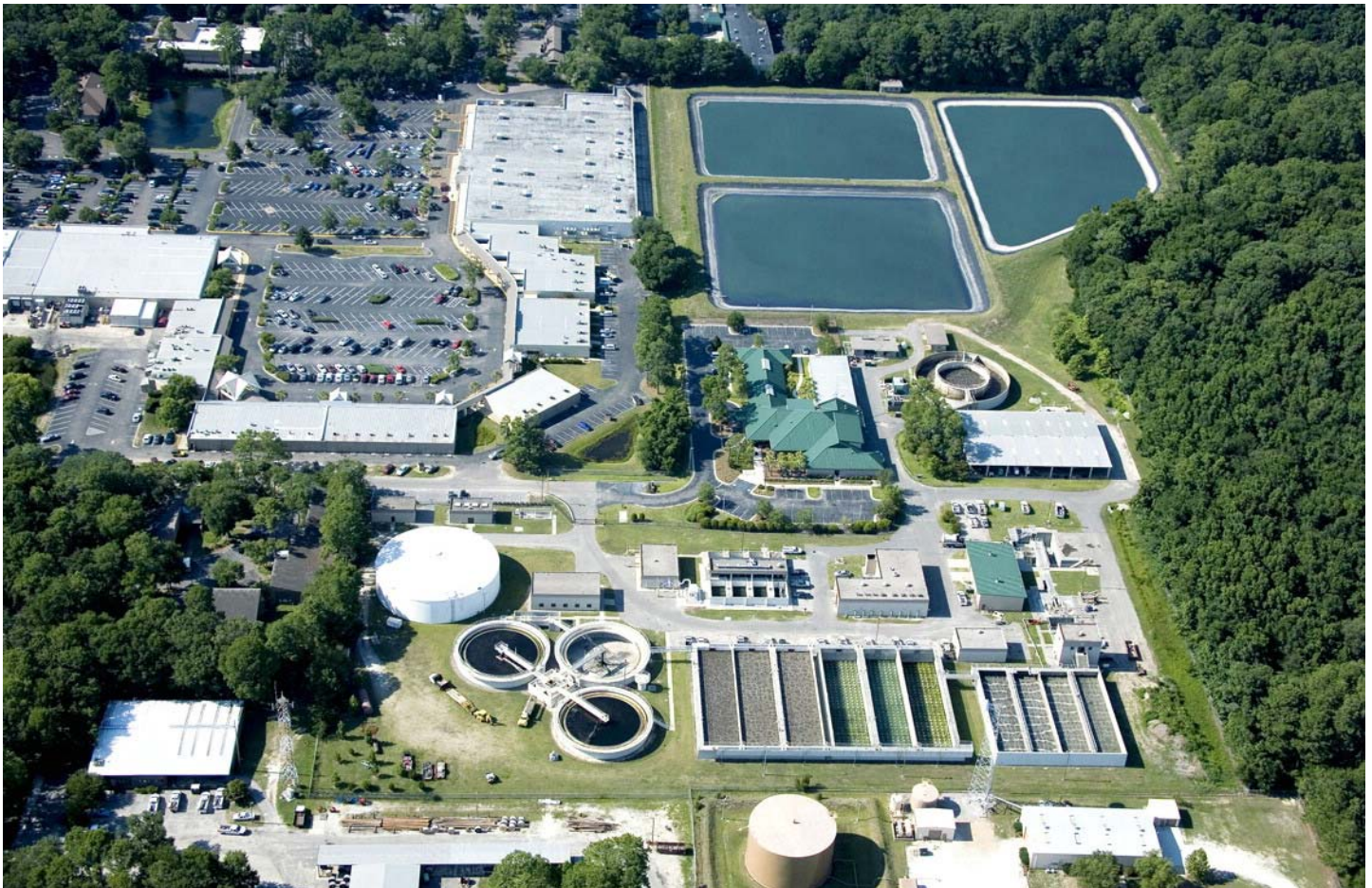




Hilton Head Island, South Carolina

Comprehensive Annual Financial Report



**Fiscal Year Ending
June 30, 2012**

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INTRODUCTION



The Hilton Head PSD Water Resources Center, 21 Oak Park Drive, Hilton Head Island, SC

Board of Commissioners

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

The Commission establishes policies 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.

The 2012 Hilton Head Public Service District Commission



W. Robert "Bob" Manne, Chairman, District 4
Current Term: 2008-2012
Long Range Water Supply Committee
Community and Personnel Relations Committee



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



Gary Kratz, Treasurer, District 4
Current Term: 2008-2012
Finance Committee
Planning and Operations Committee
Long Range Water Supply Committee



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



Jack Burke, District 2
Current Term: 2008-2012
Planning and Operations Committee



Frank Drehwing, District 4
Current Term: 2010-2014
Chairman, Long-Range Water Supply Committee
Community and Personnel Relations Committee



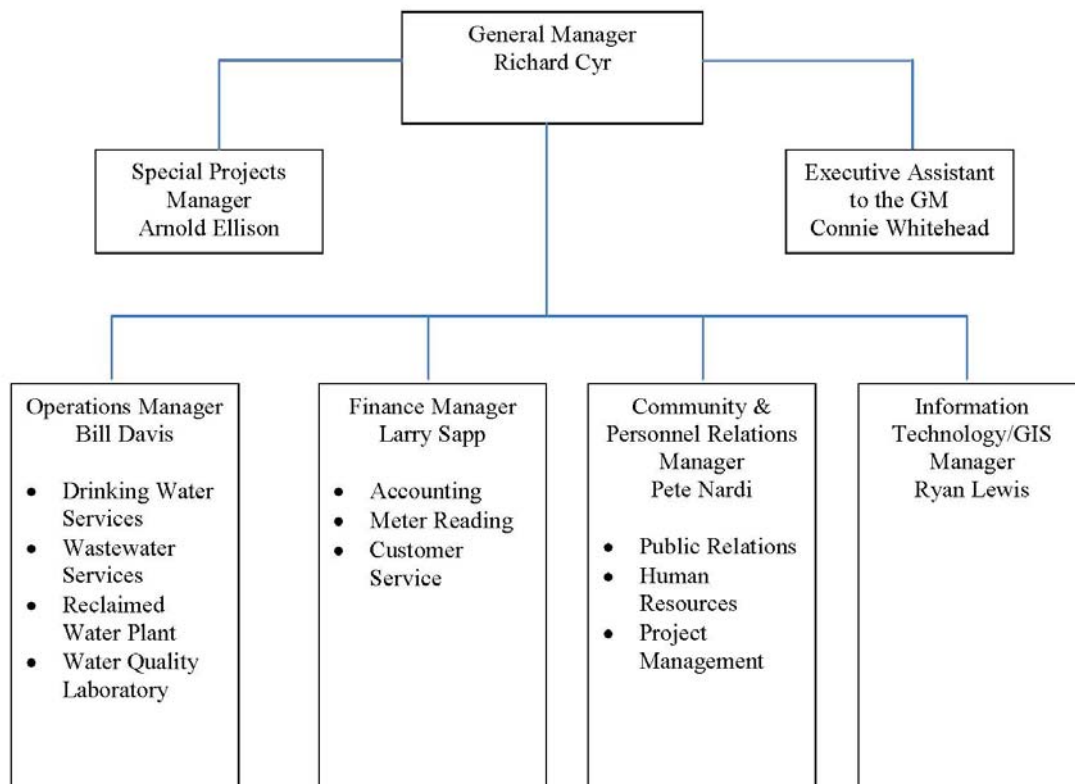
Herbert Ford, District 1
Current Term: 2010-2014
Community & Personnel Relations Committee



Members of the Hilton Head PSD Commission are joined by other utility leaders for a presentation on saltwater intrusion by hydrogeologist Dr. Richard Spruill of East Carolina University. The PSD Commission frequently provides a forum for discussions on water supply issues affecting the region.

Administrative Team

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



A Message from the General Manager



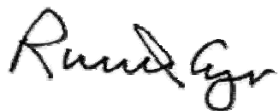
Richard C. Cyr

This Comprehensive Annual Financial Report provides an overview of Hilton Head Public Service District's financial performance and updates you on some of our most vital work. Hilton Head PSD's most important duties are the protection of public health and our island's environment. We achieve this by providing high-quality drinking water and through effective wastewater treatment that results in beneficial reused water. We're a small team focused on providing excellent value to our customers.

The PSD continues to use strategic planning in ensuring we maintain reasonable costs for our customers while continuing to provide high-quality service. Our cost-of-service and water-efficiency rate structure means that our rates cover the utility's expenses in providing our services while encouraging customers to save money and our natural resource by using less water. Hilton Head PSD has a strong history of phasing in rate adjustments that are reasonable for our customers and keep the utility on solid financial footing.

Smart planning, conducted alongside our elected Board of Commissioners, has put the PSD in excellent shape to meet the challenges of tomorrow while providing top-notch services today. The men and women who work for Hilton Head PSD are our most important asset. Their expertise and experience shines through 24/7, 365 days a year as we embody the PSD's motto: ***We're Always Working for You!***

Best Regards,

A handwritten signature in black ink, appearing to read "Richard Cyr". The signature is fluid and cursive.

Richard C. Cyr
General Manager
Hilton Head PSD

HILTON HEAD PUBLIC SERVICE DISTRICT

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 20, 2011

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 – Water Reclamation Services: Meet all of the District's wastewater process and reclamation services at a reasonable cost while enhancing and protecting the Island's environment.

Goal No. 3 – Environmental: Operate in a sustainable manner with high 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 under the guidance of careful strategic planning.

Goal No. 7 – Asset Management: Improve, maintain and secure the District's property, information, 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 more than 18,000 residential and commercial customers in the north and mid-island areas of Hilton Head Island, SC.
- Drinking water sources are: brackish groundwater from the 600-foot-deep Middle Floridan Aquifer treated in Reverse Osmosis Plant that began operations in April 2009; fresh groundwater from the 150-to-300-foot-deep Upper Floridan Aquifer; and treated Savannah River surface water purchased from the Beaufort-Jasper Water & Sewer Authority.
- Utilizes an Aquifer Storage & Recovery (ASR) well, which stores treated drinking water in the Middle Floridan Aquifer during times of low demand, and withdraws and retreats the water for distribution during times of high or peak demand – providing 2 million gallons a day during the summer months.
- 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 more than 1 billion gallons of reclaimed water for golf course irrigation and wetlands nourishment.

Priorities and Projects

Fiscal Year 2012 Highlights

The PSD's significant accomplishments during the past fiscal year included:

- Placed our Aquifer Storage & Recovery (ASR) well into operation – a key component of our alternative water supply and water distribution improvement program.
- Completed sewer installation projects in the Stoney neighborhood in conjunction with the Town of Hilton Head Island's Tax Increment Finance District, a program to improve quality of life and generate economic development.
- Obtained a commitment from the Town of Hilton Head Island to fund \$1.2 million in sewer projects for the Spanish Wells and Baygall neighborhoods.
- Completed an Automated Meter Information (AMI) pilot study.
- Completed a Water System Hydraulic Study, which resulted in improvements to our water-supply planning.
- Refinanced State Revolving Fund loans, resulting in a net present value savings of \$312,500 in future interest and bond expenses.
- Completed an array of wastewater treatment and reused water infrastructure improvements, including: new grit removal; new reused lagoon liners; Port Royal Plantation sewer trunk line; and rehabilitation of the biosolids dewatering centrifuge.
- Completed efficiency studies of our Reused Water Plant and overall electricity use, and implemented multiple recommendations.
- Reorganized our Operations Department to improve efficiency, customer service and system operation and maintenance.

The Saltwater Intrusion Battle Continues

Hilton Head PSD in 2012 continued its efforts to replace drinking water supply it has lost as a result of saltwater intrusion into the 150-foot-deep Upper Floridan Aquifer – the island’s original source of drinking water. The PSD has lost six drinking water wells since 2000 as a result of saltwater intrusion and anticipates losing five of its six remaining wells by 2025. The intrusion is being caused by the over-pumping of the aquifer in the Savannah, Ga., area and by naturally occurring phenomena. Studies currently show that the saltwater is advancing through the aquifer at a rate of about 400 feet a year and there is nothing the PSD can do on its own to reduce or stop the intrusion.

Hilton Head PSD, under the leadership of General Manager Richard Cyr, has been at the forefront of the regional issue of saltwater intrusion. The utility has responded to the water-supply crunch in a variety of ways. It has reduced its use of the Upper Floridan Aquifer. Today, the Upper Floridan accounts for less than 30 percent of the PSD’s water supply. Prior to 1999, it constituted 100 percent of the supply. The PSD has continued its reused water program, which saves potable water by recycling more than 1 billion gallons of treated wastewater a year. This water is reused for golf course irrigation and wetlands nourishment. The PSD also has worked to educate customers about the issue of saltwater intrusion and to encourage the efficient use of water.

The utility has planned for and implemented capital projects to provide alternative water supplies. In 2009, the PSD began use of its Reverse Osmosis (RO) Drinking Water Treatment Facility, which provides 3 million gallons of drinking water a day and is expandable to provide 6 million gallons a day. The RO plant treats brackish groundwater that is drawn from the 600-foot-deep Middle Floridan Aquifer. The PSD is the first utility in the region to develop the Middle Floridan into a source of drinking water.

In 2012, the PSD began providing drinking water from its Aquifer Storage & Recovery (ASR) well. The well stores treated drinking water in the Middle Floridan Aquifer during times of low demand. It then withdraws and retreats the water for distribution during times of high or peak demand. This is the first ASR well to be implemented on Hilton Head Island. It provides 2 million gallons of drinking water a day in the summer months.

Informal estimates show that since 1998 the PSD has spent \$77 million combatting saltwater intrusion, which includes costs related to capital projects, debt service, operations, and purchasing more wholesale water. The utility anticipates it may need to expend another \$50 million in the next 20 years on similar saltwater-intrusion related costs. The PSD’s planning for capital projects has involved scientific, operational and financial planning, and has included multiple stakeholders, such as the PSD Board of Commissioners and the utility’s regulators at the South Carolina Department of Health and Environmental Control.

Our Sewer Extension Program

Hilton Head PSD and the Town of Hilton Head Island in 2012 continued their partnership to extend public sewer service throughout the PSD’s service area. A series of projects completed in 2011 and 2012 has brought sewer access to approximately 200 properties along Squire Pope and Wildhorse roads and William Hilton Parkway, in both the Stoney and Chaplin neighborhoods. These projects have been made possible through the Town’s Tax Increment Finance (TIF) District in the project areas. TIF is a funding method of allocating tax revenues to create public owned projects that stimulate private investment and improve the quality of life on Hilton Head Island. The public sewer system, which has long been desired in the neighborhoods that comprise the TIF District, is critical in providing a high quality of life on the island.

The partnership kept going strong in 2012 as the Town Council voted to provide \$1.2 million from the Town's Capital Improvement Program (CIP) to install sewer infrastructure in the Spanish Wells and Baygall neighborhoods, which are the primary areas still in need of sewer access. Those projects entered the design and permitting stages in late 2012 and are on track for implementation in 2013.

The PSD's sewer extension efforts have come a long way in a relatively short period of time. In 2003, approximately 80 percent of all properties in the District's service area had access to the public sewer system. Today, approximately 96 percent of all properties in the PSD service area have sewer access. That leaves about 1,000 properties awaiting sewer access.

The PSD's front-foot assessment method of financing customer sewer projects provides property owners with a long-term, low-interest financing option to pay for their sewer connection. The assessment is placed on owners' Beaufort County, S.C. property tax bill.

Project SAFE



Project SAFE (Sewer Access for Everyone) is one of the most important tools used by the PSD to offer sewer access throughout our service area. Project SAFE is a fund managed by the nonprofit Community Foundation of the Lowcountry. It provides income-based grants to low-to-moderate income homeowners. The PSD assists customers in the application process, and the Foundation makes all grant award determinations. Homeowners can receive partial or full grants to cover their connection costs.

Unfortunately, many of the homes that are without sewer connection are owned by low-income families that struggle to meet the cost of installing sewer. These homes are relying upon septic systems that are ill-suited for the island's high groundwater table and numerous tree roots. Septic system failures can be common on Hilton Head. These failures can pose a threat to public health and to the island's environment and waterways. Public health protection and environmental stewardship have resulted in the PSD and the Town of Hilton Head Island developing a shared goal of eliminating septic system usage on the island.

Project SAFE has been the chief vehicle for providing assistance to low-income families seeking sewer connection. The fund is backed by the generosity of PSD customers, who annually contribute more than \$35,000 to Project SAFE. More than \$280,000 has been donated to SAFE since 2001, which has helped more than 120 families connect to sewer.

Project SAFE's role will continue to be critical to the sewer extension effort as the PSD works toward completion of the final projects needed to provide sewer access throughout its service area.



Some parts of Hilton Head Island still lack sewer access and are in need of Project SAFE's assistance



A partnership between Hilton Head PSD and the Town of Hilton Head Island has helped extend the public sewer system

COMMISSIONERS

Bob Manne, Chair
Bob Gentzler, Vice-Chair
John Geisler, Secretary
Gary Kratz, Treasurer
Jack Burke
Frank J. Drehwing
Herbert Ford

**EXECUTIVE STAFF**

Richard C. Cyr, General Manager
William C. Davis, Operations Manager
Larry M. Sapp, Finance Manager
Pete Nardi, Community Relations Manager

HILTON HEAD PUBLIC SERVICE DISTRICT

October 26, 2012

Management Letter of Transmittal

The Commission and staff of the PSD are pleased to present the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2012. This is the third report issued as a CAFR and it will be made available to the general public via the 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 contains the report of the independent auditor, management's discussion and analysis, the PSD's financial statements, and supplemental financial data. The Statistical section includes 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.

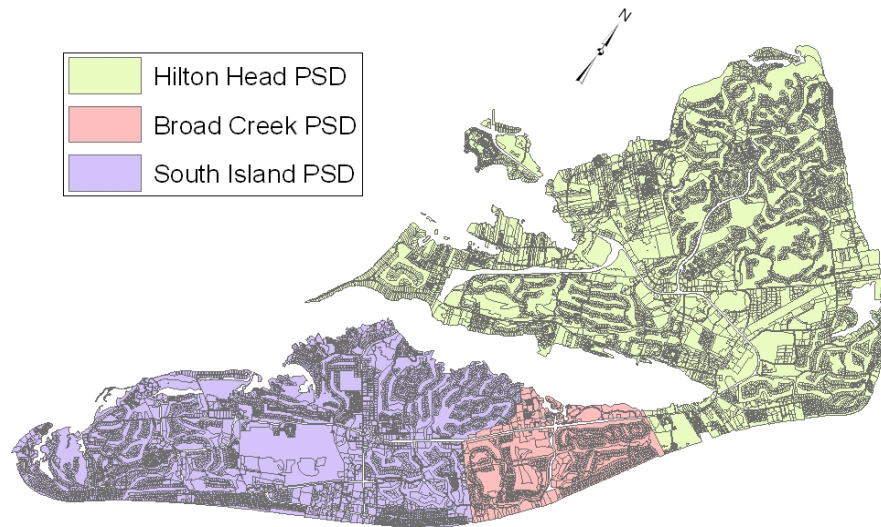
Residents of Hilton Head Island relied upon private wells for their drinking water needs until 1957. At that time, a private development firm introduced a community waterworks system, installing water lines and drilling wells throughout the island.

The island was once served by 10 different water and wastewater utilities. Beginning in 1995, the PSD acquired the four utilities that now encompass its current service area. In addition, the PSD 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, Hilton Head 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:



Our Sources of Water

Hilton Head PSD uses three sources of drinking water. This diversity of supply is a necessary response to saltwater intrusion into our traditional groundwater source. It also is an important recovery tool in the event of a hurricane or other disaster. The three sources are blended in the PSD's drinking water distribution system, at varying rates depending upon time of year, time of day, or other factors.

The PSD supplies its customers with an average of 6 million gallons of drinking water a day – more than 2 billion gallons a year – using our three sources. The sources are:

- Groundwater from the Middle Floridan Aquifer treated at the PSD's Reverse Osmosis (RO) Drinking Water Treatment Facility.
- Treated Savannah River surface water purchased wholesale by the PSD from the Beaufort-Jasper Water & Sewer Authority (BJWSA). The PSD buys wholesale water at an off-peak rate during the winter months and stores it in our new Aquifer Storage & Recovery (ASR) well for re-treatment and distribution during the summer months when both demand and the wholesale water rate increase.
- Groundwater from the Upper Floridan Aquifer treated with chloramine injection at well sites.

The past year saw the RO facility provide 41 percent of the PSD's overall drinking water supply, while Savannah River surface water and Upper Floridan wells comprised 32 and 27 percent of the overall supply, respectively.

The Reverse Osmosis Facility

The PSD's primary source of 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 April 2009. It provides 3 MGD of drinking water, about half of the PSD's average daily demand, and is expandable to provide 6 MGD. The facility was needed in order to replace water supply lost as a result of saltwater intrusion into the island's traditional source of water, the 150-foot-deep Upper Floridan Aquifer.

The RO Facility earned a National Recognition Award in the American Council of Engineering Companies (ACEC) Engineering Excellence Awards competition. The award is presented to projects that demonstrate exceptional achievement in engineering. The facility was designed and built by AECOM engineering company in Greenville, S.C. The plant also was awarded an Engineering Excellence Award from the South Carolina chapter of the ACEC.

The RO Facility incorporates sustainable principles into its design. Water recovery is maximized using technologically-advanced membrane design and lower-pressure membranes to reduce power consumption.



Interior of the RO Facility



RO Facility



RO Filter Tubes

Surface Water and ASR

The second source for potable and irrigation water is the Savannah River. The District purchases treated Savannah River surface water from the Beaufort-Jasper Water and Sewer Authority (BJWSA), via a contract between the two utilities. The PSD has the right to draw up to 4 MGD of treated surface water under the contract. In September 2009, the PSD entered into an off-peak water purchasing contract with BJWSA, which provides for the purchase of water in the late-fall and winter months at a dramatically reduced rate. During the designated off-peak period, the reduced rate is applied to all water purchased in excess of the 1 MGD minimum that the PSD must purchase under the contract with BJWSA.

The off-peak rate is used in conjunction with the PSD's new Aquifer Storage & Recovery (ASR) well. ASR is a water storage and distribution technique. The PSD purchases treated Savannah River surface water during the winter months using the off-peak rate. That water is injected into the 600-foot-deep Middle Floridan Aquifer using the ASR well. A freshwater bubble is created underground through this injection. The ASR well then is used to withdraw and retreat the water for distribution during the summer months, when demand and the wholesale cost of surface water increase. This process allows the PSD to minimize its use of the more expensive wholesale surface water during the summer. The ASR well, located inside Hilton Head Plantation, gives the PSD nearly 400 million gallons of stored water. The well yields 2 MGD during the summer months

and provides a key pressure zone to optimize the distribution of drinking water in our system. The PSD's ASR well is the first-ever ASR well installed on Hilton Head Island.



The ASR Well

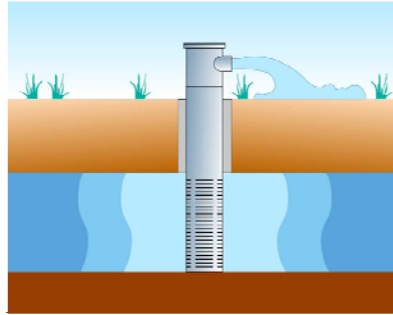


Diagram of ASR



ASR Well Control Building

Upper Floridan Wells

The PSD's third source of water is fresh water from the Upper Floridan Aquifer, located approximately 150 to 200 feet below sea level. It is the island's original source of drinking water. The fresh groundwater requires very little treatment and is an inexpensive source of water. Unfortunately, this source has been diminished as a result of saltwater intrusion into the aquifer. The utility has lost six Upper Floridan wells as a result of saltwater intrusion since 2000. The PSD anticipates losing five of its six remaining Upper Floridan wells by 2024, as the saltwater advances from Port Royal Sound south through Hilton Head Island at a rate of about 400 feet a year.



Upper Floridan Well House



Upper Floridan Well & Pump



Water Quality Field Test

Reused Water

Hilton Head Island is a 100-percent reused water community. That means that all municipal wastewater generated here is reused for beneficial purposes. Hilton Head PSD alone recycles more than 1 billion gallons of treated wastewater each year by reusing that water for golf-course irrigation and wetlands nourishment. Collectively, more than 3 billion gallons of treated wastewater is reused on Hilton Head each year. Hilton Head PSD's reused water is used to irrigate 11 different golf courses. It also is used to nourish four, distinct wetlands in Hilton Head Plantation and Palmetto Hall. Reused water plays an integral role in the island's economy by providing an affordable source of irrigation water for our golf industry. The wetlands provide vital habitat for numerous species – these rare ecosystems would struggle to survive without the reused water program.



Whooping Crane Wetlands



Cypress Wetlands



Reused Golf Irrigation

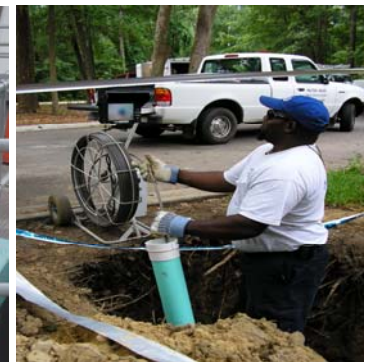
Hilton Head PSD operates a 6.4-MGD wastewater treatment plant. The plant has more than enough treatment capacity to meet the PSD service area's build-out scenario. The PSD has lagoons and ground-level storage tanks that allow us to store 45 million gallons of reused water. The utility's sewer system includes more than 110 sewer pump stations located throughout our service area. The PSD conducts ongoing maintenance of our sewer system, including a program in which we clean and run cameras through our sewer lines in order to verify the integrity of the lines.



Wastewater treatment headworks



Grit removal



Sewer line inspection

Community Outreach

The PSD believes in maintaining stakeholder relationships through a proactive community outreach effort. We regularly communicate to customers through our direct-mail newsletter, *On the Waterfront*, and our annual Water Quality Report. PSD staff members give presentations to community groups throughout the year on topics such as our alternative water supply planning and our reused water system. We have partnered with renowned environmental scientist Todd Ballantine to provide customer education about the beneficial reused water program and its role in providing wetlands habitat. The PSD provides updates on its activities through the local news media and also through social media platforms such as our "Liquid Letter" blog.

The PSD's Community Room, located at the Water Resource Center, is a gathering place for scores of community groups that would otherwise have no public meeting space available to them on Hilton Head Island. The room is used by a wide array of community members, from property owners' associations and civic groups to programs for special-needs adults and professional trade associations. The Community Room also is the site of training programs for PSD staff members and joint training sessions held in conjunction with the island's other PSDs.

In October 2012, PSD Commissioner Frank Drehwing and General Manager Richard Cyr gave a presentation entitled "Hilton Head PSD Groundwater Crisis Management: Past – Present – Future" at the Water Environment Federation's annual WEFTEC conference. The presentation focused upon the extensive

planning and community outreach that has gone into the PSD's ongoing alternative water supply efforts in response to the saltwater intrusion into the Upper Floridan Aquifer.

Cyr also joined South Island PSD General Manager Kelley Ferda and Broad Creek PSD General Manager Rusty Hildebrand for a presentation to the Beaufort County Council in September 2012 that updated the council on the PSDs' collective response to saltwater intrusion. This outreach highlighted the regional nature of the problem and the extensive steps taken by Hilton Head Island's water utilities to replace lost water supply.



Richard Cyr at County Council



PSD at WEFTEC



Fire Department Demo at Island Rec

PSD Staff

The PSD staff consists of 35 employees working in a variety of job functions. The utility's small size means that staff members must be flexible and able to work across a range of duties. Our technicians are licensed by the State of South Carolina and work on the operations and maintenance of the water distribution, wastewater collections and treatment and reused water systems. PSD staff members maintain professional excellence through continuing education through our utility trade associations such as the Water Environment Association of South Carolina and the state chapter of the American Water Works Association. Our Water Quality Laboratory is licensed by the U.S. Environmental Protection Agency (EPA), and our wastewater treatment plant annually is audited by the South Carolina Department of Health & Environmental Control (DHEC) for compliance with all applicable environmental regulations.

Our water quality is monitored by our own Water Quality Laboratory, which must submit its testing results weekly to DHEC. The annual results of our water quality monitoring are reported to our customers in our Water Quality Report. The PSD annually tests more than 500 samples of our water, which is subject to more than 100 primary and 15 secondary standards regulated by the U.S. EPA. In addition, we voluntarily test for unregulated substances. The PSD's water and wastewater systems are monitored 24/7 by a state-of-the-art computer system that gives our technicians real-time data and system control.



Technicians make a repair



Project mapping



Laboratory testing

Waterworks System

The District's waterworks system currently consists of the following components: (a) six Upper Floridan Aquifer wells with treatment, (b) five elevated storage tanks with a total capacity of 1,350,000 gallons; (c) one 2,000,000 gallon ground storage tank; (d) four booster pump stations; (e) approximately 1,268,678 linear feet of water line ranging in size from 2 inches to 20 inches in diameter; (f) a 3.0 million gallon per day (MGD) capacity reverse osmosis water treatment facility (the "RO Facility"); and (g) an aquifer storage and recovery well with 240 MG withdrawal capacity. 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 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. For fiscal year 2011, the Off-Peak Rate is \$0.76 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 17,495 water taps (comprising 10,565 residential taps, 4,850 master metered residential and 2,080 commercial water taps) in 2012. 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 15,109 customers (comprising 8,847 residential, 4,850 master metered residential, and 1,412 commercial) on June 30, 2012. 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 with costs 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 Commission approved budget revision.

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.

The Finance Committee of the Board of Commissioners 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.

As stated in the District's financial policies, all user charges and fees are set 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).

Cost 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.

In compliance with the District's financial policies, water and sewer rate increases are minimized whenever possible. However, both water and sewer rate increases have been necessary in the past to sustain necessary revenues to support related water and sewer expenses. The following two paragraphs cover both the water and sewer rate increases which have occurred over the past ten years.

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. The most recent water rate increase took place on May 1, 2011 and was the first in almost 12 years to increase the water base rate charge.¹ The first consumption tier for residential irrigation was also increased from \$1.40 to \$1.71 for the first 10,000 gallons of irrigation consumption. For a summary of the District's historical and present water rates, please reference the Water Rates Comparisons Table in the Statistical Section on page 88.

¹ The water base rate was increased by \$1.00 per unit for all customers.

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. On October 1, 2009, another sewer rate increase was put into effect increasing both residential and commercial consumption rates by \$0.10 per thousand gallons. The most recent sewer rate increase took place on May 1, 2011 and was also the first in almost 12 years to increase the sewer base rate charge.² The commercial sewer volume charge also was adjusted from \$1.60 to \$2.00 per 1,000 gallons of water consumption. For a summary of the District's historical and present sewer rates, please reference the Wastewater Rates Comparison Table in the Statistical Section on page 88.

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

² The sewer base rate was increased by \$2.00 per unit for all customers.

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

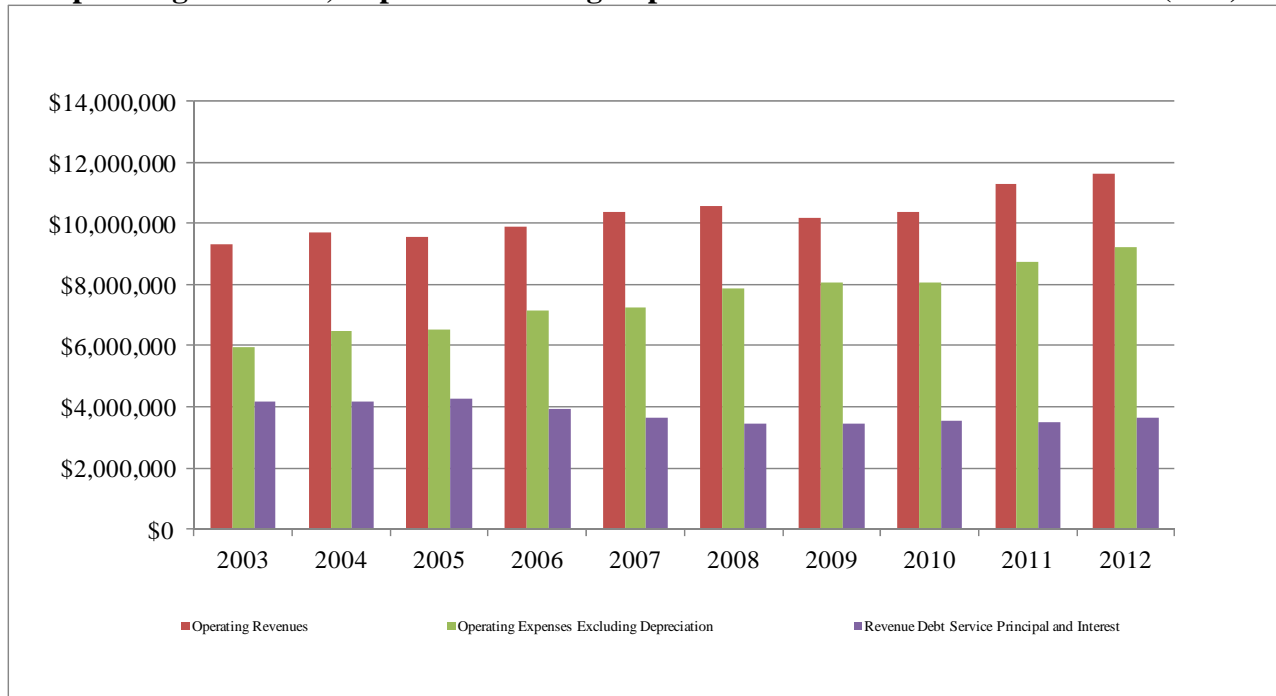
7. to purchase capital equipment and make expenditures related to the installation, operation, and purchase of the capital equipment including, but not limited to, taxes, duty, transportation, delivery, and transit insurance, in a county having a population of less than one hundred thousand persons and 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

Operating revenues, operating expenses (excluding depreciation), and revenue related debt service payments for the past ten fiscal years are summarized in the following graph.

Operating Revenues, Expense Excluding Depreciation and Revenue Debt Service (P&I)

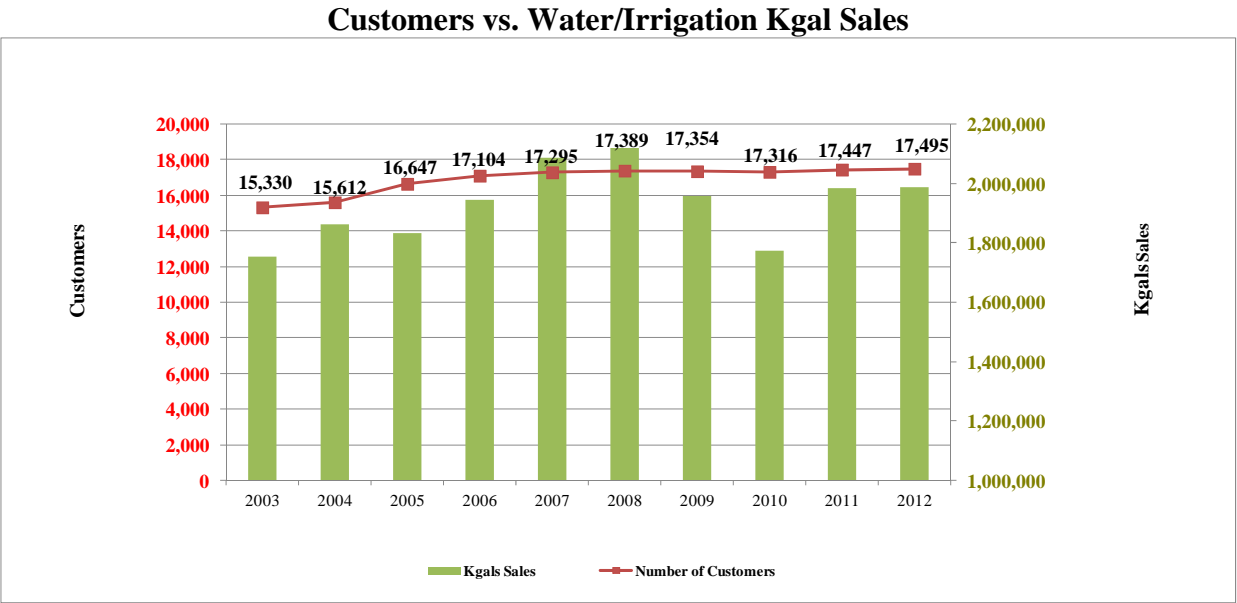


Billed water consumption for fiscal 2012 was just slightly higher than fiscal year 2011, but combined water and sewer revenues increased by \$427,000 (rounded) or 4.2% due to a water and sewer rate increase put into effect on May 1, 2011. While operating revenues increased by \$358,000 (rounded) or 3.2% for fiscal year 2012, departmental expenses increased \$484,000 (rounded) or 5.6 percent mainly due to increased operations, payroll & related and professional fees expenses. Departmental expenses are covered in more detail in the Management Discussion and Analysis section of this report on page 38.

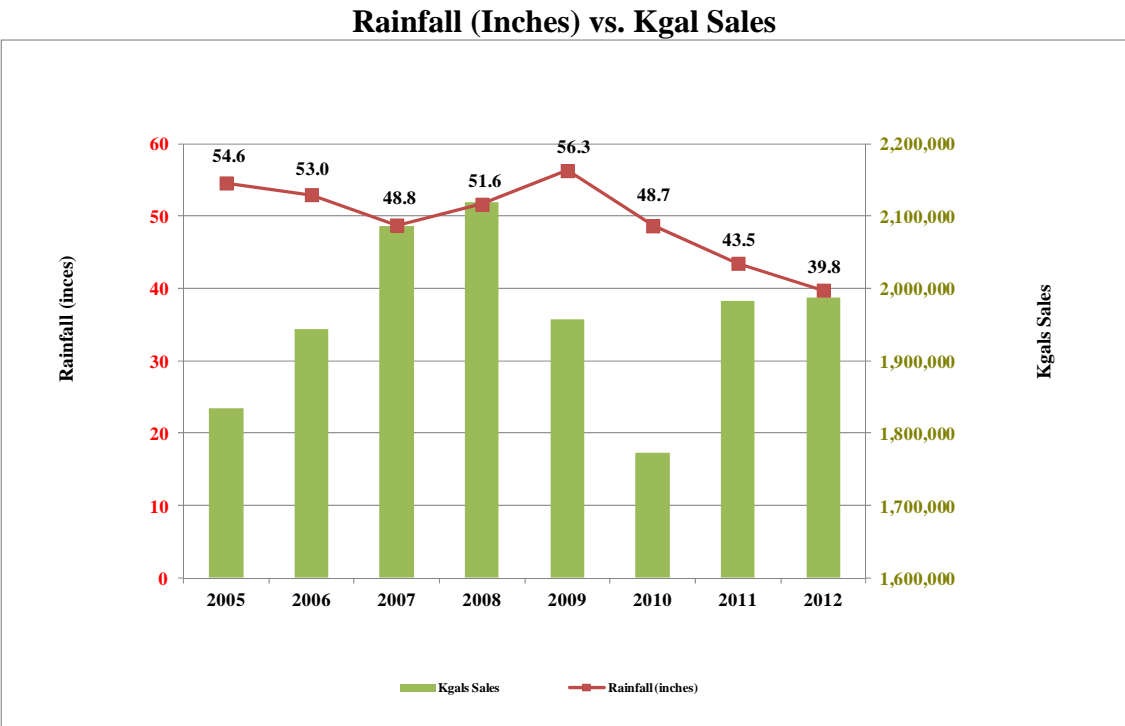
Fiscal year 2011 billed consumption rebounded to its highest level since fiscal year 2008 resulting in higher revenues. Water/irrigation consumption increased 11.8% or 210 million gallons for fiscal year 2011 when compared to fiscal year 2010. Higher consumption levels and resulting higher revenues for fiscal year 2011 were mainly due to more seasonable weather and higher island occupancy rates for both housing and, to a higher degree, tourism. The combined home, villa and hotel occupancy percentage increased by 1 percent for Hilton Head Island for fiscal year 2011 when compared to fiscal year 2010.³ Combined with more seasonable weather was the fact that the District's area also had 5.2 less inches of rainfall compared to fiscal year 2010. Only a very small portion of increased revenues for fiscal year 2011 can be attributed to the water and sewer rate increase (reference page 21 of the Rates and Charges Section) put into effect on May 1, 2011.

³ Source: The Hilton Head Chamber of Commerce, <http://www.thinkhiltonheadisland.org/article-details?hhaid=54>.

The following table shows customer counts in relation to water and irrigation Kgal sales. While typically more customers equates to more water consumed, there is no evident direct relationship between the District’s customer counts and overall consumption levels due to the other variables that influence customer water consumption (e.g. weather, economy).



The following chart is a comparison of rainfall amounts in relation to water and irrigation Kgal sales.



Despite lower rainfall amounts for fiscal years 2010, 2011 and 2012, respective water consumption levels were also low when compared to past fiscal years with higher rainfall such as 2007 and 2008. As previously discussed, other seasonal factors such as temperature and economic influences such as new housing development, housing vacancies, and tourism occupancy levels also have a material effect on customer water consumption levels.

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.

Certificate of Achievement for Excellence in Financial Reporting


The Government Finance Officer Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to Hilton Head Public Service District for its comprehensive annual financial report for the fiscal year ended June 30, 2011. This was the second year that the District achieved this prestigious award. In order to be awarded a Certificate of Achievement, a government must establish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. Management believes that the current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements and is submitting it to the GFOA to determine its eligibility for another certificate.

Final Comments

Management has developed policies and procedures that direct personnel actions toward the Board's adopted mission of providing high quality water and sewer service to all properties within the District and provide those services at a reasonable cost. Further, the Board adopted the District's Strategic Goals in November 2011. These goals support the District's mission and are reviewed annually during the early planning process of creating staff work plans for the upcoming fiscal budgeting process.

We are thankful to all District employees for their hard work and dedication. Additionally, we would like to recognize the District's General Manager and Board of Directors for their leadership, support, and continued commitment to excellence.



Larry Sapp, CGFO, Finance Manager



Brian Cronin, Senior Accountant

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Hilton Head Public Service
District, South Carolina

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2011

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



Linda C. Sanborn
President
Jeffrey R. Ennis
Executive Director

FINANCIAL



Robinson Grant & Co., P.A.

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INDEPENDENT AUDITORS' REPORT

October 26, 2012

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

We have audited the accompanying balance sheets of Hilton Head No. 1 Public Service District (the "District") as of June 30, 2012 and 2011, 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, 2012 and 2011, 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 certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements as a whole. 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.

Robinson Grant & Co., P.A.

Management's Discussion and Analysis

This section of the Hilton Head No. 1 Public Service District's (the "District") annual financial statements presents our analysis of the District's financial performance during the fiscal years ending June 30, 2012, 2011 and 2010. Please read it in conjunction with the unaudited financial statements contained in this section.

Financial Highlights

- Total assets at the end of the fiscal year 2012 were approximately \$93.75 million, exceeding liabilities by \$37.77 million (See Table A-1, Page 33).
- On August 23, 2011, the District refinanced the Series 2000A SRF Revenue Bond which resulted in a total of \$312,458 in net present value savings. Through this refinancing the District was able to lower the effective bond interest rate from 3.50% to 2.89%. The District also eliminated the Letter of Credit that was funding the Debt Service Reserve Fund. This bond closed on August 24, 2011 with an annual savings is \$43,855, which includes cost savings attributable to the elimination of the Letters of Credit.
- During October 2011, the South Carolina Budget and Control Board contacted the District regarding the FY 2012 Amendment for all prior SRF Loan Policies related to its State Drinking Water Revolving Loan Funds (DWSRF). The amendment relates to the interest rates and debt service funds on all currently outstanding SRF loans. Interest rate reductions are available during FY 2012 as a one time opportunity until June 30, 2012. Staff submitted a formal written request during October requesting the Budget and Control Board to re-amortize the outstanding principal balance of the District Series 2007 SRF GO Bonds. As of November 2011, the District received the revised Loan Agreement for the interest rate reductions. The interest rate reduction lowers the permanent quarterly payment from \$48,135 to \$45,350, thereby saving the District \$11,138 annually and \$189,344 over the remaining term of the loan. The new quarterly payments were effective January 1, 2012.
- Water Customer Growth: The District added 48 new water/irrigation taps to the system in fiscal year 2012. As of June 30, 2012, the District has a total of 17,495 equivalent dwelling units (EDUs). This is a 0.3% increase for FY'12. For FY'11 there was a 0.8% increase in total EDUs. The current EDUs consist of 16,441 water service units, 1,003 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>
2012	10,565	4,850	2,080	17,495	0.3%
2011	10,527	4,843	2,077	17,447	0.8%
2010	10,415	4,843	2,058	17,316	-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: The District added 79 new sewer connections to the system in fiscal year 2012. As of June 30, 2012, sewer service EDUs total 15,109. This is a 0.5% increase for FY'12 as compared to the FY'11 increase of 0.9% or 139 EDUs.

Sewer Customers

<u>Fiscal Year</u>	<u>Residential</u>	<u>Master Metered Residential</u>	<u>Commercial</u>	<u>Total</u>	<u>% Growth</u>
2012	8,847	4,850	1,412	15,109	0.5%
2011	8,775	4,843	1,412	15,030	0.9%
2010	8,653	4,843	1,395	14,891	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 91.90% percent since the beginning of fiscal year 2011.⁴

Sewer Connection Growth 06/30/2012								
<u>Date</u>	<u>All Water/Irrigation EDU's</u>	<u>Water EDU's</u>	<u>Inactive Water EDU's</u>	<u>Change in Water EDU's</u>	<u>Sewer EDU's</u>	<u>Inactive Sewer EDU's</u>	<u>Change in Sewer EDU's</u>	<u>% Water to Sewer EDU's</u>
06/30/11	17,447	16,395	318	N/A	15,030	165	N/A	91.67%
09/30/11	17,452	16,398	295	3	15,037	143	7	91.70%
12/31/11	17,452	16,397	316	-1	15,047	154	10	91.77%
03/31/12	17,451	16,399	328	2	15,065	165	18	91.87%
06/30/12	17,495	16,441	327	<u>42</u>	15,109	165	<u>44</u>	91.90%
Total EDU's Added				<u>46</u>			<u>79</u>	

Subsequent Events

- On October 23, 2012 the Board approved a motion to set a rate hearing for November 13, 2012. The associated proposed rate change would increase the water base rate by \$1.00 for each billing unit and also increase the sewer base rate by \$1.00 for each sewer billing unit. The proposed effective date of this rate change is January 1, 2013.
- On October 23, 2012 the Board adopted a resolution providing for the issuance and sale of waterworks and sewer system refunding revenue bonds, the Series 2004 Revenue Bonds, designated Series 2012A (taxable) in the principal amount not exceeding fourteen million dollars (\$14,000,000), and waterworks and sewer system improvement revenue bonds to be designated Series 2012B (tax exempt), in the principal amount of not exceeding one million dollars (\$1,000,000), to fund two new lift stations. The anticipated closing date is scheduled for November 29, 2012.

⁴ This percentage is based solely on water customers and does not include irrigation, dock meters, hydrants, pool meters, and golf course water coolers etc.

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, 2012, 2011, and 2010

Year Ended June 30,	2012	2011	2010	2012 to 2011	%
Assets				Increase (decrease)	
Current assets	\$ 5,323,289	\$ 5,398,683	\$ 5,118,206	\$ (75,394)	-1.4%
Restricted assets	3,432,491	5,578,182	2,378,848	(2,145,692)	-38.5%
Net Property Plant & Equipment	80,998,121	81,348,684	80,515,057	(350,563)	-0.4%
Sewer Assessments, Long-term	3,042,577	3,459,654	3,329,883	(417,078)	-12.1%
Other	956,911	1,121,928	946,120	(165,016)	-14.7%
Total Assets	<u>93,753,389</u>	<u>96,907,131</u>	<u>92,288,114</u>	<u>(3,153,742)</u>	<u>-3.3%</u>
Liabilities					
Current Liabilities	5,146,421	4,770,476	4,577,296	375,945	7.9%
Noncurrent Liabilities, net of amortization	50,833,268	54,223,011	49,147,698	(3,389,743)	-6.3%
Total Liabilities	<u>55,979,689</u>	<u>58,993,487</u>	<u>53,724,994</u>	<u>(3,013,798)</u>	<u>-5.1%</u>
Net Assets					
Invested in capital assets, net	27,561,464	27,806,556	29,464,863	(245,091)	-0.9%
Restricted for debt service	3,419,743	2,779,466	2,378,848	640,277	23.0%
Unrestricted	6,792,493	7,327,622	6,719,409	(535,130)	-7.3%
Total Net Assets	<u>37,773,700</u>	<u>37,913,644</u>	<u>38,563,120</u>	<u>(139,944)</u>	<u>-0.4%</u>
Total Liabilities and Net Assets	<u>\$ 93,753,389</u>	<u>\$ 96,907,131</u>	<u>\$ 92,288,114</u>	<u>\$ (3,153,742)</u>	<u>-3.3%</u>

Net Assets

Changes in net assets result from operating and non-operating revenues, expenses and contributions of capital. Net assets are classified under the following three components: 1) *invested in capital assets, net of related debt*; 2) *restricted for capital activity and debt service*; and 3) *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 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 net assets consists of all other net assets not included in the above categories.

Total net assets as of June 30, 2012 were \$37,773,700 representing a \$139,944 decrease from the prior year. Fiscal year 2011 had a decrease in total net assets from fiscal year 2010 of \$649,476 or 1.7% due to decreased capital contributions.

Year Ended June 30,	Change in Net Assets		
	2012	2011	2010
Invested in Capital assets, net	\$ 27,561,464	\$ 27,806,556	\$ 29,464,863
Restricted for debt service	3,419,743	2,779,466	2,378,848
Unrestricted	6,792,493	7,327,622	6,719,409
Total Net Assets	<u>\$ 37,773,700</u>	<u>\$ 37,913,644</u>	<u>\$ 38,563,120</u>

Of the total net assets, \$5,323,289 million are current non-restricted assets available to support short-term operations (see Table A-1, page 33). This current asset balance is \$75,394 lower than on June 30, 2011.

Capital Assets

As of June 30, 2012, the District has invested \$80,998,121 (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 \$350,563 during fiscal year 2012. More detailed information on capital asset activity can be found in Note 5 – Property, plant, equipment and depreciation on page 57 and 58.

TABLE A-2
Capital Assets

Year Ended June 30,	2012	2011	2010
<u>Capital assets not being depreciated:</u>			
Land	\$ 1,299,194	\$ 1,299,194	\$ 1,299,194
Construction in Progress	<u>553,892</u>	<u>3,514,449</u>	<u>1,236,180</u>
Total Capital Assets not being depreciated	1,853,086	4,813,643	2,535,374
 Capital assets being depreciated:			
Waterworks system	55,352,880	51,387,113	51,089,748
Sewage disposal system	35,040,328	31,986,552	29,397,184
Buildings	4,299,512	4,299,512	4,299,512
Sewage treatment facilities	34,711,422	34,711,422	34,711,422
Transportation equipment	915,148	915,148	912,121
Operations furniture and equipment	1,681,614	1,639,985	1,626,043
Office furniture and equipment	<u>701,878</u>	<u>693,249</u>	<u>679,868</u>
Sub Total	\$ 132,702,782	\$ 125,632,981	\$ 122,715,898
Less Accumulated depreciation	<u>(53,557,747)</u>	<u>(49,097,940)</u>	<u>(44,736,215)</u>
Total capital assets being depreciated, net	79,145,035	76,535,041	77,979,683
 Property, Plant and Equipment, net	 80,998,121	 81,348,684	 80,515,057

Non-current Liabilities and Debt Administration

As of June 30, 2012, (see Table A-1, page 33) the District had \$50,833,268 in non-current liabilities as compared to fiscal year end 2011 total of \$54,223,011. More detailed information on long term debt obligation can be found in Note 6 – Long term obligations on page 59 and Note 7 – Non-current liabilities on page 63.

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 139%.

TABLE A-3
Coverage of Debt Service

Year Ended June 30,	2012	2011	2010
Net Income(loss) before capital contributions per Financial Statements	(\$1,488,640)	(\$1,346,128)	(\$1,681,923)
Capacity Fees	394,546	309,857	242,308
Add: Depreciation	4,459,807	4,456,160	4,405,077
Amortization	211,953	209,256	202,112
Interest Expense (Bonds)	2,212,192	2,300,439	2,208,372
Assessments - Debt Service	542,991	550,586	537,759
Less: Property Taxes – Debt Service	<u>(1,233,107)</u>	<u>(1,235,347)</u>	<u>(967,418)</u>
Net Earnings Available for Debt Service	\$5,099,741	\$5,244,822	\$4,946,286
 Debt Service on Revenue Bonds	 \$3,660,650	 \$3,477,484	 \$3,523,871
 Coverage of Debt Service by Net Earnings	 139%	 151%	 140%
 Debt Coverage without Capacity Fees	 129%	 142%	 133%

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:

TABLE A-4
Hilton Head PSD
Statement of Revenues, Expenses and Changes in Net Assets and Comparison Schedule

Year Ended June 30,	2012 Actual	2011 Actual	2010 Actual	2012 to 2011 Actual	%	2011 to 2010 Actual	%
Operating Revenues	\$ 11,640,088	\$ 11,281,715	\$ 10,398,457	\$ 358,373	3.2%	\$ 883,258	8.5%
Total Non-operating Revenues	<u>2,965,412</u>	<u>3,063,851</u>	<u>2,783,767</u>	<u>(98,439)</u>	<u>-3.2%</u>	<u>280,084</u>	<u>10.1%</u>
Total Revenues	14,605,500	14,345,566	13,182,224	259,933	1.8%	1,163,342	8.8%
Departmental Expenses	9,210,189	8,725,839	8,048,586	(484,350)	-5.6%	(677,254)	-8.4%
Depreciation	4,459,807	4,456,160	4,405,077	(3,647)	-0.1%	(51,083)	-1.2%
Total Non-operating Expenses	<u>2,424,145</u>	<u>2,509,695</u>	<u>2,410,484</u>	<u>85,551</u>	<u>3.4%</u>	<u>(99,212)</u>	<u>-4.1%</u>
Total Expenses	16,094,140	15,691,694	14,864,147	(402,446)	-2.6%	(827,547)	-5.6%
Increase (decrease) in net assets before capital contributions	(1,488,640)	(1,346,128)	(1,681,923)	(142,513)	-10.6%	335,795	20.0%
Capital Contributions:							
Water Capacity Fee	162,939	148,815	34,512	14,124	9.5%	114,303	331.2%
Sewer Capacity Fee	231,607	161,042	207,796	70,565	43.8%	(46,754)	-22.5%
Developer Contributions of Systems	954,150	42,393	416,411	911,758	2150.8%	(374,018)	-89.8%
Sewer Assessments	<u>-</u>	<u>344,402</u>	<u>320,902</u>	<u>(344,402)</u>	<u>N/A</u>	<u>23,500</u>	<u>N/A</u>
Total Capital Contributions	1,348,696	696,652	979,621	652,044	93.6%	(282,969)	-28.9%
Increase (decrease) in net assets	\$ (139,944)	\$ (649,476)	\$ (702,302)	\$ 509,531	-78.5%	\$ 52,827	7.5%
Net Assets at the beginning of the year	<u>37,913,644</u>	<u>38,563,120</u>	<u>39,265,422</u>				
Net Assets at end of year	<u>\$ 37,773,700</u>	<u>\$ 37,913,644</u>	<u>\$ 38,563,120</u>				

Operating Revenues (Fiscal Year to Year Comparisons)

Operating revenues for fiscal year 2012 total \$11,640,088, which is almost 80% of total revenues (operating and non-operating) for the year. Total operating revenues have increased 3.2% or \$358,373 compared to last year's revenues mainly due to increased water and sewer service revenues which were \$426,777 higher than fiscal year 2011. Total operating revenues increased 8.5% or \$883,258 from fiscal year 2010 to fiscal year 2011.

Higher water and sewer revenues were mainly due to a rate increase which was effective as of May 1, 2011. In addition to higher water and sewer service revenues, other line items that have contributed to this year's \$358,373 operating revenue increase include the following (see Table A-5, Page 40):

- Sewer Connection Fees increased \$11,811 or 17%.
- Availability fees have increased \$27,805 or 4.6%.

The aforementioned increased operating revenue line items were somewhat offset by lower water tap in fees, service fees, and golf course irrigation revenues.

When late fees were first implemented it was standard procedure that all delinquent accounts (including final billed accounts) incur late fees. During fiscal year 2011 staff updated the late fee procedure to require that only active delinquent accounts would incur late fees. As such, final billed accounts no longer incur late fees after the final bill date, resulting in reduced service fees collections.

The other operating revenues line item includes purchase discounts and miscellaneous income; such revenues were \$64,803 lower in fiscal year 2012 due to a refund received in fiscal year 2011 which was related to Series 2000B Revenue Bond.

Total non-operating revenues were equal to \$2,965,412. 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 increased \$484,350 or 5.6% compared to fiscal year 2011 (See Table A-5, page 40). For fiscal year 2011, departmental expenses increased \$677,254 or 8.4% from fiscal year 2010.

The following departmental expense items were increased when compared to the same period last year.

- Payroll and Related expenses have increased \$98,714 or 3.1%.
- Administrative expenses have increased \$130,850 or 15% mainly due to increased bad debt expense and higher insurance for other than group/vehicle coverage. During the fiscal year 2011 audit staff completed a review of all delinquent accounts. During fiscal year 2012 staff has been working on the associated bad debt write off.
- Operations expenses have increased \$121,957 or 7.4% due to higher bio-solids disposal costs, operations chemical costs and fuel/power costs.
- Sewer Connection expense has increased \$52,085 mainly due to increased connections associated with the Stoney Project and Project Safe.
- Purchased water expense increased just slightly by \$4,334 or 0.4%.
- ASR water expense is a new line item for fiscal year 2012 and relates to water that has been drawn out of the ASR well for customer use. During May 2012, the District withdrew 21.2 million gallons from the ASR-1 well for customer consumption.
- RO Plant expenses increased \$23,269 or 4.0% mainly due to higher well maintenance and power costs.

- ASR O&M is a new line item that covers the chemical and power expense associated with the ASR well. The small associated cost for fiscal year 2012 relates to the initial testing process that took place during the third quarter of the fiscal year.
- Professional Fees increased \$72,025 or 42% due to higher professional engineering fees associated with the wastewater treatment plant evaluation and the Middle Floridan capacity analysis.
- Vehicle expenses increased \$11,311 or 9.5% due to increased fuel and maintenance costs.

These increased expenses were partially offset by lower maintenance and water tap in expenses.

TABLE A-5
Hilton Head PSD
Statement of Revenues, Expenses and Changes in Net Assets
Year to Date as of June 30, 2012 and June 30, 2011

	(With comparative amounts for the same period in prior fiscal year)		FY 2012 to FY 2011	
	FY 2012	FY 2011	Comparison	
	Actual	Actual	Dollars	%
Operating Revenues			Favorable (Unfavorable)	
Water Service	\$ 5,949,379	\$ 5,836,921	\$ 112,458	1.9%
Sewer Service	4,522,434	4,208,115	314,319	7.5%
Tap In Fees - Water	41,861	43,041	(1,181)	-2.7%
Connection Fees - Sewer	83,425	71,614	11,811	16.5%
Service Fees	51,108	73,245	(22,137)	-30.2%
Golf Course Irrigation	338,205	358,105	(19,901)	-5.6%
Availability Fees	638,137	610,332	27,805	4.6%
Other Operating Revenues	15,539	80,342	(64,803)	-80.7%
Total Operating Revenues	11,640,088	11,281,715	358,373	3.2%
Departmental Expenses				
Payroll & Related	3,330,115	3,231,400	(98,714)	-3.1%
Administrative Expenses	985,687	854,837	(130,850)	-15.3%
Operations	1,761,310	1,639,353	(121,957)	-7.4%
Maintenance	987,389	1,012,322	24,933	2.5%
Water Tap In Expenses	37,443	64,774	27,331	42.2%
Sewer Connection Expense	78,775	26,690	(52,085)	-195.1%
Purchased Water	1,028,789	1,024,455	(4,334)	-0.4%
ASR Water	16,792	-	(16,792)	N/A
RO Plant O&M	604,539	581,270	(23,269)	-4.0%
ASR O&M	5,275	-	(5,275)	N/A
Professional Fees	243,600	171,575	(72,025)	-42.0%
Vehicle	130,473	119,162	(11,311)	-9.5%
Total Departmental Expenses	9,210,189	8,725,839	(484,350)	-5.6%
Depreciation	4,459,807	4,456,160	(3,647)	-0.1%
Total Operating Expenses	13,669,995	13,181,999	(487,996)	-3.7%
Operating income (loss)	(2,029,907)	(1,900,284)	(129,623)	-6.8%
Non-operating revenues				
Property taxes-G.O. Debt Levy	1,233,107	1,235,347	(2,240)	-0.2%
Property taxes-Operations Levy	1,023,502	1,039,316	(15,814)	-1.5%
Rental Income	80,235	81,493	(1,258)	-1.5%
Interest earned	205,100	234,668	(29,568)	-12.6%
Tower lease	423,468	465,355	(41,887)	-9.0%
Gain (Loss) of disposal of equipment	-	7,672	(7,672)	N/A
Total Non-operating Revenues	2,965,412	3,063,851	(98,439)	-3.2%
Non-operating Expenses				
Interest expense-Bonds	2,212,192	2,300,439	88,247	3.8%
Bond Defeasance Amortization	238,807	233,430	(5,377)	-2.3%
Amortization of Debt Expenses	83,661	85,952	2,291	1.0%
Bond Premium Amortization	(110,515)	(110,126)	390	0.4%
Total Non-operating Expenses	2,424,145	2,509,695	85,551	3.4%
Total Non-operating Revenues/Exp.	541,267	554,156	(12,889)	-2.3%
Increase (decrease) in net assets,				
before capital contributions	(1,488,640)	(1,346,128)	(142,512)	-10.6%
Water Capacity Fee	162,939	148,815	14,124	9.5%
Sewer Capacity Fee	231,607	161,042	70,565	43.8%
Developer Contributions of Systems	954,150	42,393	911,758	2150.8%
Assessments	-	344,402	(344,402)	N/A
Total Capital Contributions	1,348,696	696,652	652,044	93.6%
Increase (decrease) in net assets	\$ (139,944)	\$ (649,476)	\$ 509,532	-78.5%
Net Assets at the beginning of the year	\$ 37,913,644			
Net Assets Year-To-Date	\$ 37,773,700			

Water and Sewer Revenues/Expenses: Fiscal Year 2012 vs. Fiscal Year 2011.
(Please reference Table A-6, Page 42)

Water Revenues and Related Expenses:

- For FY'12, total water operating revenues have increased 1.2% or \$73,369 compared to FY'11. Water service revenues increased due to the previously discussed water rate increase which was put into effect May 1, 2011. However, this increase was partially offset by lower service fees, tap in fees and lower collections of other revenues. The service fees and other revenues decreases are explained in more detail on page 38.
- Water departmental expenses increased \$217,602 or 4.3%. Departmental expense increases are explained in more detail on pages 38 and 39.
- Water operating loss for fiscal year 2012 is \$1,163,043 compared to the fiscal year 2011 loss of \$1,017,110. A difference of \$145,932 or 14%.

Sewer Revenues and Related Expenses:

- Total sewer and related operating revenues have increased 5.5% or \$285,003 mainly due the previously discussed sewer rate increase which was put into effect May 1, 2011. This increase was partially offset by lower service fees, golf course irrigation and a lower other revenues category. The service fees and other revenues decreases are explained in more detail on page 38.
- Sewer departmental expenses increased 7.2% or \$266,746. Departmental expense increases are explained in more detail on page 38 and 39.
- Sewer operating loss for fiscal year 2012 is \$866,864 compared to the fiscal year 2011 loss of \$883,174, a difference of \$16,310 or 1.8%.

TABLE A-6
Hilton Head PSD
Water vs. Sewer Fiscal Year to Year Comparison Schedule
Year to Date as of June 30, 2012
(With comparative amounts for the same period in prior fiscal year)

			FY 2012 to FY 2011	
			Comparison	
	FY 2012	FY 2011	Dollars	%
	Actual	Actual		Favorable (Unfavorable)
Operating Revenues				
Water				
Service	\$ 5,949,379	\$ 5,836,921	\$ 112,458	1.9%
Tap In Fees	41,861	43,041	(1,181)	-2.7%
Service Fees	25,554	36,623	(11,069)	-30.2%
Availability Fees	127,627	122,066	5,561	4.6%
Other Operating Revenues	7,770	40,171	(32,401)	-80.7%
Total Water Operating Revenues	6,152,191	6,078,822	73,369	1.2%
Sewer				
Service	4,522,434	4,208,115	314,319	7.5%
Connection Fees	83,425	71,614	11,811	N/A
Service Fees	25,554	36,623	(11,069)	-30.2%
Availability Fees	510,510	488,266	22,244	4.6%
Golf Course Irrigation	338,205	358,105	(19,901)	-5.6%
Other Operating Revenues	7,770	40,171	(32,401)	-80.7%
Total Sewer Operating Revenues	5,487,897	5,202,894	285,003	5.5%
Total Operating Revenues	11,640,088	11,281,716	358,372	3.2%
Departmental Expenses				
Water				
Payroll & Related	1,531,853	1,486,444	(45,409)	-3.1%
Administrative Expenses	571,699	495,806	(75,893)	-15.3%
Operations	757,363	704,922	(52,441)	-7.4%
Maintenance	523,316	536,531	13,215	2.5%
Water Tap in Expense	37,443	64,774	27,331	42.2%
Purchased Water	1,028,789	1,024,455	(4,334)	-0.4%
ASR-1 Water	16,792	-	(16,792)	N/A
ASR-1 O&M	5,275	-	(5,275)	N/A
RO Plant O&M	604,539	581,270	(23,269)	-4.0%
Professional Fees	99,876	70,346	(29,530)	-42.0%
Vehicle	60,018	54,815	(5,203)	-9.5%
Total Water Departmental Expenses	5,236,964	5,019,362	(217,602)	-4.3%
Sewer				
Payroll & Related	1,798,262	1,744,956	(53,306)	-3.1%
Administrative	413,989	359,032	(54,957)	-15.3%
Operations	1,003,947	934,431	(69,515)	-7.4%
Maintenance	464,073	475,792	11,719	2.5%
Sewer Connection Expense	78,775	26,690	(52,085)	N/A
Professional Fees	143,724	101,229	(42,495)	-42.0%
Vehicle	70,455	64,348	(6,108)	-9.5%
Total Sewer Departmental Expense	3,973,224	3,706,478	(266,746)	-7.2%
Operating Expenses before depreciation	9,210,188	8,725,840	(484,349)	-5.6%
Depreciation - Water	2,078,270	2,076,571	(1,699)	-0.1%
Depreciation - Sewer	2,381,537	2,379,589	(1,947)	-0.1%
Total Operating Expenses	13,669,995	13,182,000	(3,647)	0.0%
Water Operating income (loss)	(1,163,043)	(1,017,110)	(145,932)	-14.3%
Sewer Operating income (loss)	(866,864)	(883,174)	16,310	1.8%
Total Operating income (loss)	(2,029,907)	(1,900,284)	(129,623)	-6.8%
Non-operating revenues (expenses), net	541,267	554,156	(12,889)	2.3%
Increase (decrease) in net assets,				
before capital contributions	(1,488,640)	(1,346,128)	(142,512)	-10.6%
Capital Contributions	1,348,696	696,652	652,044	93.6%
Increase (decrease) in net assets	\$ (139,944)	\$ (649,477)	\$ 509,532	-78.5%

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. The District's website can be located at hhpsd.com.

AUDITED FINANCIAL STATEMENTS

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

BALANCE SHEETS AS OF JUNE 30, 2012 AND 2011

	<u>2012</u>	<u>2011</u>
Current assets		
Cash available for operations	\$ 2,528,695	\$ 2,447,200
Cash in banks (restricted)	2,780,037	2,174,532
Cash held by Beaufort County Treasurer (restricted)	639,706	604,935
Cash held for construction (restricted)	12,747	2,798,716
Accounts receivable - trade, net	2,026,865	2,246,649
Sewer assessments, due within one year	383,303	362,253
Inventory	240,938	237,860
Prepaid expenses	143,489	104,720
Total current assets	<u>8,755,780</u>	<u>10,976,865</u>
Noncurrent assets		
Property, plant and equipment		
Nondepreciable assets	1,853,085	4,813,643
Depreciable assets, net	<u>79,145,036</u>	<u>76,535,041</u>
Total property, plant and equipment	80,998,121	81,348,684
Sewer assessments, due after one year	3,042,577	3,459,654
Bond issuance costs, net	950,036	1,106,751
Other assets	<u>6,875</u>	<u>15,177</u>
Total noncurrent assets	84,997,609	85,930,266
Total assets	<u>\$ 93,753,389</u>	<u>\$ 96,907,131</u>

The accompanying notes are an integral part of these financial statements.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

BALANCE SHEETS AS OF JUNE 30, 2012 AND 2011

	<u>2012</u>	<u>2011</u>
Current liabilities		
Payable from unrestricted assets:		
Accounts payable - trade	\$ 352,761	\$ 377,846
Accounts payable - construction	188,348	545,841
Notes payable, due within one year	18,000	18,000
Customer deposits	148,475	143,580
Deferred revenue	207,881	146,677
Other accrued liabilities	<u>376,274</u>	<u>329,470</u>
Total current liabilities payable from unrestricted assets	1,291,739	1,561,414
Payable from restricted assets:		
Interest payable	494,858	548,318
Bonds payable, current portion	3,213,484	2,021,897
Notes payable, current portion	<u>146,340</u>	<u>638,847</u>
Total current liabilities payable from restricted assets	<u>3,854,682</u>	<u>3,209,062</u>
Total current liabilities	5,146,421	4,770,476
Noncurrent liabilities		
Bonds payable, net of current portion	49,916,880	47,674,126
Notes payable, net of current portion	2,901,269	8,668,270
Deferred amount on refunding, net of amortization	<u>(1,984,881)</u>	<u>(2,119,385)</u>
Total noncurrent liabilities	50,833,268	54,223,011
Total liabilities	55,979,689	58,993,487
Net assets		
Invested in capital assets, net of related liabilities	27,561,464	27,806,556
Restricted for debt service	3,419,743	2,779,466
Unrestricted	<u>6,792,493</u>	<u>7,327,622</u>
Total net assets	37,773,700	37,913,644
Total liabilities and net assets	<u>\$ 93,753,389</u>	<u>\$ 96,907,131</u>

The accompanying notes are an integral part of these financial statements.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2012 AND 2011

	<u>2012</u>	<u>2011</u>
Operating Revenues		
Water service	\$ 5,949,379	\$ 5,836,921
Sewer service	4,522,434	4,208,115
Tap in fees - water	41,861	43,041
Tap in fees - sewer	83,425	71,614
Availability charges	638,137	610,332
Golf course irrigation	338,205	358,105
Service fees and penalties	51,108	73,245
Other operating revenues	<u>15,539</u>	<u>80,342</u>
Total operating revenues	11,640,088	11,281,715
Departmental Expenses		
Payroll and related expenses	3,330,115	3,231,400
Administrative expenses	985,686	854,837
Operations expenses	1,761,310	1,639,353
Maintenance expenses	987,389	1,012,322
Tap in expenses	116,219	91,465
Purchased water	1,028,789	1,024,455
RO plant expenses	604,539	581,270
ASR plant expenses	22,068	-
Professional fees	243,600	171,575
Vehicle expenses	130,473	119,162
Depreciation	<u>4,459,807</u>	<u>4,456,160</u>
Total departmental expenses	<u>13,669,995</u>	<u>13,181,999</u>
Loss from operations	(2,029,907)	(1,900,284)
Non-operating revenues (expenses)		
Property taxes - debt service	1,233,107	1,235,347
Property taxes - operations	1,023,502	1,039,316
Rental and tower lease income	503,703	546,848
Interest earned	205,100	234,668
Gain on disposal of equipment	-	7,672
Amortization of bond and note costs	(322,468)	(319,382)
Interest expense	<u>(2,101,677)</u>	<u>(2,190,313)</u>
Total net non-operating income	<u>541,267</u>	<u>554,156</u>
Decrease in net assets before capital contributions	\$ (1,488,640)	\$ (1,346,128)

The accompanying notes are an integral part of these financial statements.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2012 AND 2011

	<u>2012</u>	<u>2011</u>
Capital Contributions		
Assessments	\$ -	\$ 344,402
Capacity fees	394,546	309,857
Developer contributions of systems	<u> 954,150</u>	<u> 42,393</u>
Total capital contributions	1,348,696	696,652
 Change in net assets	 (139,944)	 (649,476)
 Net assets, beginning of the year	 <u>37,913,644</u>	 <u>38,563,120</u>
 Net assets, end of year	 <u>\$ 37,773,700</u>	 <u>\$ 37,913,644</u>

The accompanying notes are an integral part of these financial statements.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED JUNE 30, 2012 AND 2011

	<u>2012</u>	<u>2011</u>
Cash flows from operating activities:		
Cash received from customers	\$ 11,849,228	\$ 10,899,305
Cash paid to suppliers	(6,910,505)	(6,717,042)
Cash paid to employees	(2,319,811)	(2,304,229)
Other revenues	<u>15,539</u>	<u>80,342</u>
Net cash provided by operating activities	2,634,451	1,958,376
Cash flows from investing activities		
Interest earned	<u>205,100</u>	<u>234,668</u>
Net cash provided by investing activities	205,100	234,668
Cash flow from noncapital financing activities:		
Property taxes collected - operations	1,023,502	1,039,316
Rental and tower lease income	573,209	567,794
Sewer assessment	<u>396,027</u>	<u>187,598</u>
Net cash provided by noncapital financing activities:	1,992,738	1,794,708
Cash flow from capital and related financing activities		
Capacity fees	394,546	309,857
Property taxes collected - debt service	1,233,107	1,235,347
Interest expense	(2,265,652)	(2,282,990)
Proceeds from GO bonds	-	3,987,185
Proceeds from revenue bonds	6,003,544	3,843,568
Payoff of SRF Note Payable	(6,100,698)	-
Bond issuance and other capitalized costs	(31,250)	(270,741)
Principal payments on bonds and notes	(2,617,498)	(2,476,106)
Proceeds from sale of capital assets	-	11,281
Purchases of property, plant and equipment	<u>(3,512,586)</u>	<u>(5,253,518)</u>
Net cash used by capital and related financing activities	(6,896,487)	(896,117)
Net increase (decrease) in cash	(2,064,198)	3,091,635
Cash and cash equivalents at beginning of year	<u>8,025,383</u>	<u>4,933,748</u>
Cash and cash equivalents at year end	<u>\$ 5,961,185</u>	<u>\$ 8,025,383</u>

The accompanying notes are an integral part of these financial statements.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED JUNE 30, 2012 AND 2011

	<u>2012</u>	<u>2011</u>
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	\$ (2,029,907)	\$ (1,900,284)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	4,459,807	4,456,160
Increase in allowance for doubtful accounts	10,335	35,000
Changes in assets and liabilities		
Accounts receivable - trade	209,449	(345,638)
Inventories	(3,078)	(1,025)
Prepaid assets	(38,769)	(58,300)
Accounts payable - trade	(25,085)	(156,228)
Customer deposits	4,895	8,570
Other accrued liabilities	46,804	(79,879)
Net cash provided by operating activities	<u>2,634,451</u>	<u>1,958,376</u>
<u>Schedule of cash and cash equivalents</u>		
Available for operations		
Demand deposits (interest and non-interest bearing)	2,341,376	2,287,326
Held by Beaufort County Treasurer	187,319	159,874
Total available for operations	<u>2,528,695</u>	<u>2,447,200</u>
Restricted		
Cash in banks	2,780,037	2,174,532
Held by Beaufort County Treasurer	639,706	604,935
Held for construction	12,747	2,798,716
Total restricted	<u>3,432,490</u>	<u>5,578,183</u>
Total cash and cash equivalents	<u>\$ 5,961,185</u>	<u>\$ 8,025,383</u>
<u>Supplemental Disclosures</u>		
Noncash financing activities:		
Assessments	\$ -	\$ 344,402
Developer contribution of systems	\$ 954,150	\$ 42,393

The accompanying notes are an integral part of these financial statements.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

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. As of June 30, 2012, the District implemented GASB Statement 62 which incorporates into the GASB's authoritative literature certain Financial Accounting Standards Board (FASB) Statements and Interpretations and Accounting Principles Board (APB) Opinions issued on or before November 30, 1989, except for those pronouncements that conflict with or contradict GASB pronouncements. Additionally, based on provisions in GASB Statement 62, the District may continue to apply, as other accounting literature, 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.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and delivering goods in connection with the District's principal ongoing operations. The principal operating revenues are charges to customers for sales and services provided to them. The District also recognizes as operating income tap fees, availability fees, and other revenues related to operations. Operating expenses include the costs of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

Note 1 - Summary of significant accounting policies (continued)

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 liabilities; restricted for 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 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.

When an expense is incurred that can be paid using either restricted or unrestricted resources, the District's policy is to first apply the expense toward restricted resources and then toward unrestricted resources.

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, 2012 and 2011, the balance of the allowance for doubtful accounts was \$57,335 and \$47,000,

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

Note 1 - Summary of significant accounting policies (continued)

Accounts receivable, allowance for doubtful accounts and bad debt expense (continued)

respectively. Bad debt expense for the years ended June 30, 2012 and 2011 was \$210,601 and \$103,627, 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 project which is being financed from the bond proceeds. No interest was capitalized for the years ended June 30, 2012 and 2011.

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
Sewage disposal system	5-33
Building	40
Sewage treatment facilities	3-40
Transportation equipment	5
Operations furniture and equipment	3-7
Office furniture and 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 \$83,661 and \$85,952 for the years ended June 30, 2012 and 2011, 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 2010 revenue bonds included two series of bonds, one issued at a premium of \$126,097 and one issued at a

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

Note 1 - Summary of significant accounting policies (continued)

Bond discount and premium (continued)

discount of \$66,931. The 2010 general obligation bonds included two series of bonds, one issued at a premium of \$53,282 and one issued at a discount of \$36,097. The net unamortized bond premium at June 30, 2012 and 2011 was \$812,333 and \$922,848, respectively, which is included as a direct deduction from bonds payable, net of current portion on the balance sheets. Bond discount and premium amortization totaled \$110,515 and \$110,126 for the years ended June 30, 2012 and 2011, respectively, and is included as a reduction in interest expense on the statements of revenues, expenses and changes in net assets.

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 \$239,855 and \$205,881 at June 30, 2012 and 2011, 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.

Reclassification

Certain accounts and amounts in the June 30, 2011 financial statements have been reclassified in order to conform to the June 30, 2012 presentation.

Date of Management's Review

In preparing the financial statements, the District has evaluated events and transactions for potential recognition or disclosure through October 26, 2012, the date that the financial statements were available to be issued.

Note 2 – Cash, cash equivalents and investments

At June 30, 2012, the bank balances of unrestricted and restricted accounts totaled \$5,202,597 and had a carrying balance totaling \$5,121,211. 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, 2012, 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:

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

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

	Unrestricted	Restricted under bond covenants	Total
FDIC insured	\$ 204,696	\$ -	\$ 204,696
Collateralized	<u>2,217,866</u>	<u>2,780,035</u>	<u>4,997,901</u>
Balance per bank at 6/30/12	<u>\$ 2,422,562</u>	<u>\$ 2,780,035</u>	<u>\$ 5,202,597</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, 2012, 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, 2012 and 2011 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.

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.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

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

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,	
	2012	2011
Unrestricted cash - Available for general operating purposes	\$ 187,319	\$ 159,874
Restricted cash - Available for construction	12,747	1,718,634
Restricted cash - Bond principal retirement and interest payments	639,706	604,935
Total	<u>\$ 839,772</u>	<u>\$ 2,483,443</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,	
	2012	2011
Receivables from customers	\$ 913,005	\$ 1,149,946
Unbilled receivables from customers	894,746	956,324
Other receivables	219,114	140,379
Total	<u>\$ 2,026,865</u>	<u>\$ 2,246,649</u>

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

Note 5 - Property, plant, equipment and depreciation

Capital asset activity during the year ended June 30, 2012 and 2011 was as follows:

	<u>June 30, 2011</u>	<u>Additions</u>	<u>Disposals</u>	<u>Transfers</u>	<u>June 30, 2012</u>
<u>Capital assets not being depreciated:</u>					
Land	\$ 1,299,194	\$ -	\$ -	\$ -	\$ 1,299,194
Construction in progress	<u>3,514,449</u>	<u>3,989,514</u>	<u>-</u>	<u>(6,950,071)</u>	<u>553,892</u>
Total capital assets not being depreciated	<u>4,813,643</u>	<u>3,989,514</u>	<u>-</u>	<u>(6,950,071)</u>	<u>1,853,086</u>
<u>Capital assets being depreciated:</u>					
Waterworks system	51,387,113	43,604	-	3,922,163	55,352,880
Sewage disposal system	31,986,552	25,868	-	3,027,908	35,040,328
Buildings	4,299,512	-	-	-	4,299,512
Sewage treatment facilities	34,711,422	-	-	-	34,711,422
Transportation equipment	915,148	-	-	-	915,148
Operations furniture and equipment	1,639,985	41,629	-	-	1,681,614
Office furniture and equipment	<u>693,249</u>	<u>8,629</u>	<u>-</u>	<u>-</u>	<u>701,878</u>
Total capital assets being depreciated	<u>125,632,981</u>	<u>119,730</u>	<u>-</u>	<u>6,950,071</u>	<u>132,702,782</u>
<u>Less accumulated depreciation for:</u>					
Waterworks system	(19,031,726)	(1,988,898)	-	-	(21,020,624)
Sewage disposal system	(8,462,968)	(1,146,395)	-	-	(9,609,363)
Buildings	(1,284,406)	(124,810)	-	-	(1,409,216)
Sewage treatment facilities	(17,509,307)	(1,069,271)	-	-	(18,578,578)
Transportation equipment	(736,923)	(70,643)	-	-	(807,566)
Operations furniture and equipment	(1,422,054)	(41,697)	-	-	(1,463,751)
Office furniture and equipment	<u>(650,556)</u>	<u>(18,093)</u>	<u>-</u>	<u>-</u>	<u>(668,649)</u>
Total accumulated depreciation	<u>(49,097,940)</u>	<u>(4,459,807)</u>	<u>-</u>	<u>-</u>	<u>(53,557,747)</u>
Total capital assets being depreciated, net	<u>76,535,041</u>	<u>(4,340,077)</u>	<u>-</u>	<u>6,950,071</u>	<u>79,145,035</u>
Year End Totals	<u>\$ 81,348,684</u>	<u>\$ (350,563)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 80,998,121</u>

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

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

	<u>June 30, 2010</u>	<u>Additions</u>	<u>Disposals</u>	<u>Transfers</u>	<u>June 30, 2011</u>
<u>Capital assets not being depreciated:</u>					
Land	\$ 1,299,194	\$ -	\$ -	\$ -	\$ 1,299,194
Construction in progress	<u>1,236,180</u>	<u>5,131,695</u>	<u>-</u>	<u>(2,853,426)</u>	<u>3,514,449</u>
Total capital assets not being depreciated	<u>2,535,374</u>	<u>5,131,695</u>	<u>-</u>	<u>(2,853,426)</u>	<u>4,813,643</u>
<u>Capital assets being depreciated:</u>					
Waterworks system	51,089,748	22,849	-	274,516	51,387,113
Sewage disposal system	29,397,184	10,458	-	2,578,910	31,986,552
Buildings	4,299,512	-	-	-	4,299,512
Sewage treatment facilities	34,711,422	-	-	-	34,711,422
Transportation equipment	912,121	101,073	(98,046)	-	915,148
Operations furniture and equipment	1,626,043	13,942	-	-	1,639,985
Office furniture and equipment	<u>679,868</u>	<u>13,381</u>	<u>-</u>	<u>-</u>	<u>693,249</u>
Total capital assets being depreciated	<u>122,715,898</u>	<u>161,703</u>	<u>(98,046)</u>	<u>2,853,426</u>	<u>125,632,981</u>
<u>Less accumulated depreciation for:</u>					
Waterworks system	(17,102,478)	(1,929,248)	-	-	(19,031,726)
Sewage disposal system	(7,435,300)	(1,027,668)	-	-	(8,462,968)
Buildings	(1,159,266)	(125,140)	-	-	(1,284,406)
Sewage treatment facilities	(16,340,777)	(1,168,530)	-	-	(17,509,307)
Transportation equipment	(744,693)	(86,665)	94,435	-	(736,923)
Operations furniture and equipment	(1,324,088)	(97,966)	-	-	(1,422,054)
Office furniture and equipment	<u>(629,613)</u>	<u>(20,943)</u>	<u>-</u>	<u>-</u>	<u>(650,556)</u>
Total accumulated depreciation	<u>(44,736,215)</u>	<u>(4,456,160)</u>	<u>94,435</u>	<u>-</u>	<u>(49,097,940)</u>
Total capital assets being depreciated, net	<u>77,979,683</u>	<u>(4,294,457)</u>	<u>(3,611)</u>	<u>2,853,426</u>	<u>76,535,041</u>
Year End Totals	<u>\$ 80,515,057</u>	<u>\$ 837,238</u>	<u>\$ (3,611)</u>	<u>\$ -</u>	<u>\$ 81,348,684</u>

Depreciation expense for the years ended June 30, 2012 and 2011 was \$4,459,807 and \$4,456,160, respectively. Transfers relate to construction in progress completed during the year.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

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 \$187,939 and \$205,939 at June 30, 2012 and 2011, 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 bore interest at the rate of 3.50 percent, and was payable quarterly through September 2021 in the amount of \$177,724, which included interest, from revenues derived from operation of the District's system, and was secured by a lien upon those revenues. The balance of this note payable was \$6,100,698 at June 30, 2011. On August 24, 2011, this note was paid in full through the issuance of the series 2011B refunding revenue bonds.

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, 2012 and 2011 amounted to \$414,429 and \$433,063, 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 3.0% per annum. These funds were used as part of the financing for the new reverse osmosis plant. Principal and interest of \$48,135 were payable quarterly beginning January 1, 2009 through October 1, 2011. Effective November 21, 2011, the interest rate was reduced to 2.25% resulting in reduced principal and interest payments of \$45,350 to be paid quarterly from January 1, 2012 through October 1, 2028. The SRF loan balance outstanding at June 30, 2012 and 2011 amounted to \$2,463,242 and \$2,585,417, respectively.

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. 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 was due May 26, 2011. Nine

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

Note 6 – Long-term obligations (continued)

Bonds payable(continued)

additional payments of principal and interest of \$23,301 are payable on May 26th of each year beginning in 2012 and continuing until 2020. The 2010A revenue bonds outstanding amounted to \$157,853 and \$174,438 at June 30, 2012 and 2011, respectively.

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 \$13,125,000 and \$13,900,000 at June 30, 2012 and 2011, 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 \$230,324 and \$243,939 at June 30, 2012 and 2011, 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 1st 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 \$17,665,000 and \$17,205,000 at June 30, 2012 and 2011, respectively.

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 20th 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 \$763,940 and \$799,953 at June 30, 2012 and 2011, 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 \$6,220,000 and \$6,520,000 at June 30, 2012 and 2011, respectively.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

Note 6 – Long-term obligations (continued)

Bonds payable (continued)

In July 2009, the District issued \$355,902 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 July 30th 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 \$321,006 and \$338,842 at June 30, 2012 and 2011, respectively.

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 1st of each year beginning in 2011 and continuing until 2024. The 2009 general obligation bonds outstanding amounted to \$1,483,078 and \$1,576,601 at June 30, 2012 and 2011, respectively.

On August 24, 2010, the District issued \$3,400,000 of series 2010B revenue bonds. Proceeds are to be used to defray the costs of system improvements. Interest on the bonds is payable semi-annually beginning December 1, 2010 at varying interest rates of between 2.00% and 4.00% per annum. Principal payments on the bonds are due annually beginning December 1, 2011 through December 1, 2029. The bonds are payable from revenues derived from operation of the District's system, and are secured by a lien upon these revenues. The 2010B revenue bonds outstanding amounted to \$3,270,000 and \$3,400,000 at June 30, 2012 and 2011, respectively.

On September 28, 2010 the District issued \$3,970,000 of general obligation bonds. Proceeds are to be used to defray the cost of constructing, furnishing and equipping a new Aquifer Storage and Recovery well. Interest on the bonds is payable semi-annually beginning March 1, 2011 at varying interest rates of between 2.00% and 3.375% per annum. Principal payments on the bonds are due annually beginning March 1, 2011 through March 1, 2029. The 2010 general obligation bonds outstanding amounted to \$3,610,000 and \$3,770,000 at June 30, 2012 and 2011, respectively.

On April 27, 2011, the District issued \$384,402 of series 2011 revenue bonds. Proceeds are to be used to defray the costs of system improvements. The series 2011 bond bears interest at a rate of 3.91% per annum. Principal and interest of \$34,356 are payable on April 27th of each year beginning in 2012 and continuing until 2026. The bonds are payable from revenues derived from operation of the District's system, and are secured by a lien upon these revenues. The 2011 revenue bonds outstanding amounted to \$365,076 and \$384,402 at June 30, 2012 and 2011, respectively.

On August 24, 2011, the District issued \$6,003,544 of series 2011B refunding revenue bonds. Proceeds were used to refund the May 2000 loan agreement with the South Carolina Water Quality Revolving Fund Authority; the purpose of the original loan agreement was to fund the expansion of the wastewater treatment plant capacity by 3,200,000 gallons per day. The series 2011B bond bears interest at a rate of 2.89% per annum. Principal and interest of \$57,666 are payable on the 24th of each month beginning in

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

Note 6 – Long-term obligations (continued)

Bonds payable (continued)

September 2011 and continuing until August 2021. The bonds are payable from revenues derived from operation of the District's system, and are secured by a lien upon these revenues. The 2011 revenue bonds outstanding amounted to \$5,566,753 at June 30, 2012.

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

Years ended June 30,	Principal	Interest	Total
2013	\$ 3,377,824	\$ 2,133,998	\$ 5,511,822
2014	3,515,889	2,003,695	5,519,584
2015	3,659,879	1,861,179	5,521,058
2016	3,804,826	1,711,639	5,516,465
2017	4,065,763	1,553,996	5,619,759
2018-2022	22,419,542	5,133,944	27,553,486
2023-2027	13,010,985	1,202,203	14,213,188
2028-2030	1,528,933	74,993	1,603,926
	<u>\$ 55,383,641</u>	<u>\$ 15,675,647</u>	<u>\$ 71,059,288</u>

Bonds with varying interest rates at June 30, 2012 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	Revenue bonds dated Aug. 24, 2010	General Obligation bonds dated Sept. 28, 2010
2013	4.250%	3.500%	4.000%	3.000%	2.000%
2014	5.000%	3.625%	4.000%	3.000%	2.000%
2015	5.000%	3.625%	4.000%	3.000%	2.000%
2016	5.000%	3.75% - 4.00%	4.000%	4.000%	2.000%
2017	5.000%	4.000%	4.000%	4.000%	2.250%
2018 - 22	-	4.000%	4.000%	4.000%	3.000%
2023	-	4.100%	4.000%	4.000%	3.000%
2024	-	4.125%	4.000%	4.000%	3.000%
2025	-	-	4.000%	4.000%	3.000%
2026 - 27	-	-	4.000%	4.000%	3.125%
2028	-	-	-	4.000%	3.250%
2029	-	-	-	3.875%	3.375%

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

Note 7 – Non-current liabilities

The non-current liability activity during fiscal years 2012 and 2011 was as follows:

	June 30, 2011	Additions	Reductions	June 30, 2012	Amounts due within one year
Revenue bonds	\$ 36,906,574	\$ 6,003,544	\$ (1,905,166)	\$ 41,004,952	\$ 2,641,015
GO bonds	11,866,601	-	(553,523)	11,313,078	572,469
Notes payable	9,325,117	-	(6,259,507)	3,065,610	164,340
Bond discount/premium	922,848	-	(110,515)	812,333	-
Less deferred amount	(2,119,385)	(104,303)	238,807	(1,984,881)	-
Sub Total	\$ 56,901,755	\$ 5,899,241	\$ (8,589,904)	\$ 54,211,092	\$ 3,377,824
Less current portion	(2,678,744)			(3,377,824)	
Noncurrent liabilities	\$ 54,223,011			\$ 50,833,268	

	June 30, 2010	Additions	Reductions	June 30, 2011	Amounts due within one year
Revenue bonds	\$ 34,383,014	\$ 3,784,402	\$ (1,260,842)	\$ 36,906,574	\$ 1,468,375
GO bonds	8,476,338	3,970,000	(579,737)	11,866,601	553,523
Notes payable	9,960,643	-	(635,526)	9,325,117	656,846
Bond discount/premium	956,623	76,351	(110,126)	922,848	-
Less deferred amount	(2,352,815)	-	233,430	(2,119,385)	-
Sub Total	\$ 51,423,803	\$ 7,830,753	\$ (2,352,801)	\$ 56,901,755	\$ 2,678,744
Less current portion	(2,276,105)			(2,678,744)	
Noncurrent liabilities	\$ 49,147,698			\$ 54,223,011	

Note 8 – Deferred amount on refunding

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 amount 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, 2011 was 33,414. At June 30, 2012, this deferred amount was fully amortized and was retired.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

Note 8 – Deferred amount on refunding (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 amount on early retirement of \$2,234,714 over the 17-year average life of the refunded bonds. The unamortized balance at June 30, 2012 and 2011 was \$1,150,220 and \$1,281,674, 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, 2012 and 2011 was \$725,370 and \$788,873, 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 amount on early retirement of \$17,137 over the 10-year life of the refunded bonds. The unamortized balance at June 30, 2012 and 2011 was \$13,710 and \$15,424, respectively.

In August 2011, the District issued series 2011B revenue refunding bonds amounting to \$6,003,544 to refund the note payable with the South Carolina Water Quality Revolving Fund Authority amounting to \$10,194,238 of principal which were to mature in 2022 and had a principal balance of \$6,100,698 at the time of refunding. The District is amortizing the deferred amount on early retirement of \$104,303 over the 10-year life of the refunded bonds. The unamortized balance at June 30, 2012 was \$95,612.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

Note 9 – Restricted Assets

A reserve fund for debt service is mandated by bond covenants. At June 30, 2012 and 2011 the debt service reserves totaled \$3,419,743 and \$2,779,466, 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, 2012 and 2011, the District had \$12,747 and \$2,798,716, respectively, held by the Beaufort County Treasurer and US Bank relating to the September 28, 2010 GO bond issuance. Use of these funds is restricted for constructing, furnishing and equipping a new Aquifer Storage and Recovery well.

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 \$465,355 and \$423,468 for the years ended June 30, 2012 and 2011, respectively.

The future minimum lease income is as follows:

Years ended	
June 30,	Amount
2013	\$ 430,092
2014	292,636
2015	228,381
2016	103,647
2017	30,889
Thereafter	-
Total	<u>\$ 1,085,645</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.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

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 \$1,028,789 and \$1,024,455 for the years ended June 30, 2012 and 2011, 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 \$954,150 and \$42,393 and payments of capacity fees totaling \$394,546 and \$309,857 were collected during the fiscal years ended June 30, 2012 and 2011, 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 had no outstanding construction contract commitments at June 30, 2012.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

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 Beaufort 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 \$3,425,880 and \$3,821,907 as of June 30, 2012 and 2011, respectively. A portion of the annual receipts is recognized as interest income each year. For the years ended June 30, 2012 and 2011, \$184,358 and \$188,333, respectively, of the assessments collected was recognized as interest income.

Note 14 - Deferred compensation plans

Section 457/401(k) 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. In May 2012, the District also adopted a 401(k) Plan option. Under the Plan, all participants may make an elective deferral up to 100% of their annual compensation subject to Internal Revenue Code maximum contribution limitations. The District makes a 6% matching contribution to each eligible participant's account who has not chosen to also participate in the South Carolina Retirement Plan. Employee contributions for the years ended June 30, 2012 and 2011 were \$169,878 and \$150,599, respectively. The matching contribution for the years ended June 30, 2012 and 2011 was \$15,851 and \$20,152, respectively.

South Carolina Retirement System

Effective April 2004, the District 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, 2012, 2011 and 2010 were 9.385%, 9.24%, and 9.24%, respectively. The District's matching contribution for the years ended June 30, 2012, 2011 and 2010 were \$193,454, \$171,769 and \$174,808, respectively. For each of the years, the District contributed 100% of the required contribution to the SCRS.

For the years ended June 30, 2012, 2011 and 2010, \$2,061,190, \$1,858,973, and \$1,891,868, respectively, of wages were subject to retirement. During the years ended June 30, 2012, 2011 and 2010, \$133,978, \$120,833, and \$122,672, respectively, were contributed to the system for the employees' share which represented 6.50% of covered payroll for each of those years.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

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 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	2012	2011
Under 50 years of age	\$ 17,000	\$ 16,500
50 years of age and over	\$ 22,500	\$ 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.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

Note 16 - Net assets

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

	As of June 30,	
	2012	2011
Invested in capital assets, net of related liabilities		
Net property, plant and equipment in service	\$ 80,998,121	\$ 81,348,685
Less: Debt as disclosed in Notes 6 & 7	(55,383,640)	(58,098,292)
Cash for construction	12,747	2,798,716
Bond premium, net	(812,333)	(922,848)
Deferred amount on refunding, net	1,984,881	2,119,385
Bond issue costs and discounts, net	950,036	1,106,751
Accounts payable for capital assets	(188,348)	(545,841)
	<u>27,561,464</u>	<u>27,806,556</u>
Restricted for debt service	3,419,743	2,779,466
Unrestricted	<u>6,792,493</u>	<u>7,327,622</u>
Total net assets	<u>\$ 37,773,700</u>	<u>\$ 37,913,644</u>

SUPPLEMENTAL FINANCIAL INFORMATION

Hilton Head PSD
Budgetary Comparison Schedule
Year to Date as of June 30, 2012

(With comparative amounts for the same period in prior fiscal year)

	(With comparative amounts for the same period in prior fiscal year)		FY 2012 to FY 2012 Budget	
	Fiscal Year 2012		Comparison	
	Actual	Budget	Dollars	%
Operating Revenues			Favorable (Unfavorable)	
Water Service	\$ 5,949,379	\$ 5,980,400	\$ (31,021)	-0.5%
Sewer Service	4,522,434	4,456,500	65,934	1.5%
Tap In Fees - Water	41,861	45,500	(3,639)	-8.0%
Connection Fees - Sewer	83,425	4,500	78,925	N/A
Service Fees	51,108	83,100	(31,992)	-38.5%
Golf Course Irrigation	338,205	358,800	(20,595)	-5.7%
Availability Fees	638,137	641,400	(3,263)	-0.5%
Other Operating Revenues	15,539	17,200	(1,661)	-9.7%
Total Operating Revenues	11,640,088	11,587,400	52,688	0.5%
Departmental Expenses				
Payroll & Related	3,330,115	3,416,200	86,085	2.5%
Administrative Expenses	985,687	850,600	(135,087)	-15.9%
Operations	1,761,310	1,625,100	(136,210)	-8.4%
Maintenance	987,389	876,700	(110,689)	-12.6%
Water Tap In Expenses	37,443	21,395	(16,048)	-75.0%
Sewer Connection Expenses	78,775	28,605	(50,170)	-175.4%
Purchased Water	1,028,789	984,400	(44,389)	-4.5%
ASR Water	16,792	-	(16,792)	N/A
RO Plant O&M	604,539	691,700	87,161	12.6%
ASR O&M	5,275	-	(5,275)	N/A
Professional Fees	243,600	203,000	(40,600)	-20.0%
Vehicle	130,473	134,800	4,327	3.2%
Total Departmental Expenses	9,210,189	8,832,500	(377,689)	-4.3%
Depreciation	4,459,807	4,357,100	(102,707)	-2.4%
Total Operating Expenses	13,669,995	13,189,600	(480,395)	-3.6%
Operating income (loss)	(2,029,907)	(1,602,200)	(427,707)	-26.7%
Non-operating revenues				
Property taxes-G.O. Debt Levy	1,233,107	1,238,200	(5,093)	-0.4%
Property taxes-Operations Levy	1,023,502	1,028,800	(5,298)	-0.5%
Rental Income	80,235	95,500	(15,265)	-16.0%
Interest earned	205,100	299,400	(94,300)	-31.5%
Tower lease	423,468	473,600	(50,132)	-10.6%
Gain (Loss) of disposal of equipment	-	-	-	N/A
Total Non-operating Revenues	2,965,412	3,135,500	(170,088)	-5.4%
Non-operating Expenses				
Interest expense-Bonds	2,212,192	2,181,400	(30,792)	-1.4%
Bond Defeasance Amortization	238,807	233,400	(5,407)	-2.3%
Amortization of Debt Expenses	83,661	85,900	2,239	2.6%
Bond Premium Amortization	(110,515)	(110,100)	415	0.4%
Total Non-operating Expenses	2,424,145	2,390,600	(33,545)	-1.4%
Total Non-operating Revenues/Exp.	541,267	744,900	(203,633)	-27.3%
Increase (decrease) in net assets, before capital contributions	(1,488,640)	(857,300)	(631,340)	73.6%
Water Capacity Fee	162,939	50,000	112,939	225.9%
Sewer Capacity Fee	231,607	230,700	907	0.4%
Developer Contributions of Systems Assessments	954,150	-	N/A	N/A
	-	-	N/A	N/A
Total Capital Contributions	1,348,696	280,700	1,067,996	380.5%
Increase (decrease) in net assets	\$ (139,944)	\$ (576,600)	\$ 436,656	75.7%
Net Assets at the beginning of the year	\$ 37,913,644			
Net Assets Year-To-Date	\$ 37,773,700			

Notes to Budgetary Comparison Schedule

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. A budgetary comparison schedule can be found on the previous page.

Operating Revenues: Actual of \$11,640,088 vs. FY'12 Budget of \$11,587,400 represents a variance of \$52,688 or 0.5% more than budget.

The following is a summary of material variances for the Operating Revenue categories:⁵

- Sewer Service revenues are above budget by \$65,934 or 1.5%.
- Sewer Connection Fees are above budget by \$78,925 due to increased connections associated with the Stoney Project and Project Safe.
- Service fees are below budget by \$31,992 or 39%. When late fees were first implemented it was procedure that all delinquent accounts (including final billed accounts) incur late fees. For fiscal year 2012, final billed accounts no longer incur late fees after the final bill date resulting in lower than anticipated service fee collected.

Total Departmental Expenses (excludes depreciation): Total departmental expenses are \$377,689 or 4.3% over budget. The following is a summary of material variances for the Departmental Expenses categories:¹

- Payroll and Related Expenses: Actual of \$3,330,115 vs. FY'12 Budget of \$3,416,200 is \$86,085 or 2.5% lower than budget. This is mainly due to staffing reduction during the year.
- Administrative Expenses: Actual of \$985,687 vs. FY'12 Budget of \$850,600 is \$135,087 or 16% higher than budget. This variance is mainly due to higher than expected bad debt expense. After a review of all delinquent accounts staff has been working on the associated bad debt write off during fiscal year 2012, which has increased bad debt expense. Insurance other than group/vehicle expense was also higher than expected by approximately \$26,000 or 11%.
- Operations Expenses: Actual of \$1,761,310 vs. FY'12 Budget of \$1,625,100 is \$136,210 or 8.4% higher than budget. This is mainly due to higher than expected costs for biosolids disposal, operations chemicals, and power.
- Maintenance Expenses: Actual of \$987,389 vs. FY'12 Budget of \$876,700 is \$110,689 or 13% higher than budget. This is mainly due to higher than anticipated effluent system, lift station, and water/sewer systems maintenance costs.
- Water Tap In Expenses: Actual of \$37,443 vs. FY'12 Budget of \$21,395 is \$16,048 or 75% over budget. This expense is more than offset by associated water tap in fees revenue.

⁵ A variance of more than \$50,000 or 10 percent constitutes a material variance for this report. In some cases variances that borderline these parameters are also discussed in this section.

- Sewer Connection Expenses: Actual of \$78,775 vs. FY'12 Budget of \$28,605 is \$50,170 over budget due to increased sewer connections. This expense and associated budget overage is more than offset by increased sewer connection fee revenues.
- ASR Water Expense: ASR water expense relates to water that has been drawn out of the ASR well for customer use. During May 2012, the District withdrew 21.2 million gallons from the ASR-1 well for customer consumption. ASR Water Expense was a non budgeted item for fiscal year 2012.
- RO Plant O&M: Actual of \$604,539 vs. FY'12 Budget of \$691,700 represents a variance of \$87,161 or 13% below budget. During off peak months the District has been running two RO trains instead of three in coordination with the purchase of off peak water to meet customer demands during the winter months. This has lowered RO maintenance, chemical, and power expenses.
- ASR O&M: This is a new line item that covers the chemical and power expense associated with the ASR well. This was a non budgeted item for fiscal year 2012. The small associated cost to date relates to the initial testing process that took place during the third quarter of the fiscal year.
- Professional Fees: Actual of \$243,600 vs. FY'12 Budget of \$203,000 represents a variance of \$40,600 or 20% above budget due to higher than expected professional engineering fees associated with the wastewater treatment plant evaluation and the Middle Floridan capacity analysis.

Total Non-Operating Revenues: Actual of \$2,965,412 vs. FY'12 Budget of \$3,135,500 represents a variance of \$170,088 or 5.4% below budget mainly due to reduced interest income and tower lease revenue.

Total Non-Operating Expenses: Actual of \$2,424,145 vs. FY'12 Budget of \$2,390,600 represents a variance of \$33,545 or 1.4% above budget mainly due to higher than anticipated bond interest expense.

Capital Contributions: Actual Capacity Fees of \$394,546 vs. FY'12 Budget of \$280,700 represents a variance of \$113,846 above budget due to capacity fees received for a new building in Bluewater Marina. The developer contribution of systems category has a balance of \$954,150 which is a reimbursement due from the Town of Hilton Head for the TIF Stoney Project. Both developer contributions of systems and assessments are non-budgeted items.

Bond Disclosure: In compliance with necessary requirements.

Fiscal year 2012's decrease in net assets was \$139,944, which was \$436,656 under the projected decrease in net assets of \$576,600.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
SUMMARY SCHEDULE OF DEBT
JUNE 30, 2012

<u>Description</u>	<u>Rate</u>	<u>06/30/2010</u>	<u>Addition</u>	<u>Reduction</u>	<u>6/30/2011</u>	<u>Addition</u>	<u>Reduction</u>	<u>06/30/2012</u>	<u>Current</u>
<u>Notes Payable</u>									
*SCJEDA - Notes Payable	0.00%	\$ 223,939	\$ -	\$ (18,000)	\$ 205,939	\$ -	\$ (18,000)	\$ 187,939	\$ 18,000
<u>Revenue Bonds</u>									
Series 2004	2.00% to 5.00%	14,640,000	-	(740,000)	13,900,000	-	(775,000)	13,125,000	1,385,000
Series 2004B	5.19%	256,882	-	(12,943)	243,939	-	(13,615)	230,324	14,321
Series 2006	3.50 to 4.13%	18,105,000	-	(440,000)	17,665,000	-	(460,000)	17,205,000	480,000
Series 2007	4.22%	834,507	-	(34,554)	799,953	-	(36,013)	763,940	37,532
Series 2009A	4.55%	355,902	-	(17,060)	338,842	-	(17,836)	321,006	18,648
Series 2010	2.00% to 4.00%	-	3,400,000	-	3,400,000	-	(130,000)	3,270,000	130,000
Series 2010A	3.85%	190,722	-	(16,284)	174,438	-	(16,585)	157,853	17,223
Series 2011	3.91%	-	384,402	-	384,402	-	(19,326)	365,076	20,082
Series 2011B	2.89%	-	-	-	-	6,003,544	(436,791)	5,566,753	538,209
Total Revenue Bonds		34,383,013	3,784,402	(1,260,841)	36,906,574	6,003,544	(1,905,166)	41,004,952	2,641,015
<u>State Revolving Fund Loans:</u>									
SRF - Series 2000A Revenue Bond	3.50%	6,587,375	-	(486,677)	6,100,698	-	(6,100,698)	-	-
SRF - Series 2007 GO Bonds	2.25% / 3.00%	2,698,270	-	(112,853)	2,585,417	-	(122,175)	2,463,242	127,046
SIRF Series 2007 GO Bonds	3.50%	451,059	-	(17,996)	433,063	-	(18,634)	414,429	19,294
Total State Revolving Loans		9,736,704	-	(617,526)	9,119,178	-	(6,241,507)	2,877,671	146,340
<u>General Obligation Bonds:</u>									
Series 2007	4.00% to 4.50%	6,810,000	-	(290,000)	6,520,000	-	(300,000)	6,220,000	310,000
Series 2009	4.22%	1,666,338	-	(89,737)	1,576,601	-	(93,523)	1,483,078	97,469
Series 2010	2.00% to 3.38%	-	3,970,000	(200,000)	3,770,000	-	(160,000)	3,610,000	165,000
Total General Obligation Bonds		8,476,338	3,970,000	(579,737)	11,866,601	-	(553,523)	11,313,078	572,469
Total Long-Term Liabilities		\$ 52,819,994	\$ 7,754,402	\$ (2,476,104)	\$ 58,098,292	\$ 6,003,544	\$ (8,718,196)	\$ 55,383,640	\$ 3,377,824
Less current portion		<u>(2,276,105)</u>			<u>(2,678,744)</u>			<u>(3,377,824)</u>	
Bond discount/premium, net of amortization		956,624			922,848			812,333	
Deferred amount on refunding, net of amortization		(2,352,815)			(2,119,385)			(1,984,881)	
Total Long Term Debt		<u>\$ 49,147,698</u>			<u>\$ 54,223,011</u>			<u>\$ 50,833,268</u>	

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

SCHEDULE OF BOND PRINCIPAL AND INTEREST PAYMENTS

JUNE 30, 2012

For the Year ending June 30,	\$190,722 Series 2010A Revenue Bonds Dated June 16, 2010		\$17,575,000- Refunded Revenue Bonds Dated April 11, 2004		\$430,000 Revenue Bond Dated August 10, 2004		\$18,770,000 Revenue Bonds Dated February 2, 2006		\$930,000 Revenue Bond Dated June 20, 2007		\$7,350,000 GO Bond Dated October 3, 2007		\$335,902 Series 2009A FFA Dated July 30, 2009	
	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal
2013	6,077	17,223	616,431	1,385,000	11,954	14,321	680,724	480,000	32,238	37,532	248,800	310,000	14,606	18,648
2014	5,414	17,886	550,500	1,460,000	11,211	15,064	663,443	490,000	30,654	39,116	236,400	325,000	13,757	19,496
2015	4,726	18,575	475,625	1,535,000	10,428	15,846	645,318	510,000	29,004	40,767	223,400	335,000	12,870	20,383
2016	4,010	19,290	396,875	1,615,000	9,606	16,669	625,574	525,000	27,283	42,487	210,000	350,000	11,943	21,311
2017	3,268	20,033	324,375	1,285,000	8,741	17,534	594,068	1,055,000	25,490	44,280	196,000	365,000	10,973	22,280
2018	2,497	20,804	258,375	1,355,000	7,831	18,444	551,061	1,100,000	23,622	46,149	181,400	380,000	9,959	23,294
2019	1,696	21,605	188,875	1,425,000	6,874	19,401	506,161	1,145,000	21,674	48,097	166,200	390,000	8,900	24,354
2020	864	22,437	115,875	1,495,000	5,867	20,408	459,461	1,190,000	19,645	50,126	150,600	405,000	7,791	25,462
2021	-	-	39,250	1,570,000	4,808	21,467	410,761	1,245,000	17,529	52,242	134,400	420,000	6,633	26,620
2022	-	-	-	-	3,694	22,581	325,361	3,025,000	15,325	54,446	117,600	440,000	5,422	27,832
2023	-	-	-	-	2,522	23,753	200,184	3,155,000	13,027	56,744	100,000	460,000	4,155	29,098
2024	-	-	-	-	1,289	24,837	67,753	3,285,000	10,632	59,138	81,600	480,000	2,831	30,422
2025	-	-	-	-	-	-	-	-	8,137	61,634	62,400	500,000	1,447	31,806
2026	-	-	-	-	-	-	-	-	5,536	64,235	42,400	520,000	-	-
2027	-	-	-	-	-	-	-	-	2,825	66,946	21,600	540,000	-	-
2028	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2029	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2030	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	<u>\$ 28,552</u>	<u>\$ 157,853</u>	<u>\$ 2,966,181</u>	<u>\$ 13,125,000</u>	<u>\$ 84,825</u>	<u>\$ 230,325</u>	<u>\$ 5,729,868</u>	<u>\$ 17,205,000</u>	<u>\$ 282,622</u>	<u>\$ 763,939</u>	<u>\$ 2,172,800</u>	<u>\$ 6,220,000</u>	<u>\$ 111,288</u>	<u>\$ 321,006</u>

Current		<u>\$ 17,223</u>		<u>\$ 1,385,000</u>		<u>\$ 14,321</u>		<u>\$ 480,000</u>		<u>\$ 37,532</u>		<u>\$ 310,000</u>		<u>\$ 18,648</u>
Noncurrent		<u>\$ 140,630</u>		<u>\$ 11,740,000</u>		<u>\$ 216,004</u>		<u>\$ 16,725,000</u>		<u>\$ 726,407</u>		<u>\$ 5,910,000</u>		<u>\$ 302,358</u>

For the Year ending June 30,	\$1,781,694 Series 2009 GO Bond Dated July 30, 2009		\$3,400,000 Revenue Bond Dated August 24, 2010		\$3,970,000 GO Bond Dated September 25, 2010		\$6,003,544 Revenue Bond Dated August 24, 2011		\$384,000 Revenue Bond Dated April 27, 2011		BOND TOTALS		
	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Total Interest	Total Principal	Total
2013	62,571	97,469	121,575	130,000	102,350	165,000	153,787	538,209	14,274	20,082	2,065,388	3,213,484	5,278,872
2014	58,459	101,581	118,250	135,000	99,050	170,000	138,025	553,971	13,489	20,867	1,938,652	3,347,982	5,286,634
2015	54,173	105,867	114,125	140,000	95,650	175,000	121,802	570,194	12,673	21,683	1,799,793	3,488,315	5,288,108
2016	49,707	110,333	109,925	140,000	92,150	180,000	105,103	586,893	11,826	22,531	1,654,002	3,629,514	5,283,516
2017	45,052	114,988	104,825	150,000	88,550	185,000	87,916	604,080	10,945	23,412	1,500,202	3,886,607	5,386,809
2018	40,200	119,839	98,725	155,000	84,368	190,000	70,225	621,771	10,029	24,327	1,338,292	4,054,628	5,392,921
2019	35,144	124,895	92,425	160,000	78,688	195,000	52,015	639,981	9,078	25,278	1,167,729	4,218,611	5,386,341
2020	29,875	130,165	85,925	165,000	72,838	200,000	33,273	658,723	8,090	26,267	990,103	4,388,587	5,378,691
2021	24,383	135,656	79,125	175,000	66,838	205,000	13,982	678,014	7,063	27,294	804,772	4,556,293	5,361,065
2022	18,660	141,380	72,025	180,000	60,688	210,000	416	114,917	5,995	28,361	625,185	4,244,517	4,869,702
2023	12,695	147,345	64,625	190,000	54,388	220,000	-	-	4,887	29,470	456,482	4,311,409	4,767,892
2024	6,479	153,561	56,925	195,000	47,788	230,000	-	-	3,734	30,622	279,031	4,488,580	4,767,611
2025	-	-	48,925	205,000	40,888	240,000	-	-	2,537	31,819	164,334	1,070,260	1,234,593
2026	-	-	40,625	210,000	33,688	245,000	-	-	1,293	33,064	123,541	1,072,299	1,195,840
2027	-	-	32,163	220,000	26,031	255,000	-	-	-	-	82,619	1,081,946	1,164,565
2028	-	-	23,444	230,000	18,063	265,000	-	-	-	-	41,506	495,000	536,506
2029	-	-	14,338	240,000	9,450	280,000	-	-	-	-	23,788	520,000	543,788
2030	-	-	4,844	250,000	-	-	-	-	-	-	4,844	250,000	254,844
	<u>\$ 437,399</u>	<u>\$ 1,483,079</u>	<u>\$ 1,282,813</u>	<u>\$ 3,270,000</u>	<u>\$ 1,071,461</u>	<u>\$ 3,610,000</u>	<u>\$ 776,544</u>	<u>\$ 5,566,753</u>	<u>\$ 115,913</u>	<u>\$ 365,076</u>	<u>\$ 15,060,265</u>	<u>\$ 52,318,031</u>	<u>\$ 67,378,295</u>

Current		<u>\$ 97,469</u>		<u>\$ 130,000</u>		<u>\$ 165,000</u>		<u>\$ 538,209</u>		<u>\$ 20,082</u>		<u>\$ 3,193,402</u>		
Noncurrent		<u>\$ 1,385,610</u>		<u>\$ 3,140,000</u>		<u>\$ 3,445,000</u>		<u>\$ 5,028,544</u>		<u>\$ 344,994</u>		<u>\$ 48,759,553</u>		

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
Schedule of Bond Principal and Interest Payments
June 30, 2012

For the Year ending June 30,	\$530,000 SCJESA Note		\$2,887,826 SRF GO Bond		\$481,080 SIRF GO Bond		NOTE TOTALS		
	Dated November 30, 1988		Dated October 3, 2007		Dated October 3, 2007		Total	Total	Total
	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Total
2013	-	18,000	54,356	127,046	14,254	19,294	68,610	164,340	232,950
2014	-	18,000	51,473	129,928	13,569	19,979	65,043	167,907	232,950
2015	-	18,000	48,525	132,877	12,861	20,687	61,386	171,564	232,950
2016	-	18,000	45,510	135,892	12,127	21,421	57,637	175,312	232,950
2017	-	18,000	42,427	138,975	11,368	22,180	53,794	179,156	232,950
2018	-	18,000	39,273	142,129	10,581	22,967	49,854	183,096	232,950
2019	-	18,000	36,048	145,354	9,767	23,781	45,815	187,135	232,950
2020	-	18,000	32,750	148,652	8,923	24,625	41,673	191,276	232,950
2021	-	18,000	29,377	152,025	8,050	25,498	37,427	195,523	232,950
2022	-	18,000	25,928	155,474	7,146	26,402	33,073	199,876	232,950
2023	-	7,939	22,500	158,902	6,210	27,339	28,709	194,179	222,889
2024	-	-	18,792	162,610	5,240	28,308	24,032	190,918	214,950
2025	-	-	15,102	166,300	4,236	29,312	19,338	195,611	214,950
2026	-	-	11,329	170,073	3,197	30,351	14,526	200,424	214,950
2027	-	-	7,470	173,932	2,120	31,428	9,590	205,360	214,950
2028	-	-	3,523	177,879	1,006	32,542	4,529	210,421	214,950
2029	-	-	254	45,197	73	8,315	326	53,511	53,838
	-	-		-	-	-	-	-	-
	<u>\$ -</u>	<u>\$ 187,939</u>	<u>\$ 484,636</u>	<u>\$ 2,463,242</u>	<u>\$ 130,728</u>	<u>\$ 414,429</u>	<u>\$ 615,364</u>	<u>\$ 3,065,610</u>	<u>\$ 3,680,974</u>
Current		<u>\$ 18,000</u>		<u>\$ 127,046</u>		<u>\$ 19,294</u>		<u>\$ 164,340</u>	
Noncurrent		<u>\$ 169,939</u>		<u>\$ 2,336,196</u>		<u>\$ 395,134</u>		<u>\$ 2,901,269</u>	

STATISTICAL SECTION

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HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

Statements of Revenues, Expenses, and Debt Service per Bond Covenants

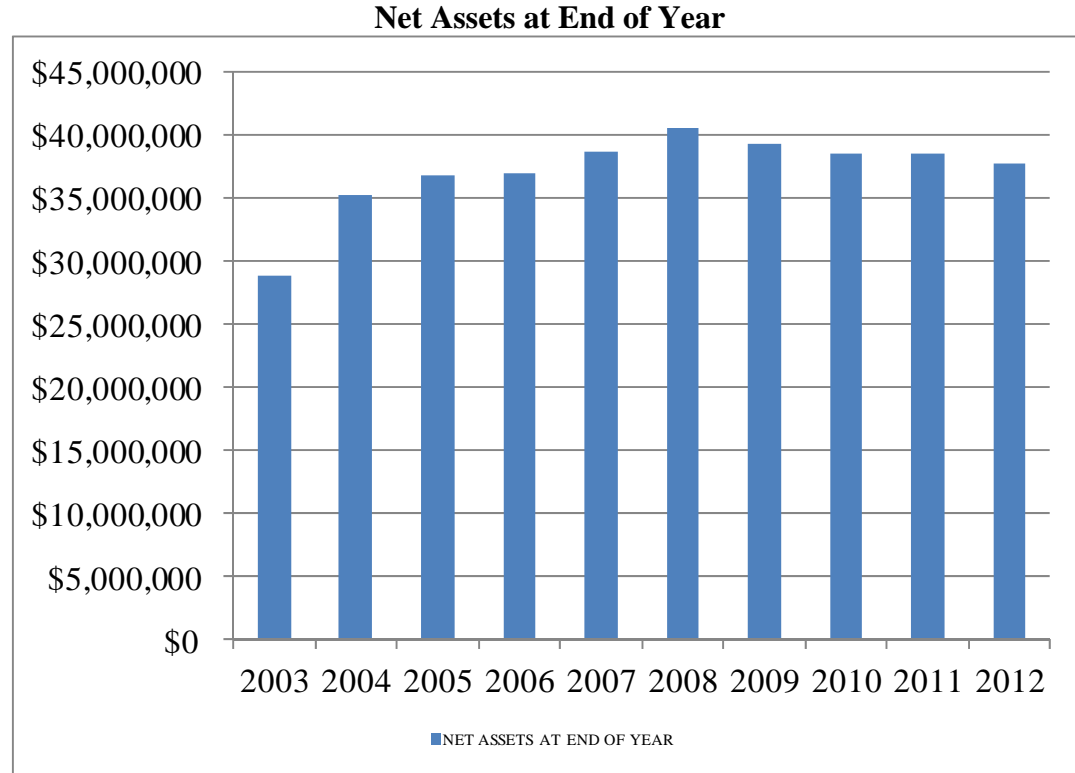
Last Ten Fiscal Years

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
<u>Operating Revenues</u>										
Water service	\$4,633,117	\$4,992,011	\$4,870,847	\$5,162,771	\$5,465,028	\$5,518,049	\$5,307,260	\$5,308,798	\$5,836,921	\$5,949,379
Sewer service	3,342,647	3,503,456	3,525,405	3,655,945	3,941,776	4,059,860	3,959,087	4,034,068	4,208,115	4,522,434
Tap in fees - water	324,760	264,670	262,564	175,964	106,768	72,569	35,133	31,305	43,041	41,861
Tap in fees - sewer	266,792	272,536	294,286	72,493	19,600	11,284	2,330	117,367	71,614	83,425
Availability charges	503,166	443,559	400,503	546,788	504,303	540,104	547,354	570,169	610,332	638,137
Service fees and penalties	38,601	32,199	41,985	42,121	38,218	38,153	50,311	70,488	73,245	51,108
Golf course irrigation	123,858	181,379	157,944	216,700	261,616	301,856	243,274	230,583	358,105	338,205
Other operating Revenues	92,011	29,181	12,647	7,803	16,712	16,188	19,154	35,679	80,342	15,539
Total Operating Revenues	\$9,324,953	\$9,718,991	\$9,566,181	\$9,880,585	\$10,354,021	\$10,558,063	\$10,163,903	\$10,398,457	\$11,281,715	\$11,640,088
<u>Operating Expenses</u>										
Payroll and related expenses	\$2,601,065	\$2,506,686	\$2,416,236	\$2,593,804	\$2,735,039	\$2,975,752	\$3,165,506	\$3,166,896	\$3,231,400	\$3,330,115
Administrative expenses	586,073	533,999	555,416	563,365	556,794	606,608	759,594	754,453	854,837	985,687
Operations expenses	702,466	857,153	938,247	1,086,507	1,098,914	1,197,436	1,430,222	1,410,295	1,639,353	1,761,310
Maintenance expenses	504,543	683,354	630,142	637,588	626,455	733,394	677,372	768,575	1,012,323	987,389
Water Tap In Expenses	138,683	118,665	191,691	172,549	93,757	79,818	26,620	23,030	64,774	37,443
Sewer Connection Expense	8,249	22,177	21,039	19,249	16,473	3,512	3,900	128,227	26,690	78,775
Purchased water	1,146,852	1,225,760	1,394,283	1,645,206	1,671,703	1,596,183	1,356,803	746,571	1,024,455	1,028,789
ASR-1 Water	-	-	-	-	-	-	-	-	-	16,792
RO Plant O&M	-	-	-	-	-	-	127,852	674,039	581,270	604,539
ASR-1 O&M	-	-	-	-	-	-	-	-	-	5,275
Professional fees	166,255	408,970	243,961	291,336	294,484	532,391	410,736	269,207	171,575	243,600
Vehicle expenses	103,496	105,783	129,805	140,672	140,654	146,335	131,379	107,292	119,162	130,473
Depreciation	3,197,862	3,208,842	3,221,943	3,349,668	3,540,690	3,720,333	3,965,632	4,405,077	4,456,160	4,459,807
Total Operating Expenses	\$9,155,544	\$9,671,389	\$9,742,763	\$10,499,944	\$10,774,963	\$11,591,762	\$12,055,616	\$12,453,662	\$13,181,999	\$13,669,995
Operating Income (Loss from operations)	\$169,409	\$47,602	(\$176,582)	(\$619,359)	(\$420,942)	(\$1,033,699)	(\$1,891,713)	(\$2,055,205)	(\$1,900,284)	(\$2,029,907)
<u>Non-operating revenues (expenses)</u>										
Property taxes-debt service	\$360,384	\$378,626	\$320,228	\$269,130	\$125,052	\$409,292	\$817,751	\$967,418	\$1,235,347	\$1,233,107
Property taxes-operations	551,967	566,682	831,083	848,076	760,054	901,072	924,702	1,028,416	1,039,316	1,023,502
Sewer Assessments	464,888	-	-	-	-	-	-	-	-	-
Rental income	-	18,395	58,039	80,852	87,011	84,546	84,496	82,150	81,493	80,235
Interest earned	192,692	116,629	354,611	538,646	508,389	437,209	269,950	256,948	234,668	205,100
Tower leases	380,467	415,892	426,723	454,800	472,207	599,135	471,303	448,673	465,355	423,468
Tower lease contract settlement	-	-	-	(\$275,000)	-	-	-	-	-	-
Amortization of bond costs	(138,690)	(150,479)	(170,672)	(360,077)	(204,719)	(204,689)	(206,685)	(202,112)	(209,256)	(211,953)
Loss on disposal of equipment	-	1,450	-	-	-	(33,175)	2,000	161	7,672	0
Interest expense	(2,767,890)	(2,357,062)	(2,368,340)	(1,911,202)	(1,888,236)	(1,860,432)	(1,911,438)	(2,208,372)	(2,300,439)	(2,212,192)
Total Non-Operating Income (Loss)	(\$956,181)	(\$1,009,867)	(\$548,328)	(\$354,775)	(\$140,242)	\$332,958	\$452,079	\$373,282	\$554,156	\$541,267
Net Income(loss) before capital contributions per Financial Statements	(\$786,772)	(\$962,265)	(\$724,911)	(\$974,134)	(\$561,184)	(\$700,741)	(\$1,439,634)	(\$1,681,923)	(\$1,346,128)	(\$1,488,640)
Capacity Fees	1,508,090	1,337,085	1,808,924	907,349	1,070,629	985,723	109,037	242,308	309,857	394,546
Add: Depreciation	3,197,862	3,208,842	3,221,943	3,349,668	3,540,690	3,720,333	3,965,632	4,405,077	4,456,160	4,459,807
Amortization	138,690	150,479	170,672	360,077	204,719	204,689	206,685	202,112	209,256	211,953
Interest Expense (Bonds)	2,767,890	2,357,062	2,368,340	1,911,202	1,888,236	1,860,432	1,911,438	2,208,372	2,300,439	2,212,192
Assessments - Debt Service	-	427,784	244,854	244,956	365,377	419,060	508,381	537,759	550,586	542,991
Less: Property Taxes – Debt Service	(360,384)	(378,626)	(320,228)	(269,130)	(125,052)	(409,292)	(817,751)	(967,418)	(1,235,347)	(1,233,107)
Net Earnings Available for Debt Service	\$6,465,375	\$6,140,361	\$6,769,594	\$5,529,988	\$6,383,415	\$6,080,204	\$4,443,788	\$4,946,286	\$5,244,823	\$5,099,741
Debt Service on Revenue Bonds	\$4,177,462	\$4,181,197	\$4,290,731	\$3,944,189	\$3,637,421	\$3,441,126	\$3,438,347	\$3,523,871	\$3,477,484	\$3,660,650
Required per Bond Covenants	120%	120%	120%	120%	120%	120%	120%	120%	120%	120%
Coverage of Debt Service by Net Earnings	155%	147%	158%	140%	175%	177%	129%	140%	151%	139%
Debt Coverage without Capacity Fees	119%	115%	116%	117%	146%	148%	126%	133%	142%	129%

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

Schedule of Change in Net Assets

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Operating Income (Loss from operations)	\$77,398	\$47,602	(\$176,582)	(\$619,359)	(\$420,942)	(\$1,033,699)	(\$1,891,713)	(\$2,055,205)	(\$1,900,284)	(\$2,029,907)
Total Non-Operating Income (Loss)	(\$864,170)	(\$1,009,867)	(\$548,328)	(\$354,775)	(\$140,242)	\$332,958	\$452,079	\$373,282	\$554,156	\$541,267
Capital Contributions	<u>\$2,342,934</u>	<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>	<u>\$696,652</u>	<u>\$1,348,696</u>
Increase (decrease) in net assets	\$1,556,162	\$1,148,866	\$1,646,725	\$179,374	\$1,663,599	\$1,854,345	(\$1,238,061)	(\$702,302)	(\$649,476)	(\$139,944)
Effect of prior period adjustments on net assets		\$5,200,344								
Net assets at beginning of year, as previously reported		\$28,810,231								
Net assets at beginning of year	<u>\$27,254,070</u>	<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>	<u>\$38,563,120</u>	<u>\$37,913,644</u>
Net assets at end of year	<u>\$28,810,231</u>	<u>\$35,159,441</u>	<u>\$36,806,166</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>	<u>\$37,913,644</u>	<u>\$37,773,700</u>



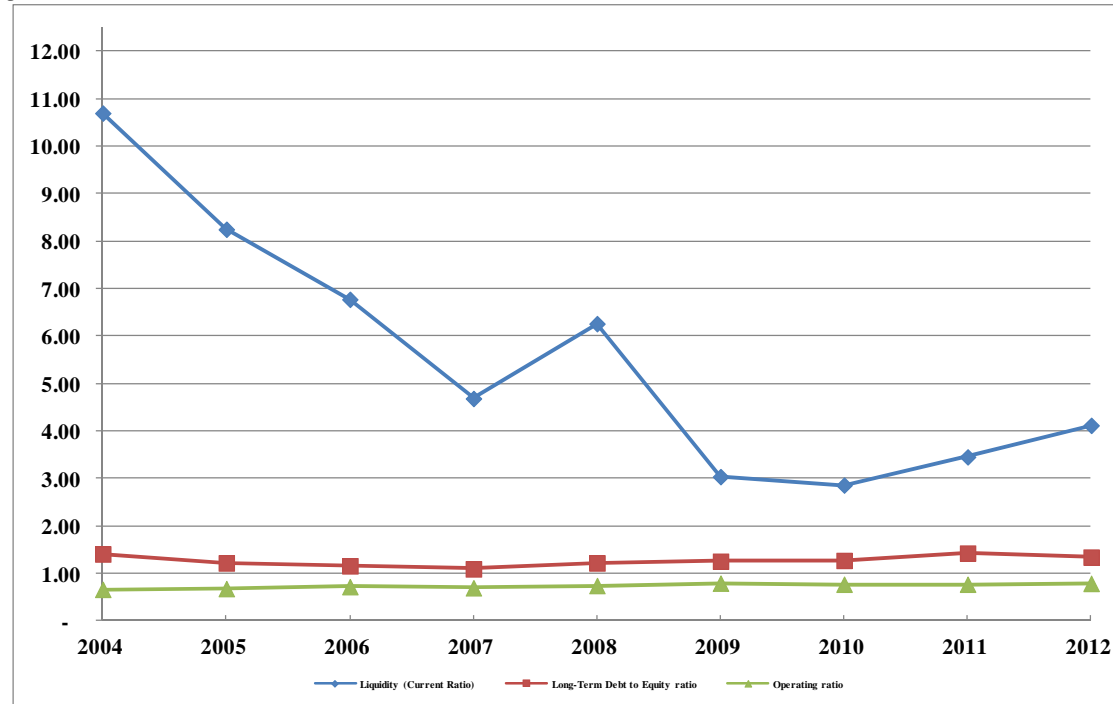
HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

Net Assets by Component⁷

	2004	2005	2006	2007	2008	2009	2010	2011	2012
Net assets									
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	\$27,806,556	\$27,561,464
Restricted for debt service	2,097,137	5,442,647	2,176,688	2,708,532	2,334,594	2,446,988	2,378,848	2,779,466	3,419,743
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>	<u>7,327,622</u>	<u>6,792,493</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>	<u>\$37,913,644</u>	<u>\$37,773,700</u>

Ratio Analysis⁸

	2004	2005	2006	2007	2008	2009	2010	2011	2012
Liquidity (Current Ratio)	10.70	8.25	6.78	4.69	6.26	3.04	2.86	3.46	4.12
Long-Term Debt to Equity ratio	1.41	1.22	1.16	1.10	1.22	1.26	1.27	1.43	1.35
Operating ratio	0.66	0.68	0.72	0.70	0.75	0.80	0.77	0.77	0.79



⁷ Less than 10 years of data is illustrated due to the unavailability of information and the implementation GASB No.34 in fiscal year 2004.

⁸ Less than 10 years of data is illustrated due to the unavailability of information and the implementation GASB No.34 in fiscal year 2004.

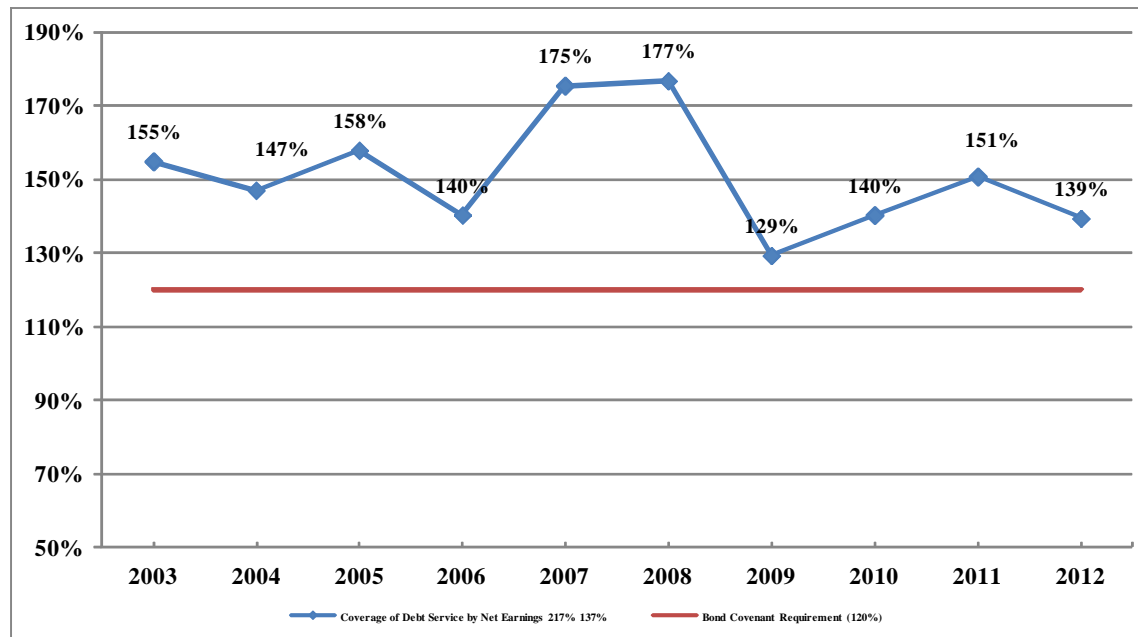
HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

Outstanding Debt by Debt Type

Fiscal Year	GO Bonds	Revenue Bonds	SRF Revenue Loans*	SRF GO Loans	Notes Payable	Total Outstanding Debt	Average Debt Per Customer
2003	1,450,000	44,009,899	9,558,064		349,939	55,367,902	3,485
2004	795,000	42,282,972	9,176,733		331,939	52,586,644	3,243
2005	530,000	41,192,626	8,781,879		313,939	50,818,444	3,058
2006	275,000	37,803,495	8,373,023		295,939	46,747,457	2,779
2007	-	37,972,665	7,949,668		277,939	46,200,272	2,671
2008	7,350,000	36,853,711	7,511,300		259,939	51,974,950	2,989
2009	7,085,000	35,388,165	7,057,386	3,276,237	241,939	53,048,727	3,057
2010	8,476,338	34,383,013	6,587,376	3,149,328	223,939	52,819,994	3,050
2011	11,866,601	36,906,574	6,100,698	3,018,480	205,939	58,098,292	3,330
2012	11,313,078	41,004,952	-	2,877,671	187,939	55,383,640	3,166

* Note: The Series 2000A SRF Revenue Loan was refunded in August 2011. Also, please reference the Summary Schedule of Debt on page 74 for supporting documentation.

Debt Service Coverage Analysis



HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT
Schedule of Changes in Capital Assets
Last Ten Fiscal Years

	June 30, 2003	Additions	Disposals	Fiscal Year 2011 Transfers Reclassifications*	June 30, 2012
<u>Capital assets not being depreciated:</u>					
Land	\$ 368,614	930,580	-	-	\$ 1,299,194
Construction in Progress	1,836,586	39,959,142	-	(41,241,837)	553,892
Total Capital Assets not being depreciated	2,205,200	40,889,722	-	(41,241,837)	1,853,086
 Capital assets being depreciated:					
Waterworks system	34,827,349	1,465,220	(1,024,703)	19,827,152	55,352,880
Sewage disposal system	10,013,537	2,308,867	(119,253)	21,240,924	35,040,328
Buildings	4,153,874	81,227	(2,452)	81,721	4,299,512
Sewage treatment facilities	36,522,658	92,670	(3,560)	26,736	34,711,422
Transportation equipment	1,016,536	619,536	(945,132)	-	915,148
Operations furniture and equipment	1,962,348	244,543	(352,008)	62,188	1,681,614
Office furniture and equipment	854,435	152,466	(404,094)	-	701,878
Sub Total	89,350,737	4,964,528	(2,851,202)	41,238,721	132,702,782
Less Accumulated depreciation	(21,961,131)	(34,331,762)	2,735,147	-	(53,557,747)
Total capital assets being depreciated, net	67,389,606	(29,367,234)	(116,055)	41,238,721	79,145,035
 Year End Totals	\$ 69,594,806	11,522,488	(116,055)	-	\$ 80,998,121

* During Fiscal Year 2012 Capital Assets items were revisited to verify that all assets were designated in the correct categories for Fiscal Year 2011.
It was determined at that time that certain assets should be moved from one category to another with an effective date of June 30, 2011.

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

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
PP&E	\$ 89,719,351	\$ 93,660,892	\$ 95,834,607	\$ 96,222,163	\$ 101,306,310	\$ 107,539,856	\$ 121,309,803	\$ 124,015,092	\$ 126,932,175	\$ 134,001,976
Accumulated Depreciation	(21,961,131)	(24,905,146)	(28,027,340)	(29,642,022)	(33,057,250)	(36,681,713)	(40,512,192)	(44,736,215)	(49,097,940)	(53,557,747)
Net PP&E in Service	67,758,220	68,755,747	67,807,266	66,580,141	68,249,059	70,858,143	80,797,611	79,278,877	77,834,235	80,444,229
Construction in Progress	1,836,586	306,918	928,300	3,005,393	2,720,938	4,542,373	641,980	1,236,180	3,514,449	553,892
 Net PP&E	\$ 69,594,805	\$ 69,062,665	\$ 68,735,566	\$ 69,585,534	\$ 70,969,998	\$ 75,400,516	\$ 81,439,592	\$ 80,515,057	\$ 81,348,684	\$ 80,998,121

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

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
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%
2011	16,395	0.5%	15,030	0.9%	91.7%
2012	16,441	0.3%	15,109	0.5%	91.9%

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

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

Reported in kgals (thousands of gallons)

Year	Water	Percent Increase	Wastewater	% Inc
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%
2011	1,644,020	10.6%	1,426,486	11.5%
2012	1,656,442	0.8%	1,425,564	-0.1%

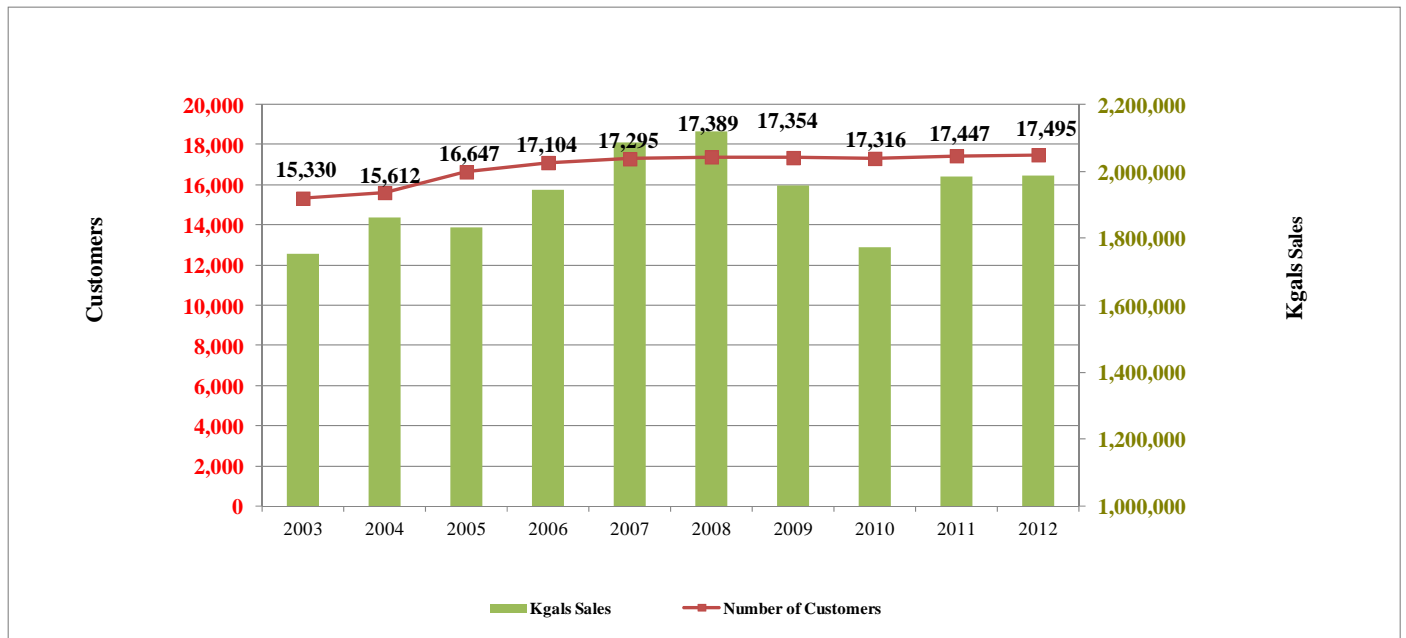
Billings at Fiscal Year-End (Water and Irrigation)

Reported in kgals (thousands of gallons)

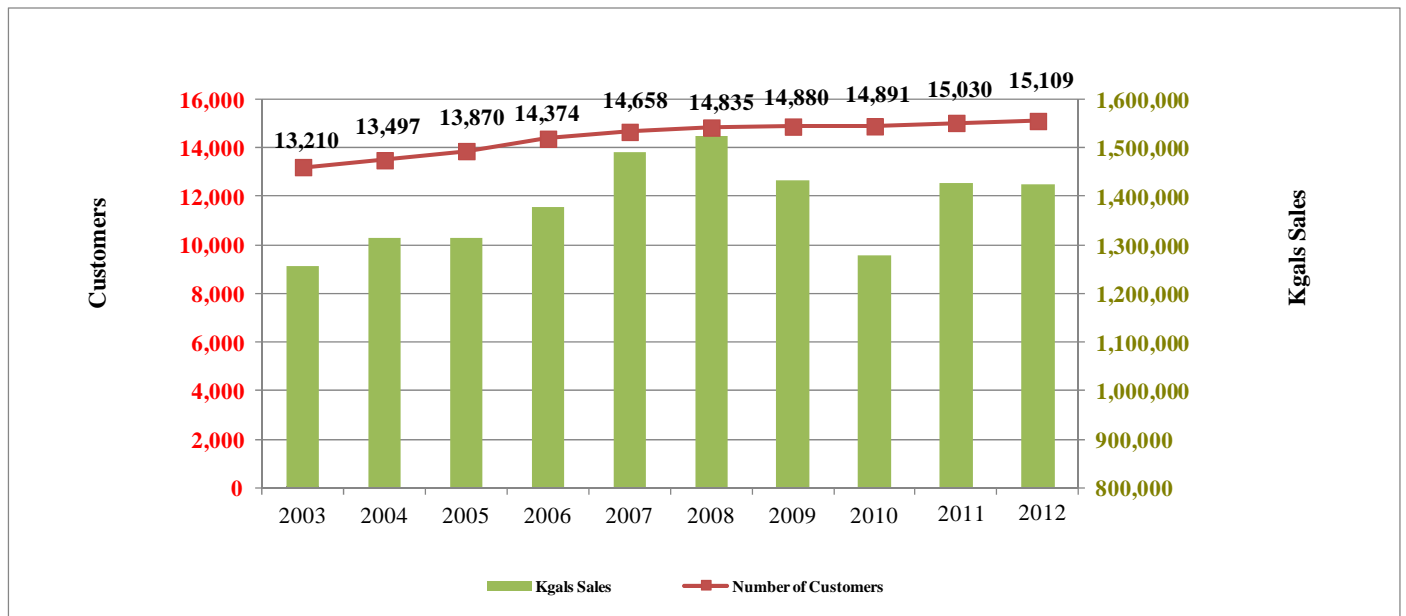
Year	Water/Irrigation	Percent Increase	Wastewater	% Inc
2003	1,753,397	-8.7%	1,255,115	-5.7%
2004	1,861,014	6.1%	1,314,219	4.7%
2005	1,834,200	-1.4%	1,313,400	-0.1%
2006	1,943,868	6.0%	1,378,504	5.0%
2007	2,086,348	7.3%	1,490,636	8.1%
2008	2,119,295	1.6%	1,523,113	2.2%
2009	1,957,926	-7.6%	1,432,874	-5.9%
2010	1,773,200	-9.4%	1,279,144	-10.7%
2011	1,983,289	11.8%	1,426,486	11.5%
2012	1,986,913	0.2%	1,425,564	-0.1%

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

Customers vs. Water/Irrigation Kgal Sales



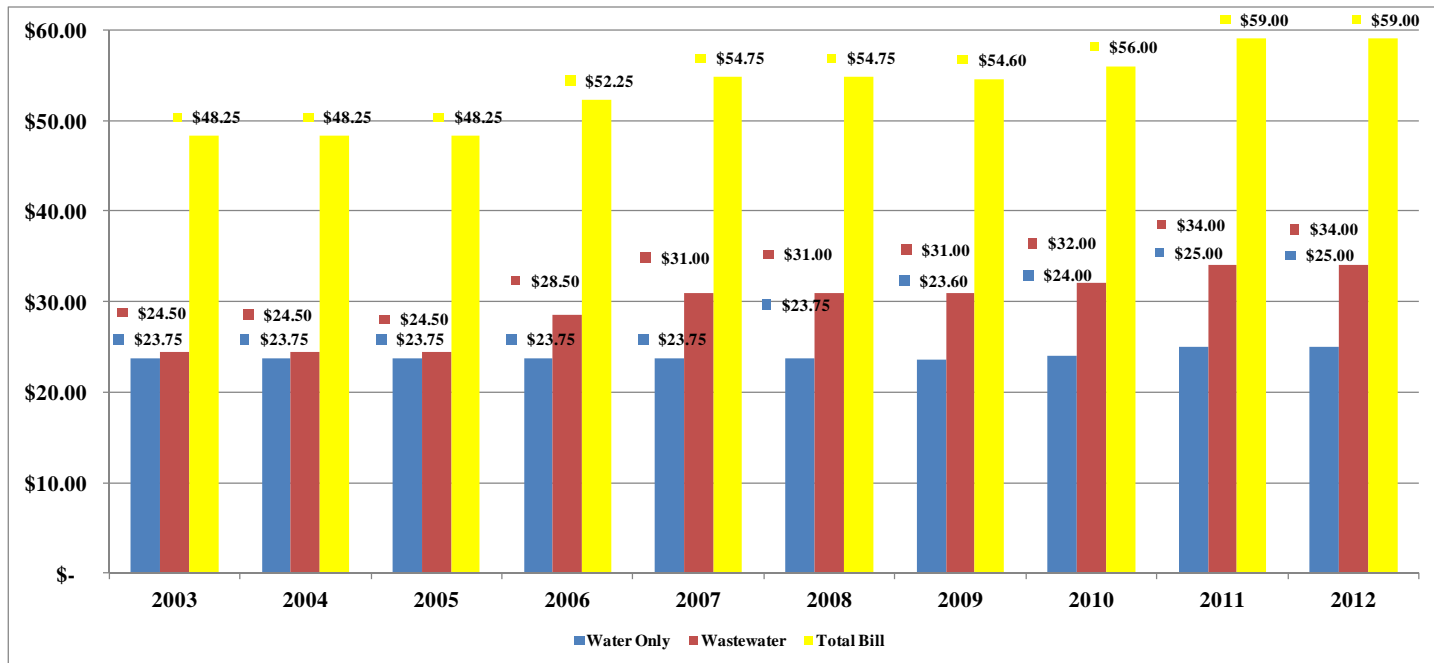
Customers vs. Wastewater Kgal Sales



HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

Water Rate Comparison											
Effective Date											
		FY'03	FY'04	FY'05	FY'06	FY'07	FY'08	FY'09*	FY'10**	FY'11***	FY'12
Residential	Base Charge	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 10.00	\$ 11.00	\$ 11.00
	First 5,000 Gallons	\$ 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				
	Next 18,000 to 32,000 gallons	\$ 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				
	First 10,000 Gallons Water							\$ 1.36	\$ 1.40	\$ 1.40	\$ 1.40
	First 10,000 Gallons Irrigation							\$ 1.36	\$ 1.40	\$ 1.71	\$ 1.71
	Next 11,000 to 20,000 gallons							\$ 1.64	\$ 1.71	\$ 1.71	\$ 1.71
	Next 21,000 to 30,000 gallons							\$ 1.91	\$ 2.20	\$ 2.20	\$ 2.20
	Over 30,000 gallons							\$ 2.18	\$ 2.55	\$ 2.55	\$ 2.55
Commercial	Base Charge	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 15.00	\$ 16.00	\$ 16.00
	First 5,000 Gallons	\$ 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				
	Next 18,000 to 32,000 gallons	\$ 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				
	First 10,000 Gallons							\$ 1.64	\$ 1.69	\$ 1.69	\$ 1.69
	Next 11,000 to 20,000 gallons							\$ 1.91	\$ 1.99	\$ 1.99	\$ 1.99
	Next 21,000 to 30,000 gallons							\$ 2.18	\$ 2.51	\$ 2.51	\$ 2.51
	Over 30,000 gallons							\$ 2.45	\$ 2.87	\$ 2.87	\$ 2.87
*Effective August 1, 2008											
**Effective October 1, 2009											
***Effective May 1, 2011											
Wastewater Rate Comparison											
Effective Date											
		FY'03	FY'04	FY'05	FY'06*	FY'07**	FY'08	FY'09	FY'10	FY'11	FY'12
Residential	Base Charge	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 14.00	\$ 14.00
	Per 1,000 gallons with Cap*	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.65	\$ 1.90	\$ 1.90	\$ 1.90	\$ 2.00	\$ 2.00	\$ 2.00
Commercial	Base	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 12.00	\$ 14.00	\$ 14.00
	Per 1,000 gallons (No Cap)	\$ 1.25	\$ 1.25	\$ 1.25	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.50	\$ 1.60	\$ 2.00	\$ 2.00
*For years prior to FY'06, the effective sewer cap for residential customers was 32,000 gallons. From FY'06 to the present date the sewer cap is lowered to 10,000 gallons.											
**Per Thousand Increase Effective August 1, 2006											

Water Water/Wastewater Bill History (Residential Customers Using 10 Kgals/Month)



HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

Population per Capita Income

Last Ten Available Years

	Hilton Head		Beaufort County		South Carolina	
Year	Population	Per Capita	Population	Per Capita	Population	Per Capita
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	41,411	146,722	44,123	4,404,914	31,990
2008	33,913	42,611	150,415	44,583	4,479,800	32,971
2009	34,249	41,951	155,215	42,313	4,554,258	31,653
2010	37,099	40,798	162,233	42,430	4,625,364	32,462
2011	37,675	41,846	164,684	N/A	4,679,230	33,673

Source: Bureau of Economic Analysis, Regional Economic Information Systems, U.S. Census Bureau

Beaufort County Top Employers

Employer	Employees	Percentage of Total County Employment	Type of Business
Department of Defense	7,352	12.2%	Military
Beaufort County School District	3,159	5.3%	Educational Services
Beaufort Memorial Hospital	1,404	2.3%	Health Services
County of Beaufort	1,128	1.9%	Government
Marine Corps Community Services	789	1.3%	Military
Hilton Head Health System	700	1.2%	Health Services
Sea Pines Resort	479	0.8%	Hospitality
CareCore National	419	0.7%	Health Services
Wal-Mart	400	0.7%	Retail
University of South Carolina Beaufort	389	0.6%	Educational Services

Source: Beaufort County Regional Chamber of Commerce

Beaufort County Labor Force and Employment

Category	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002
Civilian Labor Force	63,623	63,125	62,784	63,855	64,019	62,759	61,381	58,830	55,921	53,372
Employment	58,091	57,397	57,173	60,488	61,256	59,786	58,372	55,914	53,259	51,130
Unemployment	5,532	5,728	5,611	3,367	2,763	2,973	3,009	2,916	2,662	2,242
Unemployment Rate	8.69%	9.07%	8.94%	5.27%	4.32%	4.74%	4.90%	4.96%	4.76%	4.20%

Source: South Carolina Department of Employment and Workforce

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

Unemployment Rate Comparison

Year	County	South Carolina	United States
2011	8.7%	11.2%	9.6%
2010	9.1	11.7	9.3
2009	8.9	6.9	5.8
2008	5.3	5.6	4.6
2007	4.3	6.5	4.6
2006	4.7	6.7	5.1
2005	4.9	6.8	5.5
2004	5.0	6.7	6.0
2003	4.8	5.9	5.8
2002	4.2	N/A	N/A
Source: South Carolina Department of Employment and Workforce			

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

The District's Millage History

Debt Type	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
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	1.10	1.00	0.50	1.50	2.70	2.82	3.61	3.61
Total	5.00	5.00	4.10	4.00	3.50	4.50	5.70	5.82	6.61	6.61

Sources: Beaufort County Auditor and Treasurer

Overlapping Debt

Jurisdiction	2011 Assessed Value (Capped)	2011 Assessed Value (Capped) of the District	Outstanding General Obligation Debt	Amount Applicable to the District
County of Beaufort	\$1,811,500,538	\$369,960,240	\$190,915,000	\$34,364,700
Beaufort County School District	1,811,500,538	369,960,240	314,344,621	56,582,032
Town of Hilton Head	923,053,038	345,910,777	62,010,000	21,703,500

Sources: Beaufort County Auditor and Treasurer.

Note: Overlapping governments are those that coincide, at least in part, with geographic boundaries of the District, located on Hilton Head Island, South Carolina and Beaufort County. This schedule estimates the portion of the outstanding debt of those overlapping governments that is borne by the property taxpayers of Hilton Head No. 1 Public Service. This process recognizes that, when considering the government's ability to issue and repay long-term debt, the entire debt burden borne by the property taxpayers should be taken into account. However, this does not imply that every taxpayer is a resident, and therefore responsible for repaying the debt, of each overlapping government.

Assessed Values of the District

Year	Real Property	Personal Property ⁽¹⁾	Total
2011	\$ 336,927,670	\$ 33,032,570	\$ 369,960,240
2010	337,319,400	43,129,020	380,448,420
2009 ⁽²⁾	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 ⁽³⁾	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

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.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

2011 Market Value for the District

Classification	Assessed Value	Assessment Ratio	Market Value
1. Real Property and Mobile Homes	\$ 136,321,050	4.00%	\$ 4,000,000,992
2. Real Property and Mobile Homes	200,606,620	6.00%	4,228,694,485
3. Business Personal Property	4,901,950	10.50%	46,554,250
4. Merchant's Furniture, Fixtures and Equipment	1,182,210	10.50%	11,259,570
5. Motor Vehicles ⁽¹⁾	13,926,770	Various	213,787,160
6. Marine Equipment ⁽²⁾	1,250,000	Various	20,841,320
7. Airplanes	113,230	0.00%	1,887,080
8. Manufacturing Property	222,000	10.50%	2,114,290
9. Public Utilities	8,653,000	10.50%	82,409,540
10. Rental Property and Signs ⁽³⁾	2,783,410	Various	26,382,500

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.

Source: Beaufort County Auditor.

⁽¹⁾ Includes personal automobiles and commercial vehicles, which are assessed at different ratios.

⁽²⁾ Includes personal watercraft and commercial fishing boats, which are assessed at different ratios.

⁽³⁾ Includes residential rental property and commercial signs, which are assessed at different ratios.

Tax Collection Record for the District

Fiscal Year	Taxes Subject to Collection	Current Collections	Current % Collected	Delinquent Taxes Collected	Total Collections	Total % Collected
2011-12	\$ 55,424,959	\$ 52,849,333	95.4%	\$ 163,278	\$ 53,012,611	95.6%
2010-11	59,167,642	56,320,727	95.2	161,774	56,482,501	95.5
2009-10	57,172,896	52,623,858	92.0	491,840	53,115,698	92.9
2008-09	56,329,331	54,777,459	97.2	869,821	55,647,279	98.8
2007-08	51,252,916	50,333,765	98.2	652,019	50,985,784	99.5
2006-07	54,353,422	52,223,375	96.1	424,257	52,647,631	96.8
2005-06	49,747,721	46,454,422	93.3	617,181	47,071,603	94.6
2004-05*	50,467,835	44,421,691	88.0	422,203	44,843,894	88.8
2003-04	44,449,943	41,178,415	92.6	395,576	41,573,991	93.5
2002-03	41,924,960	39,560,970	94.3	433,015	39,993,985	95.3

Source: Beaufort County Auditor and Treasurer.

* Lower collections due to unresolved appeals.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

District Largest Taxpayers

Employer	Type of Business	2011 Assessed Value	2010-11 Amounts Paid
1. Marriott Ownership Resorts, Inc.	Real Estate	\$7,474,100	\$1,444,094
2. SCG Hilton Head Property LLC	Real Estate	4,260,000	\$837,204
3. Palmetto Electric Coop, Inc	Utility	4,483,200	\$830,614
4. Hargray Telephone Company, Inc	Utility	2,681,850	\$509,898
5. Hilton Head Health System LP	Medical	1,883,870	\$371,396
6. Festival Centre (E&A) LLC	Golf	1,197,170	\$251,145
7. Heritage Golf Port Royal LLC	Golf	1,155,540	\$241,594
8. Indigo Run Asset Corp.	Property	782,440	\$169,283
9. Time Warner NY Cable LLC	Utility	724,010	\$138,915
10. SVG LLC	Property	582,580	\$120,054
Source: Beaufort County Auditor.			

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

District Top Ten Water Users

Fiscal year ended June 30, 2012

User Name	Type	2012 Billed Revenues	% of Total 2012 Billed Revenues
Hilton Head Beach & Tennis	Resort	\$ 173,215	2.91%
Cypress of Hilton Head Island Assoc.	Residential Homes	154,937	2.60%
Hilton Head Westin Resort	Resort	116,059	1.95%
Hilton Head Resort/Four Seasons	Resort	94,975	1.60%
Marriott Vacation Club	Resort	84,892	1.43%
Marriott Surfwatch	Resort	76,426	1.28%
Fiddler's Cove	Resort	63,242	1.06%
Marshside Owners Association	Apartment Complex	50,760	0.85%
Spa at Port Royal	Resort	47,010	0.79%
Hilton Head Health Systems	Medical	43,354	0.73%
Remaining Customers		<u>5,044,511</u>	<u>84.79%</u>
		<u>\$ 5,949,379</u>	100.00%

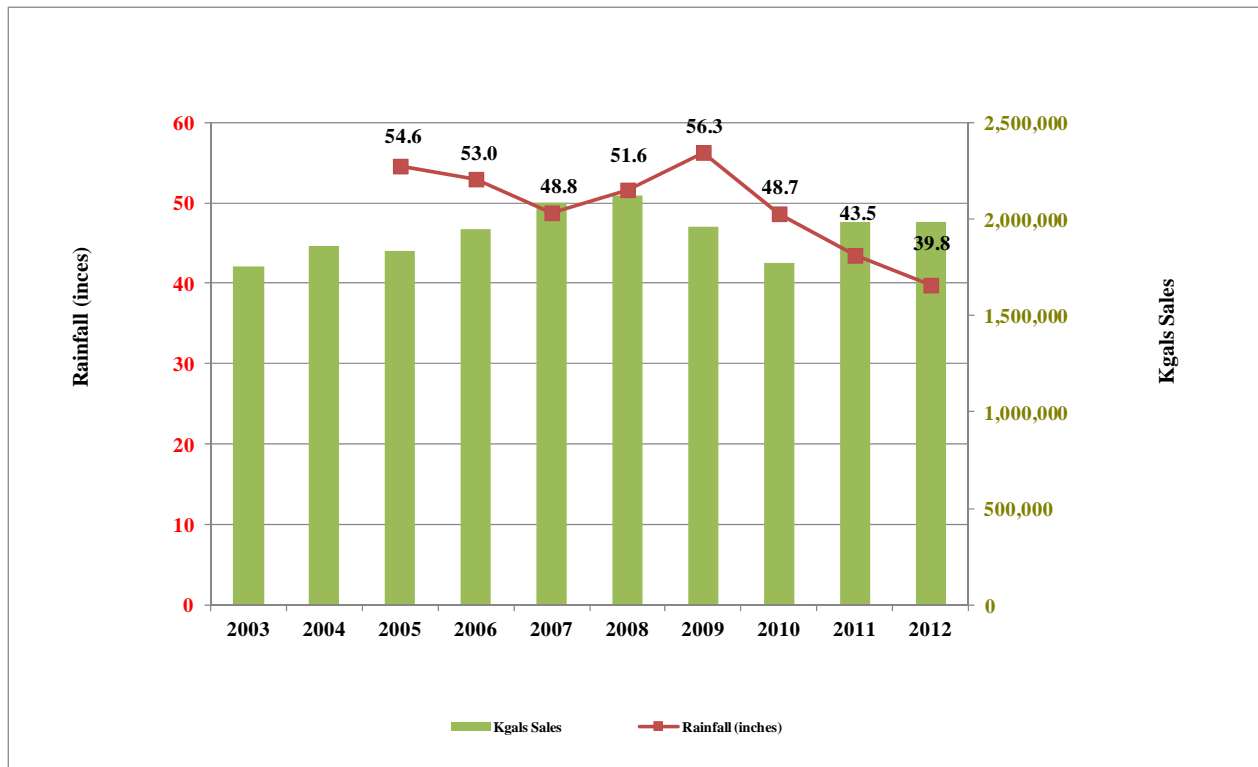
District Top Ten Wastewater Users

Fiscal year ended June 30, 2012

User Name	Type	2012 Billed Revenues	% of Total 2012 Billed Revenues
Hilton Head Beach & Tennis	Resort	\$ 186,166	4.12%
Hilton Head Resort/Four Seasons	Resort	122,670	2.71%
Hilton Head Westin Resort	Resort	105,718	2.34%
Fiddler's Cove	Resort	79,667	1.76%
Cypress of Hilton Head Island Assoc.	Residential Homes	77,071	1.70%
Marriott Vacation Club	Resort	75,704	1.67%
Spa at Port Royal	Resort	61,364	1.36%
Marriott Surfwatch	Resort	58,662	1.30%
IMC	Resort	49,352	1.09%
Marshside Owners Association	Apartment Complex	47,616	1.05%
Remaining Customers		<u>3,658,444</u>	<u>80.90%</u>
		<u>\$ 4,522,434</u>	100.00%

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

Rainfall (Inches) vs. Water/Irrigation Kgal Sales⁹



⁹ Rainfall data is not available for 2003 and 2004.

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT

Beaufort-Jasper Water and Sewer Authority (BJWSA)-Purchased Water Expense Summary												
Water Purchased from BJWSA Summary (Whole Dollars)												
	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010 ²	FY 2011	FY 2012		
All District Purchases from BJWSA	\$ 1,146,852	\$ 1,225,760	\$ 1,394,283	\$ 1,580,406	\$ 1,593,943	\$ 1,518,423	\$ 1,364,990	\$ 934,368	\$ 1,199,029	\$ 1,472,568		
Reclaimed Water Adjustment ³	-	-	-	64,800	77,760	77,760	77,760	25,920	-	-		
Broad Creek Purchases	-	-	-	-	-	-	(85,947)	(213,717)	(174,574)	(192,363)		
Capitalized Purchased Water	-	-	-	-	-	-	-	-	-	(171,887)		
Prepaid Purchased Water Expense	-	-	-	-	-	-	-	-	-	(79,529)		
Purchased Water Expense	\$ 1,146,852	\$ 1,225,760	\$ 1,394,283	\$ 1,645,206	\$ 1,671,703	\$ 1,596,183	\$ 1,356,803	\$ 746,571	\$ 1,024,455	\$ 1,028,789		
Water Purchased from BJWSA Summary (KGals)												
	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012		
All Kgals Purchased from BJWSA	924,881	988,516	1,124,422	1,089,935	1,390,980	1,047,188	863,918	679,724	877,933	1,240,631		
Reclaimed Water Adjustment	-	-	-	-	-	-	-	-	-	-		
Broad Creek Purchases	-	-	-	-	-	-	(54,397)	(208,191)	(178,539)	(192,469)		
Capitalized Purchased Water	-	-	-	-	-	-	-	-	-	(217,579)		
Prepaid Purchased Water Expense	-	-	-	-	-	-	-	-	-	(79,413)		
Purchased Water Expense	924,881	988,516	1,124,422	1,089,935	1,390,980	1,047,188	809,521	471,533	699,394	751,170		
Total Peak Purchases	924,881	988,516	1,124,422	1,089,935	822,794	1,047,188	863,918	511,537	648,537	623,380		
Total Off-peak Purchases	-	-	-	-	568,186	-	-	168,187	229,396	617,251		
Total Off-peak and Peak Purchases	924,881	988,516	1,124,422	1,089,935	1,390,980	1,047,188	863,918	679,724	877,933	1,240,631		
BJWSA Rates Per Kgal Summary												
	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012		
Rates Charged by BJWSA												
Peak Rate	\$ 1.24	\$ 1.24	\$ 1.24	\$ 1.45	\$ 1.45	\$ 1.45	\$ 1.58	\$ 1.58	\$ 1.58	\$ 1.58		
Off Peak Rate	\$ -	\$ -	\$ -	\$ -	\$ 0.71	\$ -	\$ -	\$ 0.75	\$ 0.76	\$ 0.79		
District Cost/Kgal Prior to Broad Creek Purchases⁴												
Effective District Cost/Kgal After	\$ 1.24	\$ 1.24	\$ 1.24	\$ 1.45	\$ 1.15	\$ 1.45	\$ 1.58	\$ 1.37	\$ 1.37	\$ 1.19		
Broad Creek Purchases⁵												
	N/A	N/A	N/A	N/A	N/A	N/A	\$ 1.58	\$ 1.53	\$ 1.46	\$ 1.22		
¹ Nov 2006 - Feb 2007 there was an off-Peak Rate of \$0.71/kgal applied to all consumption.												
² Off-peak rate agreement signed September, 2009 and the rate increases every year based on CPI.												
³ This adjustment adds the potable water expense associated with providing reclaimed water to golf courses at a reduced rate in exchange for potable water withdrawal rights to certain wells.												
⁴ Combined peak and off-peak purchases calculated as all District purchases from BJWSA divided by all Kgals purchased from BJWSA.												
⁵ During off-peak months, the District pays the peak rate for the first 1 million gallons purchased from BJWSA and the off-peak rate for any amount purchased over one million gallons. However, the District charges the Broad Creek PSD the off-peak rate for all of the water that they purchase during off-peak months. During peak months Broad Creek PSD is charged the peak price. As such, this calculation backs out Broad Creek PSD payments to the District and the Kgals that Broad Creek purchased to arrive at the District's Effective Cost/Kgal for its own water usage.												

HILTON HEAD NO. 1 PUBLIC SERVICE DISTRICT



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