009 was as follows:

	June 30, 2009	Additions	Reductions	June 30, 2010	Amounts due within one Year
Revenue bonds	\$ 35,388,165	\$ 546,624	\$ (1,551,775)	\$ 34,383,014	\$ 1,275,841
GO bonds	\$ 7,085,000	1,781,694	(390,356)	8,476,338	364,737
Notes payable	\$ 10,575,562	-	(614,919)	9,960,643	635,527
Advances for construction	\$ -	-	-	-	-
Bond discount/premium	\$ 1,063,321	-	(106,698)	956,623	-
Less deferred amount	\$ (2,567,394)	-	214,579	(2,352,815)	-
Noncurrent liabilities	\$ 51,544,654	\$ 2,328,318	\$ (2,449,169)	\$ 51,423,803	\$ 2,276,105
Less current portion	(2,099,625)			(2,276,105)	
	<u>\$ 49,445,029</u>			<u>\$ 49,147,698</u>	

	June 30, 2008	Additions	Reductions	June 30, 2009	Amounts due within one Year
Revenue bonds	\$ 36,554,511	\$ -	\$ (1,166,346)	\$ 35,388,165	\$ 1,209,706
GO bonds	7,350,000	-	(265,000)	7,085,000	275,000
Notes payable	7,771,239	3,368,906	(564,583)	10,575,562	614,919
Advances for construction	1,409,976	-	(1,409,976)	-	-
Bond discount/premium	1,170,019	-	(106,698)	1,063,321	-
Less deferred amount	(2,799,111)	-	231,717	(2,567,394)	-
Noncurrent liabilities	\$ 51,456,634	\$ 3,368,906	\$ (3,280,886)	\$ 51,544,654	\$ 2,099,625
Less current portion	(1,903,260)			(2,099,625)	
	<u>\$ 49,553,374</u>			<u>\$ 49,445,029</u>	

## **Note 8 - Defeased debt**

On June 1, 1995, the District issued revenue bonds amounting to \$23,395,000 with varying interest rates to advance refund general obligation bonds amounting to \$125,000 and revenue bonds amounting to \$6,045,000 which had varying interest rates. The general obligation bonds were set to mature in 1998, and the revenue bonds were set to mature in 2012. Part of the proceeds of the new revenue bond issue was used to purchase funds within an irrevocable trust with an escrow agent to provide debt service payments until the previously existing debt issues are retired. The advance refunding met the requirements of an in-substance debt defeasance, and those bonds were removed from the books of the District. As a result of the advance refunding, the District is amortizing the deferred loss on early retirement of \$630,489 over a period of the original issue of the related bond issues, which ranges from two to seventeen years. The unamortized balance at June 30, 2010 and 2009 was \$70,144 and \$106,873, respectively.

## **Note 8 - Defeased debt (continued)**

In April 2004, the District issued revenue bonds amounting to \$17,575,000 with varying interest rates to advance refund a portion of the 1995 and 1996 revenue bonds amounting to \$18,110,000 which had varying interest rates. The 1995 bond previously refunded general obligation and revenue bonds totaling \$6,170,000. The 1995 and 1996 revenue bonds were set to mature in 2020 and 2016, respectively. Part of the proceeds of the new revenue bond issue were used to purchase funds within an irrevocable trust with an escrow agent to provide debt service payments on the previously existing debt issues.

The 2004 advance refunding met the requirements of an in-substance debt defeasance, and those bonds were removed from the books of the District. As a result of the advance refunding, the District reduced its total debt service requirements by \$1,906,345, which resulted in an economic gain (difference between the present value of the debt service payments on the old and new debt) of \$1,232,494. The District is amortizing the deferred loss on early retirement of \$2,234,714 over the 17-year average life of the refunded bonds. The unamortized balance at June 30, 2010 and 2009 was \$1,413,128 and \$1,544,580, respectively.

On February 2, 2006 the District issued revenue bonds amounting to \$18,770,000 with varying interest rates to advance refund series 1998 revenue bonds amounting to \$17,825,000 of principal which were to mature in 2024. Part of the proceeds of the new revenue bond issuance was used to purchase funds within an irrevocable trust with an escrow agent to provide debt service payments on the previously existing debt issues.

The 2006 advance refunding met the requirements of an in-substance debt defeasance, and those bonds were removed from the books of the District. As a result of the advance refunding, the District reduced its total debt service requirements by \$1.28 million, which resulted in an economic gain (difference between the present value of the debt service payments on the old and new debt) of \$886,805. The District is amortizing the deferred loss on early retirement of \$1,133,015 over the 18-year life of the refunded bonds. The unamortized balance at June 30, 2010 and 2009 was \$852,407 and \$915,941, respectively.

In June 2010, the District issued revenue bonds amounting to \$190,722 with varying interest rates to advance refund series 2000B revenue bonds amounting to \$530,000 of principal which were to mature in 2020. Part of the proceeds of the new revenue bond issuance was used to purchase funds within an irrevocable trust with an escrow agent to provide debt service payments on the previously existing debt issues.

The 2010 advance refunding met the requirements of an in-substance debt defeasance, and those bonds were removed from the books of the District. As a result of the advance refunding, the District reduced its total debt service requirements by \$84,295, which resulted in an economic gain (difference between the present value of the debt service payments on the old and new debt) of \$35,268. The District is amortizing the deferred loss on early retirement of \$17,137 over the 10-year life of the refunded bonds. The unamortized balance at June 30, 2010 was \$17,137.

### **Note 9 – Restricted Assets**

A reserve fund for debt service is mandated by bond covenants. At June 30, 2010 and 2009 the debt service reserves totaled \$2,378,849 and \$2,446,988, respectively.

The District also has funds established, as mandated by bond covenants, for operation and maintenance, and depreciation and contingencies. The operating and maintenance fund is intended to provide for the payment of the operations and maintenance expenses. The depreciation and contingency fund is intended to provide a reasonable reserve for the depreciation of the system, for contingencies and for improvements, betterment and extensions of the system.

At June 30, 2010 and 2009 the District had \$0 and \$237,140 held by the Beaufort County Treasurer remaining from the October 3, 2007 note issuance. Use of these funds is restricted for constructing, furnishing and equipping a new water well and reverse osmosis plant.

### **Note 10 - Lease arrangements**

The District is currently leasing office space, land use and space on its water tower facilities to various cellular phone companies for attachment of antennae. Original lease terms range from one to five year periods, with renewal options. Rental income in connection with these leases was \$448,673 and \$471,303 for the years ended June 30, 2010 and 2009, respectively.

The future minimum lease income is as follows:

Years ended June 30,	Amount
2011	493,329
2012	473,570
2013	299,259
2014	161,969
2015	148,073
Thereafter	65,094
Total	<u>\$ 1,641,294</u>

### **Note 11 - Economic dependence**

The District has a service area that is located within the geographic boundaries of Hilton Head Island, South Carolina. A change in the overall economic conditions of this geographic area may have a significant influence upon the operating results of the District.

## **Note 12 - Construction and development commitments**

### **Policy**

The District has financed a portion of its expansion through direct charges to developers and through governmental grants. Developers basically install the systems within a given area or contribute toward treatment plant or water production facilities in exchange for a portion of the capacity. All systems contributed must be approved by the District and are contributed, generally without cost to the District, once they are completed and acceptable for use.

### **Regulatory mandates**

The District, as well as some other water authorities on Hilton Head Island, South Carolina, has entered into contracts for additional water supply sources to meet its future needs due to restrictions placed on the District by the South Carolina Department of Health and Environmental Control. The restrictions and contract for water supply have a significant financial impact on the District.

During the years ended June 30, 1998 and June 30, 2003, the District signed agreements with Beaufort Jasper Water & Sewer Authority (BJWSA) to provide an additional water supply for the District's service area. Since completion of the water supply construction, the District is required under the agreement to purchase a minimum amount of water per day, based upon BJWSA's operation and maintenance cost for providing the water. Purchases from BJWSA amounted to \$746,571 and \$1,356,803 for the years ended June 30, 2010 and 2009, respectively.

### **Expansion**

As part of an overall funding plan for expansion of the District's present facilities, the District has entered into various contracts with developers and others. Under these contracts, contributions of capital assets valued at \$416,411 and \$92,536 and payments of capacity fees totaling \$242,308 and \$109,037 were collected during the fiscal years ended June 30, 2010 and 2009, respectively.

All developer contract commitments entered into prior to the current expansion program have been substantially met. The District extended its boundaries to include those undeveloped areas on the northern part of the island under developer contracts. The cost of expansion is allocated to the developers based upon capacity requested. The infrastructure necessary to connect or serve the developers' property will be constructed by the developers and contributed to the District at no cost to the District.

### **Construction commitments**

The District has approximately \$6,503,000 of commitments remaining on construction contracts entered into prior to June 30, 2010.

### **Note 13 - Sewer assessments**

The District has constructed various sewer systems, the cost of which is to be repaid by annual sewer assessments collected by the County treasurer from the property owners that benefited from these systems. These assessments are being collected annually and are expected to be paid in full beginning 2016 through 2026. Assessments receivable totaled \$3,665,103 and \$3,594,113 as of June 30, 2010 and 2009, respectively. A portion of the annual receipts is recognized as interest income each year. For the years ended June 30, 2010 and 2009, \$212,894 and \$215,309, respectively, of the assessments collected was recognized as interest income.

### **Note 14 - Deferred compensation plans**

#### **Section 457 plan**

In April 2004, the District reactivated its Internal Revenue Code Section 457 retirement plan. All persons employed by the District on March 31, 2004 became eligible employees. Under the Plan, all participants make a minimum of 6% salary reduction contribution as elected in his or her salary deferral agreement. The District makes a 6% matching contribution to each eligible participant's account. Employee contributions for the years ended June 30, 2010 and 2009 were \$141,087 and \$118,516, respectively. The matching contribution for the years ended June 30, 2010 and 2009 was \$19,554 and \$22,098, respectively.

#### **South Carolina Retirement System**

Effective April 2004, the District also joined the South Carolina Retirement System (SCRS). SCRS is a cost sharing multiple employer defined benefit retirement plan for employees of the state and its public school districts, counties, cities, and other political subdivisions that elect participation. SCRS provides members a guaranteed monthly pension based on a formula that includes the member's average final compensation, years of service, and a benefit multiplier.

As a condition of employment, all employees are required to become members of the SCRS and contribute 6.5% of compensation. However, employees who worked for the District on the date of its admission into the Retirement System could elect non-membership within six-months. The District's required contributions for the years ended June 30, 2010, 2009 and 2008 were 9.24%, 9.24% and 9.06%, respectively. The District's matching contribution for the years ended June 30, 2010, 2009 and 2008 were \$174,808, \$162,108 and \$143,827 respectively. For each of the years, the District contributed 100% of the required contribution to the SCRS.

For the years ended June 30, 2010, 2009 and 2008, \$1,891,868, \$1,755,623, and \$1,587,492, respectively, of wages were subject to retirement. During the years ended June 30, 2010, 2009 and 2008, \$122,672, \$114,115, and \$103,183, respectively, were contributed to the system for the employees' share which represented 6.50% of covered payroll for each of those years.

## **Note 14 - Deferred compensation plans (continued)**

### **South Carolina Retirement System (continued)**

Employees are vested after 5 years and are entitled to a deferred annuity commencing at age 60. Employees who retire at age 65 with 5 years of service and have twenty-eight years of credited service are entitled to a retirement benefit, payable monthly for life equal to 1.82% of average final compensation times years of credited service. Employees who retire between the ages of 55 and 60 with 25 years of service receive an annuity reduced by 4% for each year of service under twenty-eight. Employees who retire at age 60 receive an annuity reduced by 5% for each year under the age of 65.

The System also provides disability benefits, group life insurance benefits and survivor benefits. Cost of living adjustments are granted on an ad hoc basis, subject to approval by the State Budget and Control Board.

A comprehensive annual financial report containing financial statements and required supplementary information for the South Carolina Retirement System is publicly available on the website at [www.retirement.sc.gov](http://www.retirement.sc.gov) or by submitting a request to South Carolina Retirement System, P.O. Box 11960, Columbia, SC 29211-1960.

For each plan the maximum employee contribution are as follows:

Plan year	2010	2009
Under 50 years of age	\$ 16,500	\$ 16,500
50 years of age and over	\$ 22,000	\$ 22,000

## **Note 15 - Other commitments and contingencies**

The District is subject to various claims and contingencies arising out of the normal course of business. Management of the District believes that the ultimate liability, if any, from such claims or contingencies will be covered by the District's insurance policies and are not likely to have a material adverse effect on the District's operating results, financial condition or liquidity. Currently there are no material outstanding issues being addressed by legal counsel.

## **Note 16 – Subsequent events**

In August 2010, the District issued \$3,400,000 of series 2010B revenue bonds. In September 2010, the District issued \$3,970,000 of general obligation bonds. The funds received from these issuances will be used to defray the cost of system improvements and construction commitments as disclosed in Note 12.



### **Note 17 - Net assets**

Net assets represent the difference between assets and liabilities. The net asset amounts were as follows:

	As of June 30,	
	2010	2009
<b>Invested in capital assets, net of related liabilities</b>		
Net property plant and equipment in service	\$ 80,515,057	\$ 81,439,611
Less: Debt as disclosed in Notes 6 & 7	(52,819,994)	(53,048,727)
Advances for construction	-	-
Cash held by County for construction	-	237,140
Bond premium, net	(956,624)	(1,063,321)
Deferred amount on refunding, net	2,352,815	2,567,394
Bond issue costs and discounts, net	921,962	960,765
Accounts payable for capital assets	(548,353)	(625,310)
	<u>29,464,863</u>	<u>30,467,552</u>
<b>Restricted for capital activity and debt service</b>	2,378,848	2,446,988
<b>Unrestricted</b>	6,719,409	6,350,882
Total net assets	<u>\$ 38,563,120</u>	<u>\$ 39,265,422</u>

# **SUPPLEMENTAL FINANCIAL INFORMATION**

**HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT**  
**Schedule of Bond Principal and Interest Payments**  
**June 30, 2010**

For the Year ending June 30,	\$17,575,000- Refunded Revenue Bonds			\$430,000 Revenue Bonds			\$18,770,000 Revenue Bonds			\$930,000 Revenue Bond			\$7,350,000 GO Bond			\$335,902 Revenue Bond			\$1,781,694 Series 2009 GO Bond			\$190,722 Series 2010A Revenue Bond		
	Dated April 11, 2004	Interest	Principal	Dated August 10, 2004	Interest	Principal	Dated February 2, 2006	Interest	Principal	Dated June 20, 2007	Interest	Principal	Dated October 3, 2007	Interest	Principal	Dated July 30, 2009	Interest	Principal	Dated July 30, 2009	Interest	Principal	Dated June 16, 2010	Interest	Principal
2011	691,663	13,332	740,000	12,943	712,924	440,000	35,216	34,555	273,863	290,000	16,194	17,060	70,303	89,737	16,284	17,836	66,517	93,523	89,737	6,935	16,284	6,935	16,284	
2012	661,163	12,660	775,000	13,615	697,174	460,000	33,758	36,013	261,175	300,000	15,417	17,836	261,175	300,000	16,585	18,648	62,571	97,469	97,469	6,077	17,222	6,077	17,222	
2013	616,431	11,954	1,385,000	14,321	680,724	480,000	32,238	37,532	248,800	310,000	14,606	18,648	248,800	310,000	17,886	19,496	58,459	101,581	101,581	5,414	17,886	5,414	17,886	
2014	550,500	11,211	1,460,000	15,064	663,443	490,000	30,654	39,116	236,400	325,000	13,757	20,383	236,400	325,000	19,290	21,311	49,707	110,333	110,333	4,010	19,290	4,010	19,290	
2015	475,625	10,428	1,535,000	15,846	645,318	510,000	29,004	40,767	223,400	335,000	12,870	20,436	223,400	335,000	20,983	22,280	54,173	105,867	105,867	4,726	18,575	4,726	18,575	
2016	396,875	9,606	1,615,000	16,669	625,574	525,000	27,283	42,487	210,000	350,000	11,943	21,311	210,000	350,000	22,311	22,280	49,707	110,333	110,333	4,010	19,290	4,010	19,290	
2017	324,375	8,741	1,285,000	17,534	594,068	1,055,000	25,490	44,280	196,000	365,000	10,973	22,280	196,000	365,000	20,033	22,280	45,052	114,988	114,988	3,268	20,033	3,268	20,033	
2018	258,375	7,831	1,355,000	18,444	551,061	1,100,000	23,622	46,149	181,400	380,000	9,959	23,294	181,400	380,000	20,804	23,294	40,200	119,839	119,839	2,497	20,804	2,497	20,804	
2019	188,875	6,874	1,425,000	19,401	506,161	1,145,000	21,674	48,097	166,200	390,000	8,900	24,354	166,200	390,000	21,605	24,354	35,144	124,895	124,895	1,696	21,605	1,696	21,605	
2020	115,875	5,867	1,495,000	20,408	459,461	1,190,000	19,645	50,126	150,600	405,000	7,791	25,462	150,600	405,000	17,886	25,462	29,875	130,165	130,165	864	17,886	864	17,886	
2021	39,250	4,808	1,570,000	21,467	410,761	1,245,000	17,529	52,242	134,400	420,000	6,633	26,620	134,400	420,000	-	26,620	24,383	135,656	135,656	-	-	-	-	
2022	-	3,694	-	22,581	325,361	3,025,000	15,325	54,446	117,600	440,000	5,422	27,832	117,600	440,000	-	27,832	18,660	141,380	141,380	-	-	-	-	
2023	-	2,522	-	23,753	200,184	3,155,000	13,027	56,744	100,000	460,000	4,155	29,098	100,000	460,000	-	29,098	12,695	147,345	147,345	-	-	-	-	
2024	-	1,289	-	24,837	67,753	3,285,000	10,632	59,138	81,600	480,000	2,831	30,422	81,600	480,000	-	30,422	6,479	153,561	153,561	-	-	-	-	
2025	-	-	-	-	-	-	8,137	61,634	62,400	500,000	1,447	31,806	62,400	500,000	-	31,806	-	-	-	-	-	-	-	
2026	-	-	-	-	-	-	5,536	64,235	42,400	520,000	-	-	42,400	520,000	-	-	-	-	-	-	-	-	-	
2027	-	-	-	-	-	-	2,825	66,946	21,600	540,000	-	-	21,600	540,000	-	-	-	-	-	-	-	-	-	
	4,319,007	\$ 110,817	14,640,000	\$ 256,883	\$ 7,139,967	\$ 18,105,000	\$ 351,595	\$ 834,507	\$ 2,707,838	\$ 6,810,000	\$ 142,898	\$ 355,902	\$ 574,218	\$ 1,666,339	\$ 42,203	\$ 190,722								
Current	\$ 740,000	\$ 12,943		\$ 243,940		\$ 440,000	\$ 34,555	\$ 799,952		\$ 290,000	\$ 17,060	\$ 338,842		\$ 89,737	\$ 16,284									
Noncurrent	\$ 13,900,000					\$ 17,665,000				\$ 6,520,000				\$ 1,576,602										

**BOND TOTALS**

For the Year ending June 30,	Total		Total	
	Interest	Principal	Interest	Principal
2011	1,820,430	1,640,579	3,461,009	
2012	1,754,580	1,712,572	3,467,152	
2013	1,673,401	2,360,193	4,033,594	
2014	1,569,838	2,468,143	4,037,981	
2015	1,455,544	2,581,438	4,036,982	
2016	1,334,998	2,700,090	4,035,088	
2017	1,207,967	2,924,115	4,132,082	
2018	1,074,945	3,063,530	4,138,475	
2019	935,524	3,198,352	4,133,876	
2020	789,978	3,338,598	4,128,576	
2021	637,764	3,470,985	4,108,749	
2022	486,062	3,711,239	4,197,301	
2023	332,583	3,871,940	4,204,523	
2024	170,584	4,032,958	4,203,542	
2025	71,984	593,440	665,424	
2026	47,936	584,235	632,171	
2027	24,425	606,946	631,371	
	<u>\$ 15,388,543</u>	<u>\$42,859,353</u>	<u>\$58,247,896</u>	
Current	<u>\$ 1,640,579</u>			
Noncurrent	<u>\$41,218,774</u>			

**HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT**  
**Schedule of Note Principal and Interest Payments**  
**June 30, 2010**

For the Year ending June 30,	SCJEDA		\$10,194,238		\$4,000,000		\$500,000		NOTE TOTALS	
	Dated November 30, 1998	Principal	Interest	Principal	Dated October 3, 2008	Interest	Dated April 14, 2008	Interest	Total	Total
2011	-	18,000	224,217	486,678	79,686	112,853	15,553	17,996	319,456	635,527
2012	-	18,000	206,959	503,936	76,263	116,277	14,914	18,634	298,136	656,847
2013	-	18,000	189,088	521,807	72,735	119,805	14,254	19,294	276,076	678,906
2014	-	18,000	170,584	540,311	69,100	123,440	13,569	19,979	253,253	701,729
2015	-	18,000	151,423	559,472	65,355	127,185	12,861	20,687	229,639	725,344
2016	-	18,000	131,583	579,312	61,496	131,043	12,127	21,421	205,207	749,776
2017	-	18,000	111,039	599,856	57,521	135,019	11,368	22,180	179,927	775,055
2018	-	18,000	89,767	621,128	53,424	139,115	10,581	22,967	153,772	801,210
2019	-	18,000	67,741	643,154	49,204	143,336	9,767	23,781	126,711	828,271
2020	-	18,000	44,933	665,962	44,855	147,685	8,923	24,625	98,711	856,272
2021	-	18,000	21,317	689,578	40,374	152,165	8,050	25,498	69,741	885,241
2022	-	18,000	1,542	176,182	35,758	156,782	7,146	26,402	44,445	377,366
2023	-	7,939	-	-	31,001	161,539	6,210	27,339	37,211	196,816
2024	-	-	-	-	26,100	166,440	5,240	28,308	31,340	194,748
2025	-	-	-	-	21,050	171,489	4,236	29,312	25,287	200,801
2026	-	-	-	-	15,848	176,692	3,197	30,351	19,044	207,043
2027	-	-	-	-	10,487	182,053	2,120	31,428	12,607	213,480
2028	-	-	-	-	4,963	187,576	1,006	32,542	5,969	220,118
2029	-	-	-	-	358	47,777	73	8,315	431	56,091
	\$ -	\$ 223,939	\$ 1,410,193	\$ 6,587,376	\$ 815,577	\$ 2,698,270	\$ 161,195	\$ 451,058	\$ 2,386,965	\$ 9,960,643
Current		\$ 18,000		\$ 486,678		\$ 112,853		\$ 17,996		\$ 635,527
Noncurrent		\$ 205,939		\$ 6,100,698		\$ 2,585,417		\$ 433,062		\$ 9,325,116

# STATISTICAL SECTION

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<sup>8</sup> In some cases less than 10 years of data in certain tables is illustrated due to the unavailability of information and/or the implementation GASB No.34 in fiscal year 2004.

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# **Statements of Revenues, Expenses, and Debt Service per Bond Covenants** **Last Ten Fiscal Years**

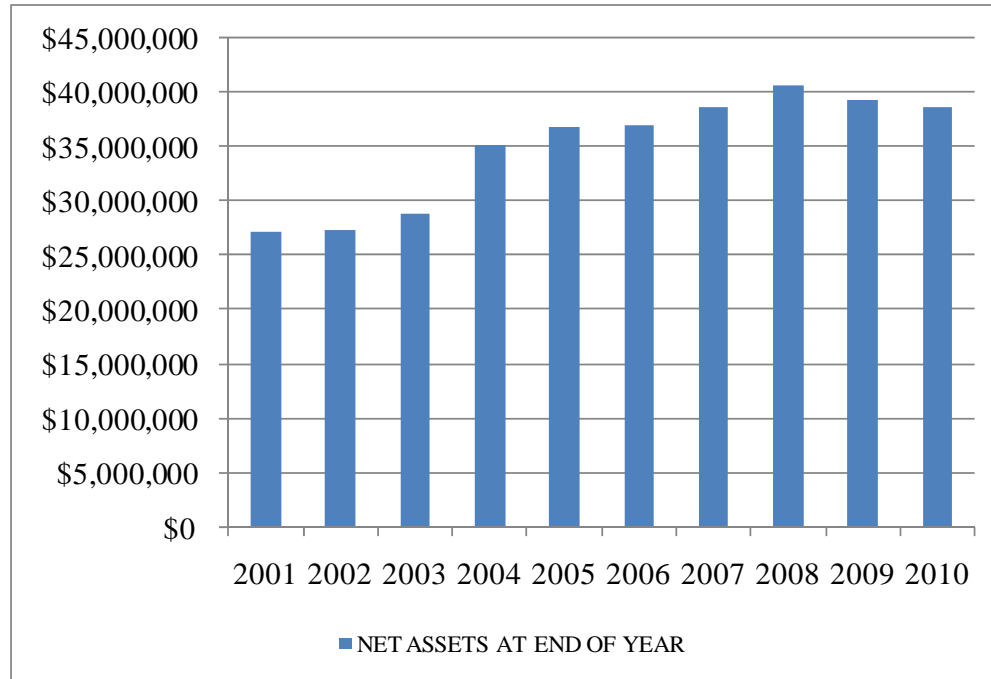
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
<b>Operating Revenues</b>										
Water service	5,011,668	4,997,200	\$4,633,117	\$4,992,011	\$4,870,847	\$5,162,771	\$5,465,028	\$5,518,049	\$5,307,260	\$5,308,798
Sewer service	3,336,732	3,405,374	3,342,647	3,503,456	3,525,405	3,655,945	3,941,776	4,059,860	3,959,087	\$4,034,068
Tap in fees - water	470,182	252,861	324,760	264,670	262,564	175,964	106,768	72,569	35,133	31,305
Tap in fees - sewer	510,600	267,231	266,792	272,536	294,286	72,493	19,600	11,284	2,330	117,367
Availability charges	554,899	501,788	503,166	443,559	400,503	546,788	504,303	540,104	547,354	570,169
Service fees and penalties	228,278	299,630	38,601	32,199	41,985	42,121	38,218	38,153	50,311	70,488
Golf course irrigation	193,074	227,662	123,858	181,379	157,944	216,700	261,616	301,856	243,274	230,583
<b>Total Operating Revenues</b>	<b>\$10,305,432</b>	<b>\$9,951,745</b>	<b>\$9,232,942</b>	<b>\$9,689,810</b>	<b>\$9,553,534</b>	<b>\$9,872,782</b>	<b>\$10,337,309</b>	<b>\$10,541,875</b>	<b>\$10,144,750</b>	<b>\$10,362,778</b>
<b>Operating Expenses</b>										
Payroll and related expenses	\$ 2,653,416	\$ 3,347,730	\$ 2,601,065	\$ 2,506,686	\$ 2,416,236	\$ 2,593,804	\$ 2,735,039	\$ 2,975,752	\$ 3,165,506	\$ 3,166,896
Administrative expenses	699,360	633,966	586,073	533,999	555,416	563,365	556,794	606,608	759,594	754,453
Operations expenses	636,940	669,274	702,466	857,153	938,247	1,086,507	1,098,914	1,197,436	1,430,222	1,410,295
Maintenance expenses	662,961	686,019	651,475	824,196	842,872	829,386	736,685	816,724	707,892	919,832
Purchased water	1,427,257	1,298,780	1,146,852	1,225,760	1,394,283	1,645,206	1,671,703	1,596,183	1,356,803	746,571
RO Plant O&M	-	-	-	-	-	-	-	-	127,852	674,039
Professional fees	115,195	146,028	166,255	408,970	243,961	291,336	294,484	532,391	410,736	269,207
Vehicle expenses	125,127	96,618	103,496	105,783	129,805	140,672	140,654	146,335	131,379	107,292
Depreciation	2,469,190	2,882,264	3,197,862	3,208,842	3,221,943	3,349,668	3,540,690	3,720,333	3,965,632	4,405,077
<b>Total Operating Expenses</b>	<b>\$ 8,789,445</b>	<b>\$ 9,760,680</b>	<b>\$ 9,155,544</b>	<b>\$ 9,671,389</b>	<b>\$ 9,742,763</b>	<b>\$ 10,499,944</b>	<b>\$ 10,774,963</b>	<b>\$ 11,591,762</b>	<b>\$ 12,055,616</b>	<b>\$ 12,453,662</b>
<b>Operating Income (Loss from operations)</b>	<b>\$1,515,987</b>	<b>\$191,065</b>	<b>\$77,398</b>	<b>\$18,421</b>	<b>(\$189,229)</b>	<b>(\$627,162)</b>	<b>(\$437,654)</b>	<b>(\$1,049,887)</b>	<b>(\$1,910,866)</b>	<b>(\$2,090,884)</b>
<b>Non-operating revenues (expenses)</b>										
Property taxes-debt service	352,371	348,968	\$360,384	\$378,626	\$320,228	\$269,130	\$125,052	\$409,292	\$817,751	\$967,418
Property taxes-operations	523,511	566,993	551,967	566,682	831,083	848,076	760,054	901,072	924,702	\$1,028,416
Sewer Assessments	466,763	464,385	464,888	-	-	-	-	0	-	0
Rental income	-	-	-	18,395	58,039	80,852	87,011	84,546	84,496	\$82,150
Interest earned	691,119	269,689	192,692	116,629	354,611	538,646	508,389	437,209	269,950	\$256,948
Tower leases	425,845	410,130	380,467	415,892	426,723	454,800	472,207	599,135	471,303	\$448,673
Other	56,171	128,936	92,011	30,631	12,646	7,803	16,712	16,188	19,153	\$35,840
Tower lease contract settlement	-	-	-	-	-	(\$275,000)	-	-	-	-
Amortization of bond costs	(\$128,126)	\$ (136,950)	(\$138,690)	(\$150,479)	(\$170,672)	(\$360,077)	(\$204,719)	(\$204,689)	(\$206,685)	(\$202,111)
Loss on disposal of equipment	-	-	-	-	-	-	-	-33,175	2,000.00	-
Interest expense	(\$2,485,169)	(\$2,639,877)	(\$2,767,890)	(\$2,357,062)	(\$2,368,340)	(\$1,911,202)	(\$1,888,236)	(\$1,860,432)	(\$1,911,438)	(\$2,208,372)
<b>Total Non-Operating Income (Loss)</b>	<b>(97,515)</b>	<b>(\$587,726)</b>	<b>(\$864,170)</b>	<b>(\$980,686)</b>	<b>(\$535,682)</b>	<b>(\$346,972)</b>	<b>(\$123,530)</b>	<b>\$349,146</b>	<b>\$471,232</b>	<b>\$408,961</b>
<b>Net Income(loss) before capital contributions per Financial Statements</b>	<b>1,418,473</b>	<b>(\$396,661)</b>	<b>(\$786,772)</b>	<b>(\$962,265)</b>	<b>(\$724,911)</b>	<b>(\$974,134)</b>	<b>(\$561,184)</b>	<b>(\$700,741)</b>	<b>(\$1,439,634)</b>	<b>(\$1,681,923)</b>
Capacity Fees	1,384,080	444,597	1,508,090	1,337,085	1,808,924	907,349	1,070,629	985,723	109,037	242,308
Add: Depreciation	2,469,190	2,882,264	3,197,862	3,208,842	3,221,943	3,349,668	3,540,690	3,720,333	3,965,632	4,405,077
Amortization	128,126	136,950	138,690	150,479	170,672	360,077	204,719	204,689	206,685	202,112
Interest Expense (Bonds)	2,485,169	2,639,877	2,767,890	2,357,062	2,368,340	1,911,202	1,888,236	1,860,432	1,911,438	2,208,372
Assessments - Debt Service	-	-	-	427,784	244,854	244,956	365,377	419,060	508,381	537,759
Less: Property Taxes – Debt Service	(352,371)	(348,968)	(360,384)	(378,626)	(320,228)	(269,130)	(125,052)	(409,292)	(817,751)	(967,418)
<b>Net Earnings Available for Debt Service</b>	<b>7,532,667</b>	<b>5,358,060</b>	<b>6,465,375</b>	<b>6,140,361</b>	<b>6,769,594</b>	<b>5,529,988</b>	<b>6,383,415</b>	<b>6,080,204</b>	<b>4,443,788</b>	<b>4,946,286</b>
<b>Debt Service on Revenue Bonds</b>	<b>3,469,512</b>	<b>3,904,146</b>	<b>4,177,462</b>	<b>\$4,181,197</b>	<b>\$4,290,731</b>	<b>\$3,944,189</b>	<b>\$3,637,421</b>	<b>\$3,441,126</b>	<b>\$3,438,347</b>	<b>\$3,523,871</b>
<b>Required per Bond Covenants</b>	<b>120%</b>	<b>120%</b>	<b>120%</b>	<b>120%</b>	<b>120%</b>	<b>120%</b>	<b>120%</b>	<b>120%</b>	<b>120%</b>	<b>120%</b>
<b>Coverage of Debt Service by Net Earnings</b>	<b>217%</b>	<b>137%</b>	<b>155%</b>	<b>147%</b>	<b>158%</b>	<b>140%</b>	<b>175%</b>	<b>177%</b>	<b>129%</b>	<b>140%</b>
<b>Debt Coverage without Capacity Fees</b>	<b>177%</b>	<b>126%</b>	<b>119%</b>	<b>115%</b>	<b>116%</b>	<b>117%</b>	<b>146%</b>	<b>148%</b>	<b>126%</b>	<b>133%</b>



### Schedule of Change in Net Assets

	2004	2005	2006	2007	2008	2009	2010
Operating Income (Loss from operations)	\$18,421	(\$189,229)	(\$627,162)	(\$437,654)	(\$1,049,887)	(\$1,910,866)	(\$2,090,884)
Total Non-Operating Income (Loss)	(\$980,686)	(\$535,682)	(\$346,972)	(\$123,530)	\$349,146	\$471,232	\$408,961
Capital Contributions	<u>\$2,111,131</u>	<u>\$2,371,635</u>	<u>\$1,153,508</u>	<u>\$2,224,783</u>	<u>\$2,555,086</u>	<u>\$201,573</u>	<u>\$979,621</u>
Increase (decrease) in net assets	\$1,148,866	\$1,646,724	\$179,374	\$1,663,599	\$1,854,345	(\$1,238,061)	(\$702,302)
Effect of prior period adjustments on net assets	\$5,200,347						
Net assets at beginning of year, as previously reported	\$28,810,228						
Net assets at beginning of year	<u>\$34,010,575</u>	<u>\$35,159,441</u>	<u>\$36,806,165</u>	<u>\$36,985,539</u>	<u>\$38,649,138</u>	<u>\$40,503,483</u>	<u>\$39,265,422</u>
Net assets at end of year	<u>\$35,159,441</u>	<u>\$36,806,165</u>	<u>\$36,985,539</u>	<u>\$38,649,138</u>	<u>\$40,503,483</u>	<u>\$39,265,422</u>	<u>\$38,563,120</u>

### Net Assets at End of Year

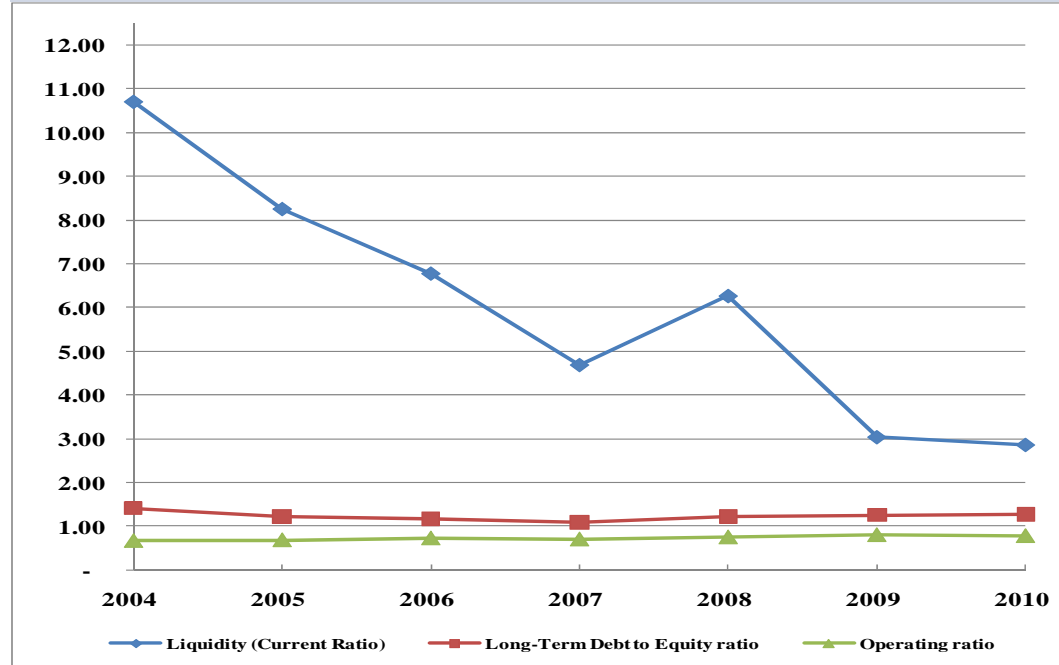


### Net Assets by Component

		2004	2005	2006	2007	2008	2009	2010
<b>Net assets</b>								
	Invested in capital assets, net of related liabilities	\$18,511,205	\$19,885,561	\$25,634,468	\$27,526,781	\$29,167,977	\$30,467,552	\$29,464,863
	Restricted for capital activity and debt service	2,097,137	5,442,647	2,176,688	2,708,532	2,334,594	2,446,988	2,378,848
	Unrestricted	<u>14,551,099</u>	<u>11,477,957</u>	<u>9,174,383</u>	<u>8,413,825</u>	<u>9,000,912</u>	<u>6,350,882</u>	<u>6,719,409</u>
	Net assets	<u>\$35,159,441</u>	<u>\$36,806,165</u>	<u>\$36,985,539</u>	<u>\$38,649,138</u>	<u>\$40,503,483</u>	<u>\$39,265,422</u>	<u>\$38,563,120</u>

### Ratio Analysis

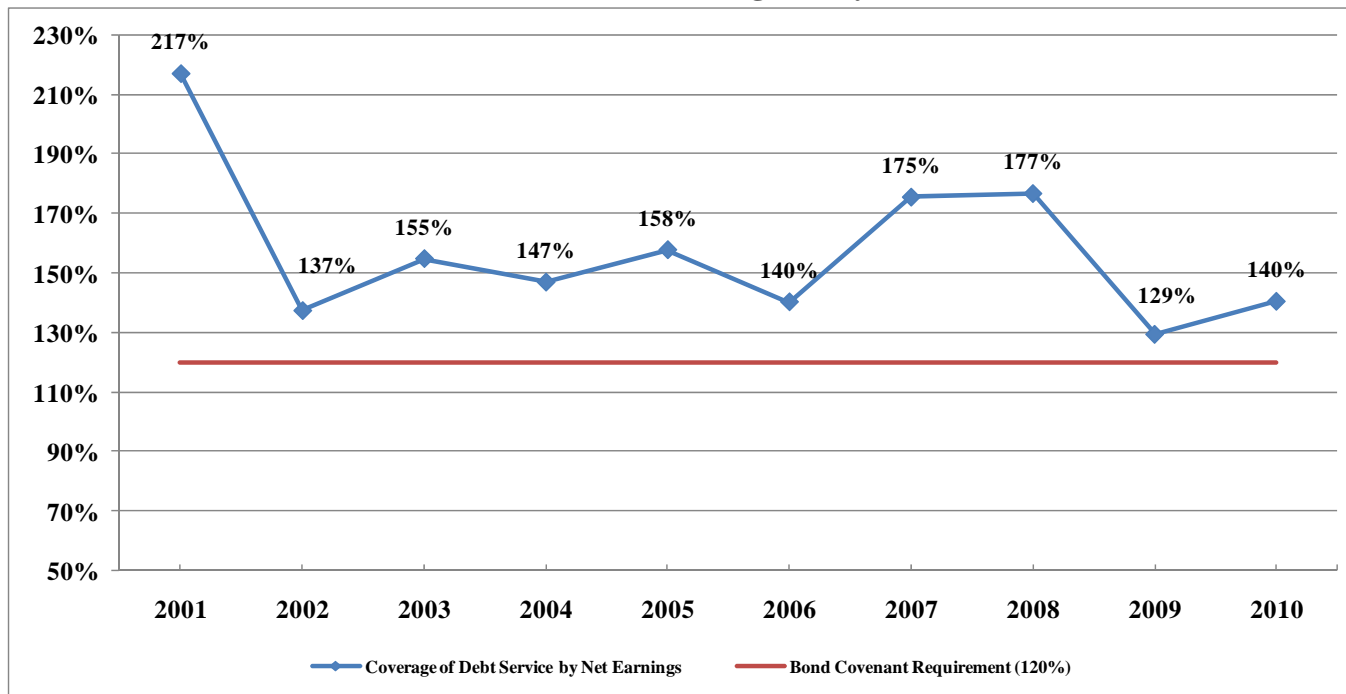
	2004	2005	2006	2007	2008	2009	2010
<b>Liquidity (Current Ratio)</b>	10.70	8.25	6.78	4.69	6.26	3.04	2.86
<b>Long-Term Debt to Equity ratio</b>	1.41	1.22	1.16	1.10	1.22	1.26	1.27
<b>Operating ratio</b>	0.67	0.68	0.72	0.70	0.75	0.80	0.78



### Outstanding Debt by Debt Type

Fiscal Year	GO Bonds	Revenue Bonds	SRF Revenue Loans	SRF GO Loans	Notes Payable	Total Outstanding Debt
2001	\$ 1,825,000	\$46,230,857	\$ 8,341,452		385,939	\$ 56,783,248
2002	1,650,000	45,145,841	9,925,439		367,939	57,089,219
2003	1,450,000	44,009,899	9,558,064		349,939	55,367,902
2004	795,000	42,282,972	9,176,733		331,939	52,586,644
2005	530,000	41,192,626	8,781,879		313,939	50,818,444
2006	275,000	37,803,495	8,373,023		295,939	46,747,457
2007	-	37,972,665	7,949,668		277,939	46,200,272
2008	7,350,000	36,853,711	7,511,300		259,939	51,974,950
2009	7,085,000	35,388,165	7,057,386	3,276,237	241,939	53,048,727
2010	8,476,339	34,383,014	6,587,376	3,149,328	223,939	52,819,996

### Debt Service Coverage Analysis



## Detailed Schedule of Change in Net Assets

Last Eight Fiscal Years

	June 30, 2003	Additions	Disposals	Transfers	June 30, 2010
Land	\$ 371,014	\$ 955,615			\$ 1,326,629
Wetlands discharge system	996,653	-	-	-	996,653
	1,367,667	955,615	-	-	2,323,282
Waterworks system	34,827,349	1,398,768	(1,024,703)	15,482,763	50,684,177
Shop furniture and equipment	124,884	31,266	(57,738)	-	98,412
Sewage disposal system	9,014,484	2,244,540	(119,253)	15,809,816	26,949,587
Buildings	4,153,874	56,192	(2,452)	81,721	4,289,335
Sewage treatment facilities	36,522,657	92,670	(3,560)	26,733	36,638,501
Transportation equipment	1,016,536	518,463	(847,086)	-	687,913
Water and sewer equipment	1,826,289	157,706	(294,270)	62,188	1,751,913
Orthophotography mapping	11,175	-	-	-	11,175
Office equipment	854,435	130,456	(404,093)	-	580,797
Sub Total	88,351,683	4,630,061	(2,753,155)	31,463,221	121,691,810
Accumulated depreciation	(21,961,131)	(25,412,185)	2,637,101	-	(44,736,215)
Property Plant & Equipment	66,390,552	(20,782,124)	(116,054)	31,463,221	76,955,595
Construction in Progress	1,836,586	30,862,814	-	(31,463,221)	1,236,180
	68,227,138	10,080,691	(116,054)	-	78,191,775
Net Property Plant & Equipment	\$ 69,594,805	\$ 11,036,306	\$ (116,054)	\$ (0)	\$ 80,515,057

## Schedule of Net Property, Plant, & Equipment (PP&E)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
PP&E	\$ 75,211,885	\$ 87,504,590	\$ 89,719,351	\$ 93,660,892	\$ 95,834,607	\$ 96,222,163	\$101,306,310	\$107,539,856	\$121,309,803	\$124,015,092
Accumulated Depreciation	(16,190,048)	(18,767,821)	(21,961,131)	(24,905,146)	(28,027,340)	(29,642,022)	(33,057,250)	(36,681,713)	(40,512,192)	(44,736,215)
Net PP&E in Service	59,021,837	68,736,769	67,758,220	68,755,747	67,807,266	66,580,141	68,249,059	70,858,143	80,797,611	79,278,877
Construction in Progress	8,975,726	407,273	1,836,586	306,918	928,300	3,005,393	2,720,938	4,542,373	641,980	1,236,180
Net PP&E	\$ 67,997,563	\$ 69,144,042	\$ 69,594,805	\$ 69,062,665	\$ 68,735,566	\$ 69,585,534	\$ 70,969,998	\$ 75,400,516	\$ 81,439,592	\$ 80,515,057

### Customer Statistics at Fiscal Year-End

Number of Water vs. Wastewater Customers at Fiscal Year-end

Year	Water	Percent Increase	Wastewater	Percent Increase	Ratio of Customers with Both Services
2001	13,782		12,505		90.7%
2002	14,176	2.9%	12,850	2.8%	90.6%
2003	14,526	2.5%	13,210	2.8%	90.9%
2004	14,764	1.6%	13,497	2.2%	91.4%
2005	15,766	6.8%	13,870	2.8%	88.0%
2006	16,168	2.5%	14,374	3.6%	88.9%
2007	16,344	1.1%	14,658	2.0%	89.7%
2008	16,392	0.3%	14,835	1.2%	90.5%
2009	16,355	-0.2%	14,880	0.3%	91.0%
2010	16,321	-0.2%	14,891	0.1%	91.2%

### Customer Statistics at Fiscal Year-End

Number of Water/Irrigation vs. Wastewater Customers at Fiscal Year-end

Year	Water and Irrigation	Percent Increase	Wastewater	Percent Increase	Ratio of Customers with Both Services
2001	14,473		12,505		86.4%
2002	14,933	3.2%	12,850	2.8%	86.1%
2003	15,330	2.7%	13,210	2.8%	86.2%
2004	15,612	1.8%	13,497	2.2%	86.5%
2005	16,647	6.6%	13,870	2.8%	83.3%
2006	17,104	2.7%	14,374	3.6%	84.0%
2007	17,295	1.1%	14,658	2.0%	84.8%
2008	17,389	0.5%	14,835	1.2%	85.3%
2009	17,354	-0.2%	14,880	0.3%	85.7%
2010	17,316	-0.2%	14,891	0.1%	86.0%

**Billings at Fiscal Year-End (Just Water, No Irrigation)**

Reported in kgals (thousands of gallons)

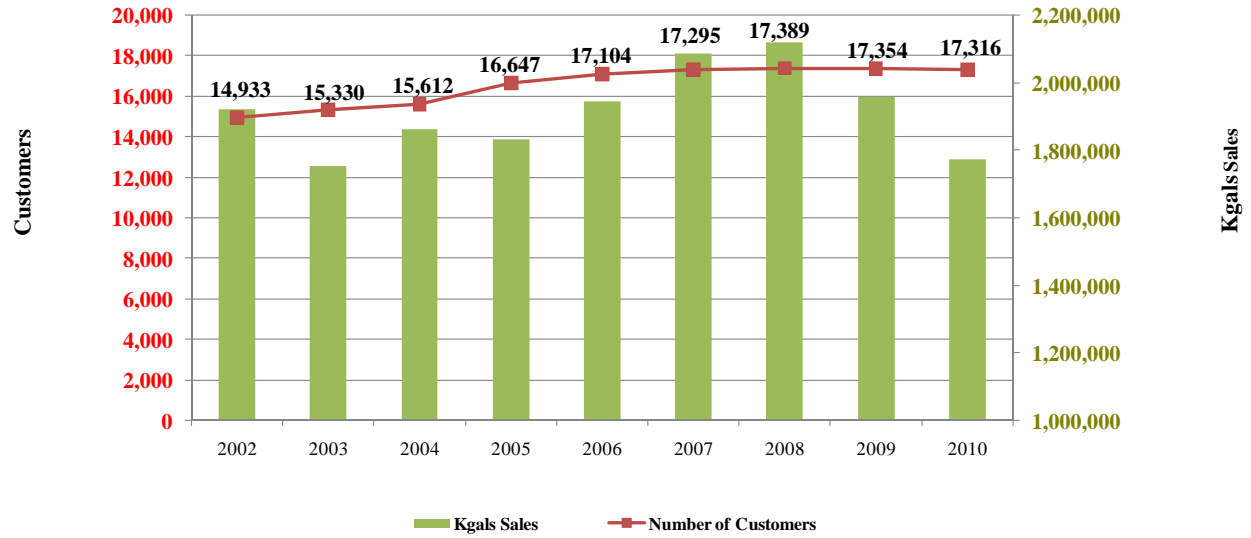
<b>Year</b>	<b>Water</b>	<b>Percent Increase</b>	<b>Wastewater</b>	<b>% Inc</b>
2001	N/A		N/A	
2002	1,594,177		1,331,003	
2003	1,488,689	-6.6%	1,255,115	-5.7%
2004	1,553,989	4.4%	1,314,219	4.7%
2005	1,545,367	-0.6%	1,313,400	-0.1%
2006	1,619,616	4.8%	1,378,504	5.0%
2007	1,721,661	6.3%	1,490,636	8.1%
2008	1,745,767	1.4%	1,523,113	2.2%
2009	1,629,557	-6.7%	1,432,874	-5.9%
2010	1,486,416	-8.8%	1,279,144	-10.7%

**Billings at Fiscal Year-End (Water and Irrigation)**

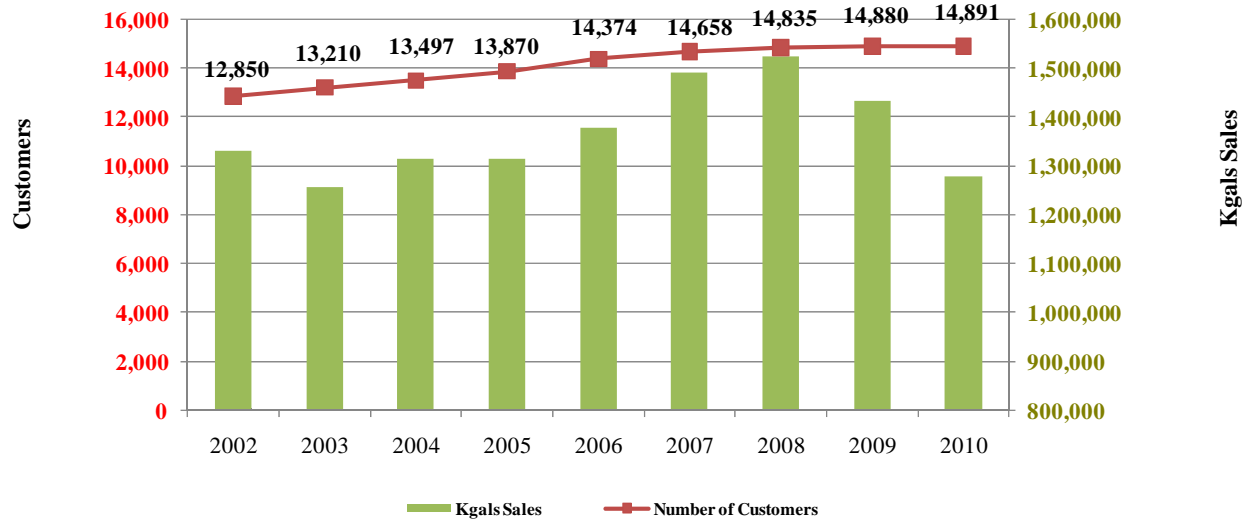
Reported in kgals (thousands of gallons)

<b>Year</b>	<b>Water/Irrigation</b>	<b>Percent Increase</b>	<b>Wastewater</b>	<b>% Inc</b>
2001	N/A		N/A	
2002	1,921,347		1,331,003	
2003	1,753,397	-8.7%	1,255,115	-5.7%
2004	1,861,014	6.1%	1,314,219	4.7%
2005	1,834,200	-1.4%	1,313,400	-0.1%
2006	1,943,868	6.0%	1,378,504	5.0%
2007	2,086,348	7.3%	1,490,636	8.1%
2008	2,119,295	1.6%	1,523,113	2.2%
2009	1,957,926	-7.6%	1,432,874	-5.9%
2010	1,773,200	-9.4%	1,279,144	-10.7%

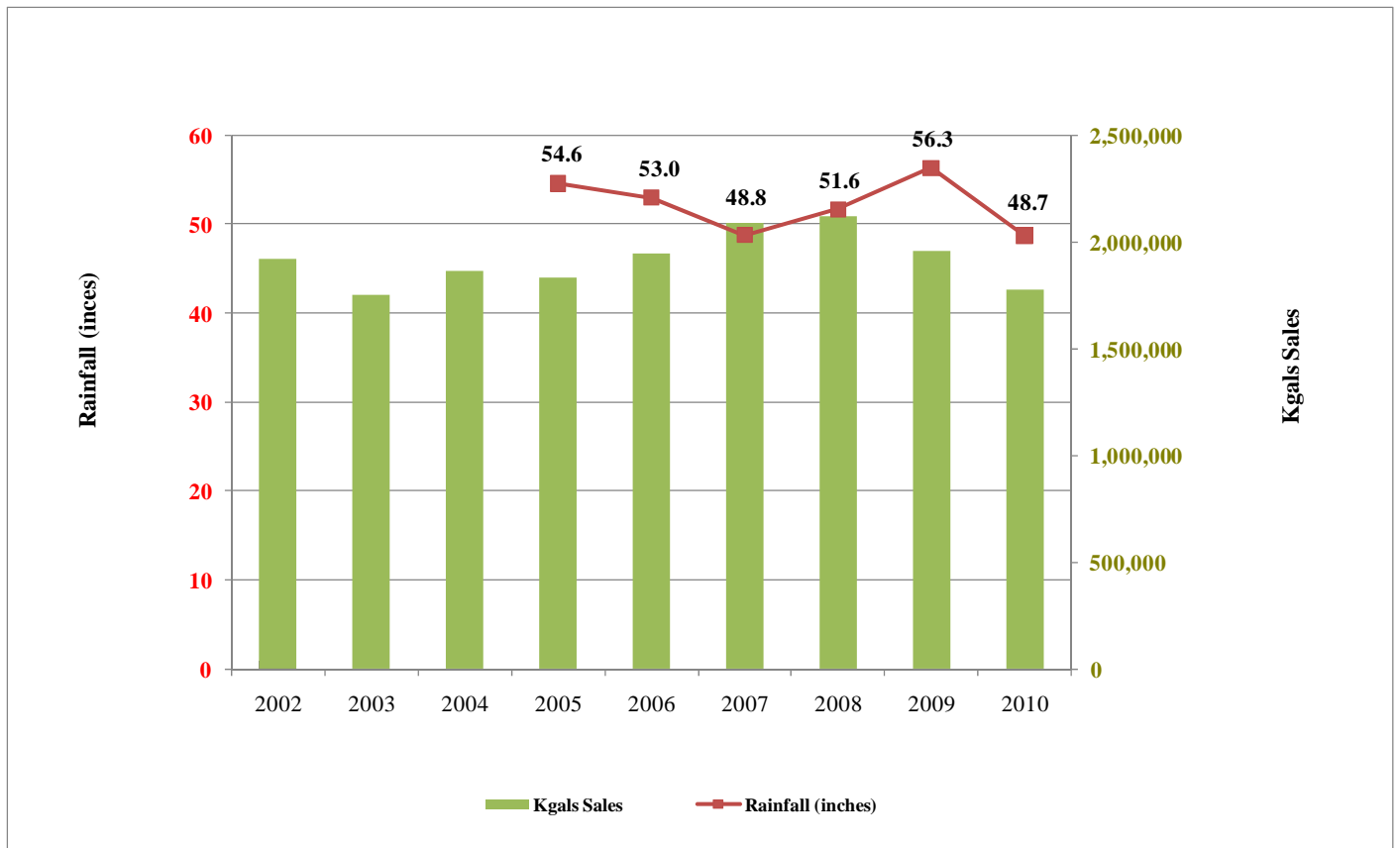
### Customers vs. Water/Irrigation Kgal Sales



### Customers vs. Wastewater Kgal Sales



**Rainfall (Inches) vs. Water/Irrigation Kgal Sales <sup>9</sup>**



<sup>9</sup> Rainfall amount data is unavailable for fiscal year 2001 and 2002. Kgal sale data is unavailable for fiscal year 2001.



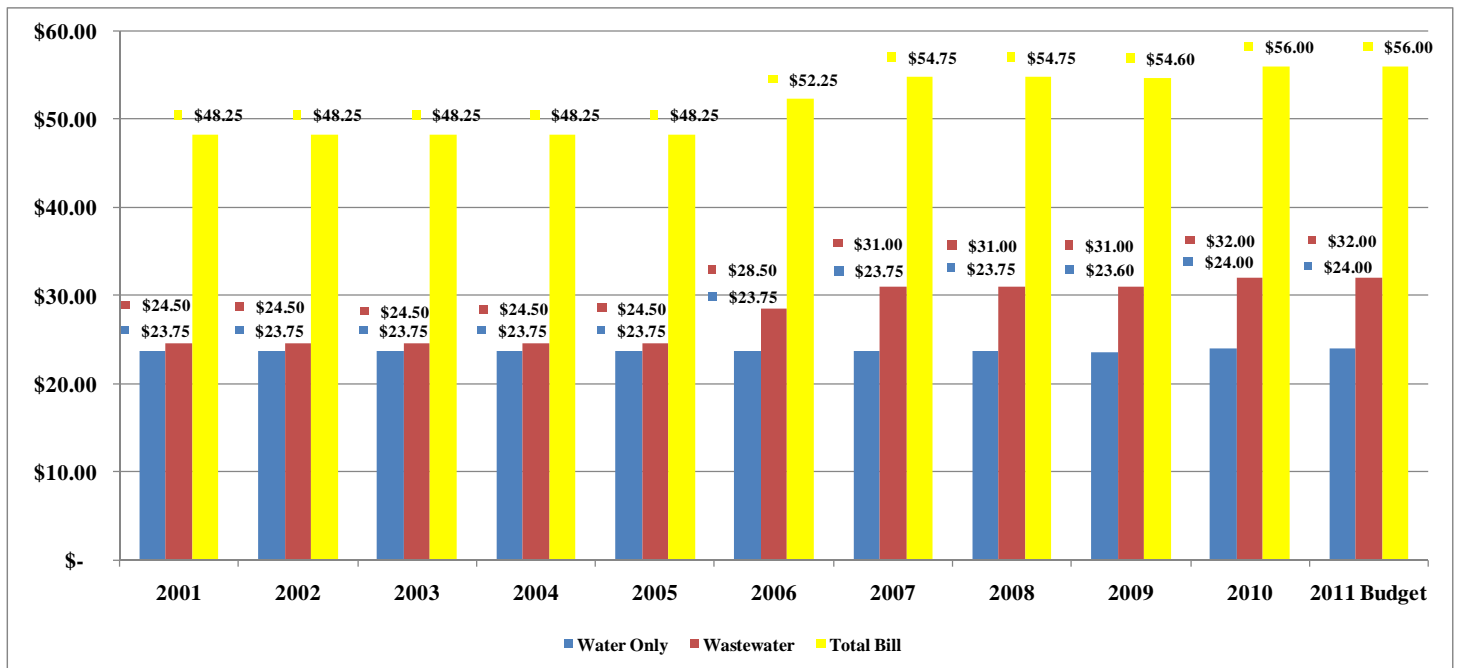
## Water Rate Comparisons

		Effective Date										
		FY'01	FY'02	FY'03	FY'04	FY'05	FY'06	FY'07	FY'08	FY'09*	FY'10**	FY'11 Bdgt.
Residential	Base Charge	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00
	First 5,000 Gallons	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.25			
	Next 6,000 to 17,000 gallons	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50			
	Next 18,000 to 32,000 gallons	\$ 1.75	\$ 1.75	\$ 1.75	\$ 1.75	\$ 1.75	\$ 1.75	\$ 1.75	\$ 1.75			
	Over 32,000 gallons	\$ 2.00	\$ 2.00	\$ 2.00	\$ 2.00	\$ 2.00	\$ 2.00	\$ 2.00	\$ 2.00			
	First 10,000 Gallons									\$ 1.36	\$ 1.40	\$ 1.40
	Next 11,000 to 20,000 gallons									\$ 1.64	\$ 1.71	\$ 1.71
	Next 21,000 to 30,000 gallons									\$ 1.91	\$ 2.20	\$ 2.20
Commercial	Over 30,000 gallons									\$ 2.18	\$ 2.55	\$ 2.55
	Base Charge	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00
	First 5,000 Gallons	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50			
	Next 6,000 to 17,000 gallons	\$ 1.75	\$ 1.75	\$ 1.75	\$ 1.75	\$ 1.75	\$ 1.75	\$ 1.75	\$ 1.75			
	Next 18,000 to 32,000 gallons	\$ 2.00	\$ 2.00	\$ 2.00	\$ 2.00	\$ 2.00	\$ 2.00	\$ 2.00	\$ 2.00			
	Over 32,000 gallons	\$ 2.25	\$ 2.25	\$ 2.25	\$ 2.25	\$ 2.25	\$ 2.25	\$ 2.25	\$ 2.25			
	First 10,000 Gallons									\$ 1.64	\$ 1.69	\$ 1.69
	Next 11,000 to 20,000 gallons									\$ 1.91	\$ 1.99	\$ 1.99
	Next 21,000 to 30,000 gallons									\$ 2.18	\$ 2.51	\$ 2.51
	Over 30,000 gallons									\$ 2.45	\$ 2.87	\$ 2.87
*Effective August 1, 2008												
**Effective October 1, 2009												

## Wastewater Rate Comparisons

		Effective Date										
		FY'01	FY'02	FY'03	FY'04	FY'05	FY'06*	FY'07**	FY'08	FY'09	FY'10	FY'11 Bdgt.
Residential	Base Charge	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00
	Per 1,000 gallons with Cap*	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.65	\$ 1.90	\$ 1.90	\$ 1.90	\$ 2.00	\$ 2.00
Commercial	Base	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00
	Per 1,000 gallons (No Cap)	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.60	\$ 1.60
*For years prior to FY'06, the effective sewer cap for residential customers was 32,000 gallons. From FY'06 to to present date the sewer cap is lowered to 10,000 gallons.												
**Per Thousand Increase Effective August 1, 2006												

## Water and Wastewater Bill History for Residential Customers Using 10,000 Gallons per Month



### District Top Ten Water Users

Fiscal year ended June 30, 2010

User Name	Type	2010 Billed Revenues	% of Total 2010 Billed Revenues
Hilton Head Beach & Tennis	Resort	\$ 145,447	2.74%
Cypress of Hilton Head Island Assoc.	Residential Homes	113,338	2.13%
Hilton Head Westin Resort	Resort	108,922	2.05%
Hilton Head Resort/Four Seasons	Resort	88,279	1.66%
Marriott Vacation Club	Resort	79,101	1.49%
Fiddler's Cove	Resort	65,334	1.23%
Marriott Surfwatch	Resort	63,479	1.20%
Spa at Port Royal	Resort	48,776	0.92%
Marshside Owners Association	Apartment Complex	43,786	0.82%
Hilton Head Health Systems	Medical	33,771	0.64%
Remaining Customers		<u>4,518,565</u>	<u>85.11%</u>
		<u>\$5,308,798</u>	100.00%

### District Top Ten Wastewater Users

Fiscal year ended June 30, 2010

User Name	Type	2010 Billed Revenues	% of Total 2010 Billed Revenues
Hilton Head Beach & Tennis	Resort	\$ 140,867	3.49%
Hilton Head Resort/Four Seasons	Resort	111,926	2.77%
Hilton Head Westin Resort	Resort	103,154	2.56%
Fiddler's Cove	Resort	77,283	1.92%
Cypress of Hilton Head Island Assoc.	Residential Homes	76,977	1.91%
Marriott Vacation Club	Resort	72,138	1.79%
Spa at Port Royal	Resort	55,341	1.37%
Marriott Surfwatch	Resort	54,640	1.35%
Marshside Owners Association	Apartment Complex	45,268	1.12%
Hilton Head Health Systems	Medical	43,337	1.07%
Remaining Customers		<u>3,253,138</u>	<u>80.64%</u>
		<u>\$4,034,068</u>	100.00%

### The District's Millage History

Debt Type	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Operations	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00
Debt Service	2.00	2.00	2.00	2.00	1.10	1.00	0.50	1.50	2.70	2.82
Total	5.00	5.00	5.00	5.00	4.10	4.00	3.50	4.50	5.70	5.82

### Overlapping Debt

Jurisdiction	2009 Assessed Value (Capped) <sup>(1)</sup>	2009 Assessed Value (Capped) of the District	Outstanding General Obligation Debt	Amount Applicable to the District
County of Beaufort	\$1,952,311,984	\$360,750,834	\$159,305,000	\$29,439,564
Beaufort County School District	1,952,311,984	360,750,834	349,490,000	64,585,752
Town of Hilton Head	991,447,353	343,608,827	59,705,000	20,693,753

<sup>(1)</sup> Assessed value is capped due to the limitations regarding property valuation under Act No. 388 as further discussed in "CERTAIN FISCAL MATTERS – Property Tax/Assessment Legislation – Reassessment Valuations Limited" herein.

Sources: Beaufort County Auditor; Town of Hilton Head Island Comprehensive Annual Report, Fiscal Year Ended June 30, 2009; Beaufort County, South Carolina Comprehensive Annual Report, Fiscal Year Ended June 30, 2009; Beaufort County School District, South Carolina Comprehensive Annual Report, Fiscal Year June 30, 2009.

### Assessed Values of the District

Year	Real Property	Personal Property <sup>(1)</sup>	Total
2009 <sup>(2)</sup>	\$ 322,448,420	\$ 38,302,414	\$ 360,750,834
2008	281,804,999	39,205,416	321,010,415
2007	266,386,512	39,155,967	305,542,479
2006	260,107,171	42,112,405	302,219,576
2005	249,949,026	43,357,300	293,306,326
2004 <sup>(3)</sup>	246,696,930	44,083,874	290,780,804
2003	145,111,702	46,455,963	191,567,665
2002	142,979,005	45,252,607	188,231,612
2001	137,925,038	45,981,108	183,906,146

Source: Beaufort County Auditor

(1) Figures do not include Merchant's Inventory, motor carrier reimbursement or manufacturer's depreciation reimbursement. Presently, there is no property in multi-county industrial parks or property otherwise subject to fee in lieu of taxes in the District.

(2) The County implemented its county-wide reassessment in fiscal year 2009.

(3) The County implemented its county-wide reassessment in fiscal year 2004.

### 2009 Market Value for the District

Classification	Assessed Value	Assessment Ratio	Market Value
1. Real Property and Mobile Homes	\$ 135,681,690	4.00%	\$ 4,115,787,945
2. Real Property and Mobile Homes	186,766,730	6.00%	3,933,367,229
3. Business Personal Property	4,607,760	10.50%	43,880,300
4. Merchant's Furniture, Fixtures and Equipment	1,406,710	10.50%	13,398,450
5. Motor Vehicles <sup>(1)</sup>	17,993,294	Various	144,247,638
6. Marine Equipment <sup>(2)</sup>	1,602,330	Various	26,751,750
7. Airplanes	436,570	4.00%	4,157,790
8. Manufacturing Property	218,110	10.50%	2,077,290
9. Public Utilities	8,535,150	10.50%	81,287,170
10. Rental Property and Signs <sup>(3)</sup>	3,502,490	Various	42,454,424
<p>Figures do not include Merchant's Inventory, motor carrier reimbursement or manufacturer's depreciation reimbursement. There is presently no property in multi-county industrial parks or property otherwise subject to fee in lieu of taxes in the District.</p> <p>Source: Beaufort County Auditor.</p> <p><sup>(1)</sup> Includes personal automobiles and commercial vehicles, which are assessed at different ratios.</p> <p><sup>(2)</sup> Includes personal watercraft and commercial fishing boats, which are assessed at different ratios.</p> <p><sup>(3)</sup> Includes residential rental property and commercial signs, which are assessed at different ratios.</p>			

### Tax Collection Record for the District

Fiscal Year	Taxes Subject to Collection	Current Collections	Current % Collected	Delinquent Taxes Collected	Total Collections	Total % Collected
2009-10	\$57,172,896.14	\$52,623,858.48	92.0%	\$491,839.61	\$53,115,698.29	92.9%
2008-09	56,329,331.01	54,777,458.84	97.2	869,820.54	55,647,279.38	98.8
2007-08	51,252,915.57	50,333,765.03	98.2	652,018.50	50,985,783.53	99.5
2006-07	54,353,422.22	52,223,374.50	96.1	424,256.63	52,647,631.13	96.8
2005-06	49,747,720.64	46,454,422.42	93.3	617,180.90	47,071,603.32	94.6
2004-05*	50,467,835.38	41,178,415.07	92.6	395,576.01	41,573,991.08	88.8
2003-04	44,449,943.19	41,178,415.07	92.6	395,576.01	41,573,991.08	89.8
2002-03	41,924,960.14	39,560,969.75	94.3	433,015.46	39,993,985.21	95.3
2001-02	38,921,768.96	36,623,650.04	93.1	373,743.80	36,997,393.84	94.1
Source: Beaufort County Auditor and Treasurer.						
* Lower collections due to unresolved appeals.						

## Beaufort County Largest Taxpayers

Employer	Type of Business	2009 Assessed Value	2008-09 Amounts Paid
1. SCG Hilton Head Property LLC	Real Estate	\$6,930,000	\$968,449.39
2. Palmetto Electric Coop. Inc.	Utility	3,930,544	816,647.40
3. Hargray Telephone Co.	Utility	3,572,786	741,592.82
4. Hilton Head Health System LP	Medical	1,755,313	369,154.09
5. Heritage Golf Port Royal LLC	Golf Course	1,188,920	255,939.08
6. Festival Centre (E&A) LLC	Shopping Center	1,064,400	231,013.14
7. Time Warner NY Cable	Utility	1,034,650	214,751.97
8. The Westin Resort Hilton Head	Hospitality	966,319	200,569.18
9. Indigo Run Asset Corp.	Property	1,026,018	188,632.43
10. Pineland Associates LLC	Property	770,316	184,174.10
Source: Beaufort County Auditor.			

## Population per Capita Income

Last Ten Available Years

	Hilton Head		Beaufort County		South Carolina	
Year	Population	Per Capita	Population	Per Capita	Population	Per Capita
1999	N/A*	\$ 29,935	117,975	32,165	1,974,682	\$ 23,550
2000	33,971	31,289	122,068	33,471	4,023,396	25,081
2001	34,048	32,331	124,740	34,554	4,061,844	25,648
2002	34,616	32,665	128,415	34,744	4,102,211	26,069
2003	34,578	33,661	130,793	35,523	4,143,120	26,684
2004	34,600	36,499	134,595	38,482	4,196,799	27,903
2005	34,761	38,411	138,959	40,392	4,249,385	29,223
2006	34,156	41,588	143,091	43,856	4,324,799	30,927
2007	33,890	42,658	146,722	45,031	4,404,914	31,925
2008	33,913	41,951	150,415	44,191	4,479,800	32,495
* Population Data for 1999 was not available.						
Source: Bureau of Economic Analysis, Regional Economic Information Systems, U.S. Census Bureau						

## Beaufort County Top Employers

Employer	Type of Business
Beaufort County School District	Educational Services
Wal-Mart Associates Inc.	Retail
County of Beaufort	Government
Department of Defense	Military
Beaufort Memorial Hospital	Health Services
Marine Corps Community Services	Health Services
Tenet Healthsystem Hilton Head Inc.	Health Services
Publix Super Markets Inc.	Retail
Hargray Communications Group Inc.	Management Services
Lowes Home Centers Inc.	Retail
Source: South Carolina Employment Security Commission, Labor Market Information Division (website: www.sces.org; 2009 data).	

## Beaufort County Labor Force and Employment<sup>1</sup>

Category	2009	2008	2007	2006	2005	2004	2003	2002	2001
Civilian Labor Force	64,805	64,103	65,083	60,707	61,900	59,198	56,329	53,781	N/A
Employment	59,101	60,711	62,198	57,667	58,897	56,272	53,657	51,533	N/A
Unemployment	5,704	3,392	2,885	3,040	3,003	2,926	2,672	2,248	N/A
Unemployment Rate	8.80%	5.29%	4.43%	5.00%	4.90%	4.90%	4.70%	4.20%	3.90%
N/A - Information not available									
-1 - Workers involved in labor disputes are included among the employed. Total employment also includes agricultural workers, proprietors, self-employed persons, workers in private households and unpaid family workers.									

## Unemployment Rate Comparison

Year	County	South Carolina	United States
2009	8.80%	11.70%	9.30%
2008	5.3	6.9	5.8
2007	4.3	5.6	4.6
2006	5	6.5	4.6
2005	4.9	6.7	5.1
2004	4.9	6.8	5.5
2003	4.7	6.7	6.0
2002	4.2	5.9	5.8
2001*	3.9	N/A	N/A
Source: South Carolina Employment Security Commission, Labor Market Information Division; U.S. Dept. of Labor, Bureau of Labor Statistics.			
* Data unavailable			



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