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SHEEP CREEK WATER COMPANY SPECIAL SHAREHOLDERS MEETING- AUGUST 17, 2019

New Business Agenda items to be presented to the Shareholders of the Sheep Creek Water Company for consideration and vote.

Agenda item IV a

Well #11 Loan Repayment Revote: A total loan amount of \$428,000 is outstanding for the completion of Well #11. Annual principal payments of \$85,000 plus monthly interest payments. The cost to install Well #11 with offsite infrastructure upgrades was \$1,113,796. The Board of Directors is asking the Shareholders how they prefer to repay the loan.

The following repayment options for the Well #11 loan repayment:

1. Assessment- \$15 per share, per year for 5 years.
2. \$8.00 base rate increase per month per meter service for 5 years.
3. \$5.00 base rate increase per month per meter service plus Tier 3 Overage Charges.

Total Estimated Cost per Option:

- 1.) **Assessment- \$75.00 per Share** (\$15 per share per year for 5 years)
- 2.) **\$8.00 Base Rate Increase- \$480.00 per Meter Service** (\$8.00 per meter per month for 5 years)
- 3.) **\$5.00 Base Rate Increase- \$300.00 per Meter Service plus Tier 3 Overage** (\$5.00 per meter per month for 5 years plus Tier 3 Overage Charges) Tier 3 Overage is not charged if customer remains within their allotment.

Agenda Item IV b

Updated Allotment Plan Revote: The Board of Directors has proposed an updated Allotment Plan to adjust allotments as needed with current safe production. Allotments cannot be increased without ground water levels increasing, in addition to well production increasing. Short term increases do not always allow for increase in allotment. Allotments will be posted on the Sheep Creek Water Company website. The Board of Directors will approve parameters for allotment adjustments when needed. The updated allotment Plan can be found at https://sheepcreekwater.com/documents/816/Allotment_Schedule_2019.pdf

Agenda Item IV c

State Water Resources Control Board- Source Capacity Violation: August 30, 2018, Compliance Order NO. 05-13-18R-002 was issued by the State Water Resources Control Board (SWRCB) Drinking Water Division. The SWRCB placed a service connection and building moratorium on Sheep Creek Water Company (SCWC). SCWC cannot place any new service connections or cannot issue any "Will Serve Letters" for any building permits. Due to the drought in California, SCWC's well levels and production have been on a steady decline and beginning in June of 2016 well production began to drop significantly. Again in 2018 well production dropped causing the SWRCB to issue a Source Capacity Violation due to SCWC unable to meet the required 10 Year Maximum Day Demand (MDD). In order for SCWC to meet the required 10 year MDD,

SCWC needs to have a pumping capacity of 1,453 gallons per minute or 2.09 million gallons a day (MGD). As of July 31, 2018, the total pumping capacity was 502 gallons per minute, or .72 MGD.

The SWRCB required a Feasibility Study be completed by SCWC. SCWC contracted with Infrastructure Engineering Corporation (IEC) to complete the required Feasibility Study. The report was required to have options to bring SCWC into compliance with the regulation to meet the MDD. One option required to be considered is consolidation with Phelan Pinon Hills Community Services District (PPHCSD). Based on production records for July 2018, SCWC could produce .72 MGD and with the addition of Well #11 (361,440 gallons per day), SCWC's total production is 1.08 MGD. The engineering report developed from IEC reduced the MDD from 2.09 MGD to 1.78 MGD leaving a deficit of .70 MGD plus a required stand-by well. SCWC will need to drill additional wells to come into compliance with the MDD regulation.

The IEC Feasibility Study can be found at:

https://sheepcreekwater.com/documents/816/Final_SCWC_Feasibility_Report_2019-01-14_Part_1.pdf

https://sheepcreekwater.com/documents/816/Final_SCWC_Feasibility_Report_2019-01-14_Part_2.pdf

I. Well Drilling for Source Compliance:

Based on the information provided about the newly constructed Well #11, SCWC will need to drill additional wells to increase available production to meet the required MDD. The engineering report developed from IEC reduced the MDD from 2.09 MGD to 1.78 MGD, which would require two to four wells be drilled. If production on additional wells is higher than the estimated 250 gpm, this may reduce the number of wells necessary to achieve the required MDD. Several meter services for the Snowline School District have been transferred to PPHCSD and if additional services are transferred, SCWC's MDD may be further reduced. Engineers estimate that the cost to drill and equip wells along with associated pipework to connect to the existing water system is **\$5,806,000**.

At this time SCWC will be borrowing funds as needed to complete the well project. Due to the length of time that the project will take, current funds that are being collected will be used towards the project to further reduce the loan needed, reducing interest and cost to Shareholders. SCWC is currently working with an Infrastructure Banking Lender to borrow the needed funds. SCWC is estimating the cost to complete each well at \$900,000, which is based on the cost to complete Well 11. SCWC is estimating to install three wells to come into compliance with the SWRCB but until the wells are drilled have to plan for four wells. SCWC's estimated cost to complete up to four wells is **\$3,600,000**. Option for loan payments will be presented to the Shareholders during the Annual Shareholders Meeting in May 2020. SCWC will begin the environmental process with the funds currently available.

Below are example payment estimates that will be presented to the Shareholders for approval.

- **Full loan amount of \$3,600,000 at an interest rate of 4.5% with 10 year repayment:**
 - **Assessment on Shares- \$30 per share twice a year for 10 years (\$600 per share).**
 - **Base Rate Increase- \$31.50 per month per meter for 10 years (\$3,782 per meter service).**
 - **Water Rate Increase- \$1.95 per HCF (\$2,808 based on 12 hcf per month).**
 - **Split Assessment & Base Rate Option - Assessment of \$30 per share once a year for ten years and Base Rate Increase of \$15.75 per month for ten years.**

- **Loan amount of \$2,500,000 at an interest rate of 4.5% with a 10 year repayment:**
 - **Assessment on Shares- \$30 per share twice a year for 7 years (\$420 per share).**
 - **Base Rate Increase- \$22 per month per meter for 10 years (\$2,655 per meter service).**
 - **Water Rate Increase- \$1.40 per HCF (\$2,016 based on 12 hcf per month).**

- **Split Assessment & Base Rate Option- Assessment of \$30 per share once a year for ten years and Base Rate Increase of \$11 per month for ten years.**

II. Evaluation of Consolidation of Sheep Creek Water Company with Phelan Pinon Hills Community Service District:

The SWRCB required SCWC to evaluate consolidation of Sheep Creek Water Company with Phelan Pinon Hills Community Service District as an option to come into compliance. The feasibility study completed by IEC evaluated this option as an alternative to drilling additional wells and remaining private. The IEC report can be found on the SCWC website.

Engineers estimated cost for consolidation with PPHCSD was **\$3,374,700**. Grant funding of **\$5,000,000** was available for consolidation through the State of California SWRCB. The remaining funds from the grant would have been used towards additional upgrades or repairs to the Sheep Creek Water System. Additional grant funding of \$5,000,000 was potentially available for additional replacement and upgrades. All existing debt owed by SCWC would have needed to be paid by the SCWC Shareholders. Current debt owed by SCWC is \$600,000.

The SCWC Board of Directors submitted a proposed Consolidation Plan along with an Appraisal Report of the Sheep Creek Water Company to the PPHCSD for its review and consideration. The Board of Directors for PPHCSD met on July 17, 2019 and rejected the proposed Consolidation Plan presented by SCWC.

The proposed Consolidation Plan can be found at:

https://sheepcreekwater.com/documents/816/Sheep_Creek_Consolidation_Plan_6-18-19.pdf

III. Action Required:

Based on PPHCSD rejection of the proposed Consolidation Plan, there will be no vote on the merger issue, and SCWC must now proceed with well drilling, in order to meet SWRCB source compliance requirements. However, SCWC By-Laws §7.01 provides that “Expenditures for capital improvements exceeding \$10,000.00 shall require approval from the Shareholders”. So, a Shareholder Vote will be taken to authorize such well drilling. Failure to authorize such well drilling will cause SCWC to be in violation of SWRCB requirements.