

City of Missoula Water Utility

Securing Our Community's Future
By Securing Its Water System

Today's Presentation

- Introduction of the team
- Review of actions to date
- Review of valuation methods
- Financial review
- Types of purchase
- Legal overview
- Expenses
- Reasons for public ownership

The Team

- Roy Koegen, bond counsel, Koegen & Edwards, Spokane, Washington
- Roger Wood, managing director, Moelis & Company investment bankers, New York, New York
- Roy Tucker, mergers and acquisitions counsel, Perkins Coie, Portland, Oregon
- Harry Schneider, litigation counsel, Perkins Coie, Seattle, Washington
- Mary Edwards, bond counsel, Koegen & Edwards, Spokane, Washington
- David MacGillivray, financial advisor, Springsted Public Sector Advisors, Minneapolis, Minnesota
- Sean Keatts, underwriter, Barclays, Seattle, Washington
- Bruce Bender, chief administrative officer, City of Missoula
- Jim Nugent, city attorney, City of Missoula
- Ginny Merriam, communications director, City of Missoula
- Brentt Ramharter, retired finance officer, City of Missoula
- Marilyn Marler, president, Missoula City Council
- Jason Wiener, member, Missoula City Council
- John Engen, mayor, City of Missoula

How we got here

- December 2010, Carlyle announces intention to buy Mountain Water
- Early 2011, City of Missoula agrees to support sale to Carlyle
- October 2011, City of Missoula advocates for sale to Public Service Commission
- December 2011, Carlyle completes transaction with PSC approval
- Carlyle, City agree to maintain dialog until former owner leaves board
- January 2013, City begins assembling informal offer to Carlyle
- Team arrives at \$65 million for a stock sale
- February 2013, Carlyle rejects informal offer, cites surprise barriers to sale
- City team works to understand Carlyle's objections and overcome them
- October 2013, City Council meeting to discuss further offer to Carlyle; council approves ordinance authorizing negotiation and condemnation as necessary
- November 2013, Carlyle rejects City's restated \$65 million offer
- December 2013, Carlyle rumored to changing investment focus away from water/infrastructure
- Team agrees to actively pursue condemnation to ensure position in any future transaction, makes offer of \$50 million for assets of Mountain Water
- To date, Carlyle has not met its commitments and obligations to the City

What's the system worth?

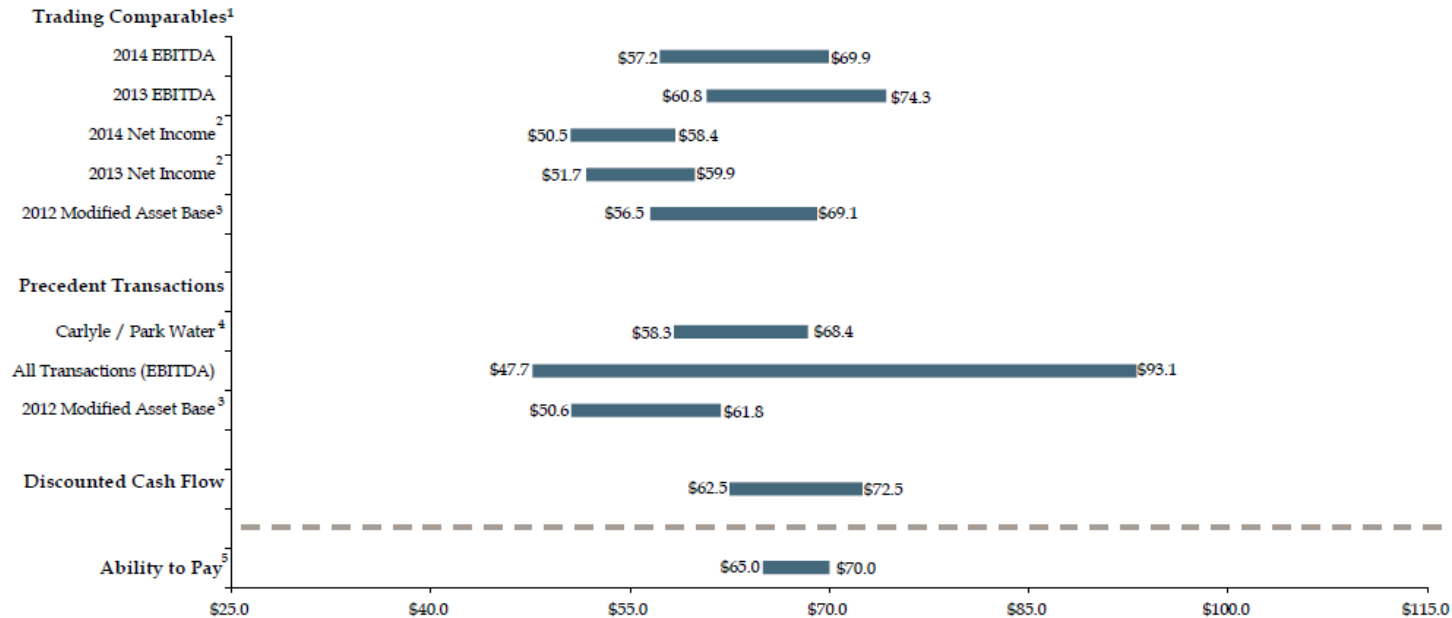
- Moelis' analysis
 - Publicly Traded Company Analysis
 - Selected Precedent Transactions Analysis
 - Discounted Cash Flow Analysis

Valuation Overview

Indicative Valuation - Overview

MOELIS & COMPANY

\$ in millions



Note:

- Includes: American States Water Company ("AWR"), American Water Works Company ("AWK"), Aqua America ("WTR"), Artesian Resources ("ARTNA"), California Water Service Group ("CWT"), Connecticut Water Service ("CTWS"), Middlesex Water ("MSEX"), SJW Corp. ("SJW"), York Water ("YORW")
- Mountain Water Net Income calculated by deducting out tax interest expense from reported earnings based on \$17mm of allocated Park Water debt at 8.385% per rate case filing
- For Mountain Water, defined as Net PP&E + Materials & Supplies + Utility Plant Acquisition Adjustment + 7% of O&M and Taxes Other Than Income - Portion of Deferred Income Taxes & ITC - Advances for Construction - Contributions in Aid of Construction; Modified Asset Base is used to approximate Rate Base
- For public and precedent comparables, defined as Net PP&E - Deferred Income Taxes & Investment Tax Credits - Advances for Construction - Contributions in Aid of Construction
- Range based on estimated purchase price of \$48.3-\$56.6mm, grown at 0.5% for 3 years
- Indicates the maximum amount of financing available to the City for an acquisition of Mountain Water based on the assumptions set out on page 16

How much did Carlyle pay?

- Carlyle purchased Park Water for \$156 million
 - Mountain Water, 23,300 customers in Missoula
 - Park Water, 28,800 customers in Los Angeles County, California
 - Apple Valley Ranchos, 21,500 customers in Apple Valley and Victorville, California

How much did Carlyle pay?

- Based on EBITDA per utility

2009 EBITDA BY UTILITY (\$mm)

	EBITDA	% of Total
Mountain Water	\$5.6	30.9%
Park Water	\$4.8	26.5%
Apple Valley Ranchos Water	\$7.7	42.5%
Total 2009 EBITDA	\$18.1	
Enterprise Value	156.0	
Implied EV / EBITDA	8.6x	
Implied Value for Mountain Water ²	\$48.3	
Adjusted for January 2014 ³	\$57.5	

How much did Carlyle pay?

- By Modified Asset Base per Utility

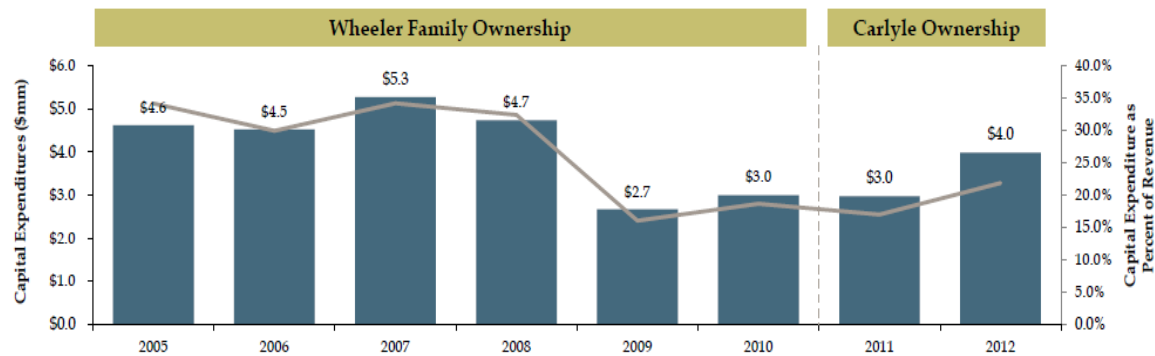
	Modified Asset	
	Base	% of Total
Mountain Water	\$36.4	36.3%
Park Water	\$28.7	28.6%
Apple Valley Ranchos Water	\$35.2	35.1%
Total 2009 Mod. Asset Base	\$100.4	
Enterprise Value	156.0	
Implied EV / Mod. Asset Base	1.6x	
Implied Value for Mountain Water ²	\$56.6	
Adjusted for January 2014 ³	\$67.4	

What has Carlyle done?

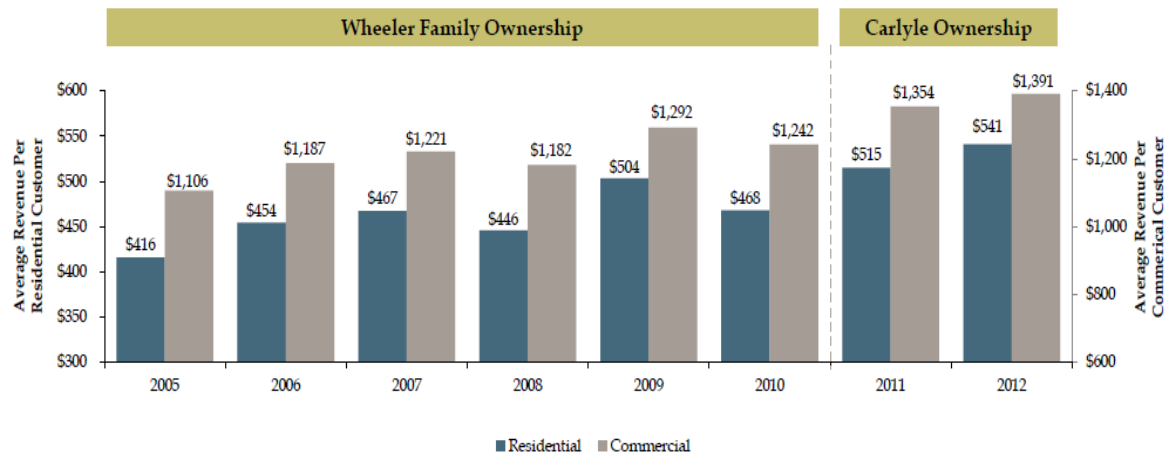
Mountain Water Historical Capital Expenditure and Rate Trends

MOELIS & COMPANY

MOUNTAIN WATER HISTORICAL CAPITAL EXPENDITURES¹



MOUNTAIN WATER HISTORICAL AVERAGE REVENUE PER CUSTOMER



Source: Mountain Water Annual Reports filed with PSC for years 2004 - 2012
 1. Calculated in each year as current year Utility Plant in Service less prior year Utility Plant in Service

What did we offer?

- \$65 million for a stock purchase of whole company, based on all valuation methods
- \$50 million for an asset purchase

How would we pay for the system?

- Our goal is to structure a debt program which provides a platform for the long-term financial viability of the Missoula Water Utility
 - Quality service = funding operations
 - Ongoing capital improvement investment
 - Minimizes user rate increases

How would we pay for the system?

- Revenue Bonds
 - Secured solely by revenues: Missoula Water Utility
 - User rates and other water system revenues
 - Property taxes and other City general revenues are not used to fund the bonds

How do we pay for the system?

- Water Utility Revenues
 - Assume Mountain Water Historical Revenues
 - Not reconfigured with public ownership, except taxes
 - No user rate changes necessary for acquisition
- Repayment Term
 - More years = more proceeds to diminishing point
- Interest Rate Market: currently low
- Credit Rating
 - Standard & Poor's: A to BBB (Strong Investment Grade)

How do we pay for the system?

- Five criteria influence credit rating
 - Customer/City Demographics & Economy
 - Utility Governance and Management
 - Utility Financial Condition
 - Debt Service Coverage:
 - $\text{Annual Net Revenues} / \text{Annual Debt Service}$
 - Cash for operations
 - Debt
 - Legal authority regarding governance and finance
 - Setting Rates, New Debt, etc

How do we pay for the system?

- Assumptions in structuring financing
 - Historical Non-Adjusted Revenues: \$6,800,000
 - Repayment Term: 30 years
 - Interest Rate Market: Current Low Market
 - Credit Rating and Interest Rates:
 - A Rating with 140 Debt Service Coverage: 5.50%
 - BBB Rating with 120 Debt Service Coverage: 6.25%

How do we pay for the system?

- Ability to Fund (net proceeds):
 - Up to \$65,000,000
- Working Capital (Cash for Operations): 45 Days
- Future Debt for Ongoing Capital Investment
 - \$4,000,000 per year

Issuing bonds to finance the system

Based upon the proposed finance plan and legal structure, the City is well-positioned to capitalize upon favorable market conditions to successfully issue bonds for the Water Utility acquisition and place its debt with investors

City of Missoula, Montana Water Utility System Revenue Bonds, 2014 (Proposed)

City of Missoula, Montana



Up to \$65 Million

Water Utility System
Revenue Bonds

Series 2014

Pending (2H 2014)

Security	▪ Net revenues of the new City Water Utility
Ongoing Debt Service Coverage Rate Covenant/Additional Bonds Test	▪ 140% of annual debt service
Reserve Fund	▪ 120% of annual debt service
Working Capital	▪ Fully funded debt service reserve fund at maximum annual debt service
Term	▪ 45 days of operating expenses
Tax Status	▪ 30 years
Ratings	▪ Tax-exempt
	▪ "A" category

Note: The proposed security features listed in the table above have been provided to Barclays by the City's financial advisors.

Comparable revenue bond financings

Several revenue bond financings with similar legal structures have successfully come to market, reinforcing the viability of the City's contemplated bond issuance

A1/A/A+ January 2014

City of Philadelphia



\$123,170,000

Water and Wastewater System
Revenue Refunding Bonds

Series 2014A

Debt Service Coverage: 1.20x

A2/AA-/NR December 2013

Pittsburgh Water and
Sewer Authority



\$216,910,000

Water and Sewer System First Lien
Revenue Bonds

Series 2013B

Debt Service Coverage: 1.81x

Ba1/A-/BB December 2013

Guam Waterworks Authority



\$172,630,000

Water and Wastewater System
Revenue Bonds

Series 2013

Debt Service Coverage: 2.03x

Note: Debt service coverage ratios reflect the last year for which audited financials were available.

Stock sale vs. asset sale

- City would prefer a stock sale, as indicated by informal offer. Buying the whole business, turn-key
- Asset sale is physical property as defined in offer, not a turn-key operation
- Whether negotiated sale, stock or asset purchase, financing fundamentals remain the same

Condemnation law and process

- Eminent domain
 - The right of the state and local government to take private property for public use.
 - Granted to original 13 states; now every state has this power.
 - Property must be taken for public use.

Condemnation law and process

- In 2001, eminent domain statutes changed to add reference to “water and water supply systems” as an express public use.
- Use must be a more necessary public use.
- Preponderance of the evidence that public interest requires the taking.
- **Preponderance of evidence means:** Evidence that is of greater weight or more convincing than the evidence that is offered in opposition to it. Evidence that as a whole shows that the fact sought to be proved is more probable than not.

Condemnation law and process

- The process
 1. Final written offer.
 2. If rejected:
 - (a) File complaint in District Court;
 - (b) Court required to give proceeding priority;
and
 - (c) Court issues preliminary condemnation order.
 - Within 30 days Park Water files claim for amount of compensation.
 - Within 20 days of service of claim City accepts or rejects amount.

Condemnation law and process

If City rejects claim, Court appoints condemnation commissioners.

- City and Park Water each nominate a condemnation commissioner, and the two nominated commissioners select a third commissioner.
- Role of the commissioners is to determine fair market value.
- Either party can appeal decision of commissioners to District Court.

Legal position

- What is the city's argument for public necessity?
- What is different today from the last try at condemnation?

Transaction costs

• Mergers & Acquisition Advisor	\$1,750,000
• M&A Counsel	250,000
• Acquisition & Bond Counsel	450,000
• Financial Advisor	350,000
• Condemnation Counsel	400,000
• Consulting Engineer	347,000
• Underwriting & Counsel	450,000
• User Rate Modeling	40,000
• Related Direct Costs	200,000
Total	\$4,237,000

Why is this so important?

- Clean, safe drinking water is critical to the health and welfare of all human beings.
- Management of that fundamental resource should not be the province of a private corporation beholden to distant investors
- I, and many other City of Missoula elected officials and citizens, strongly believe that a community's water system is a public asset that is best owned and operated by the public, through municipal government.

Why is this so important?

- City of Missoula would provide more accountability and accessibility to the public water system's board of directors.
- **Accountability:** Montana municipal utilities are required to provide mailed notice of any proposed rate increases to all persons served by the municipal utility. This is not required of private utilities in Montana.
- **Availability:** the board of directors will likely be the mayor and the Missoula City Council, who are directly elected by ratepayers, live in Missoula, and meet publicly nearly every week.

Why is this so important?

- A municipal utility does not operate to generate annual profits for its owners
- It operates for efficiency, service, and sustainability.
- Because there is no profit motive,
 - Municipal utilities typically cost less to operate and maintain.
 - There is little incentive for a municipality to consider sale, which further ensures stability and accountability for its customers.
 - There's a predisposition to a greater interest in water-conservation measures, including metered water and water-efficient fixtures and landscaping.

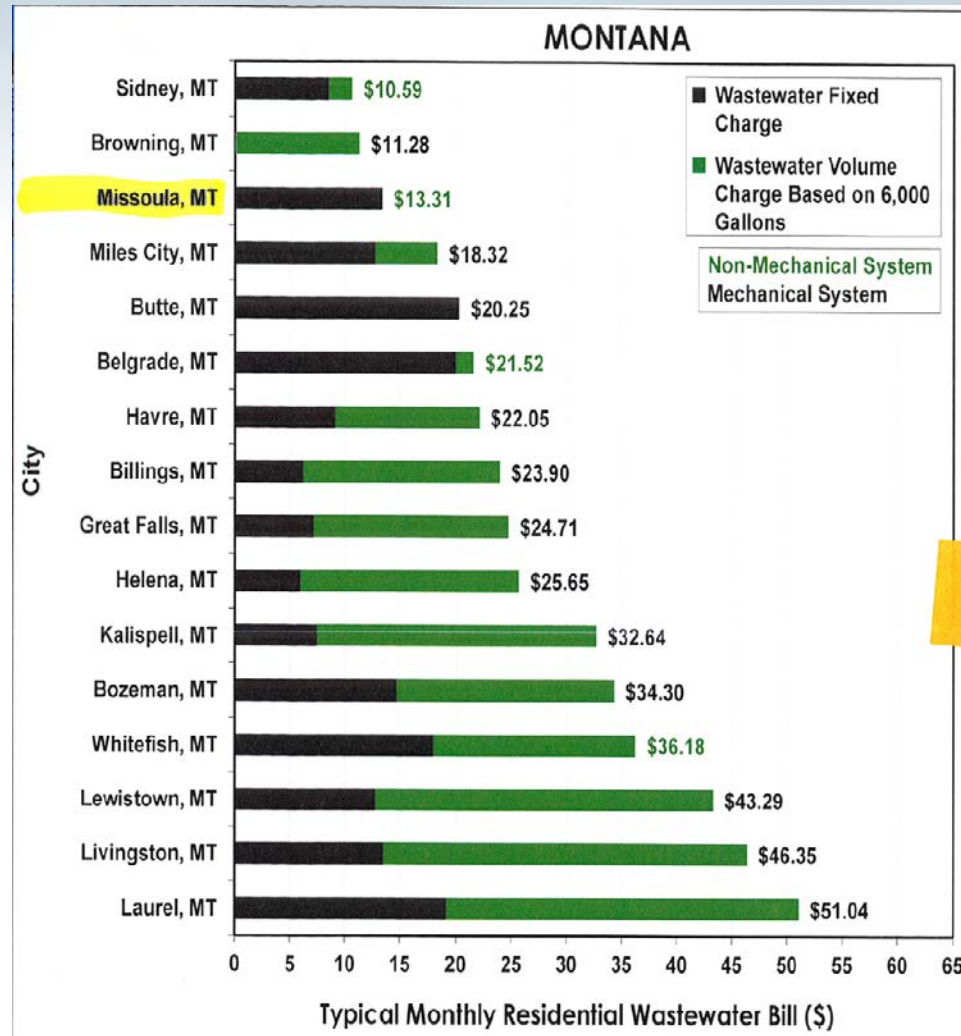
Why is this so important?

- The City of Missoula ceases to exist without a clean, reliable source of water and a reliable, effective distribution system.
- We have been previously content to have a family-owned company with roots and relationships serve as stewards of this fundamental utility.
- It is now owned by shareholders with no link to our community; nameless, faceless investors who are interested in making money, no matter the cost to the citizens.

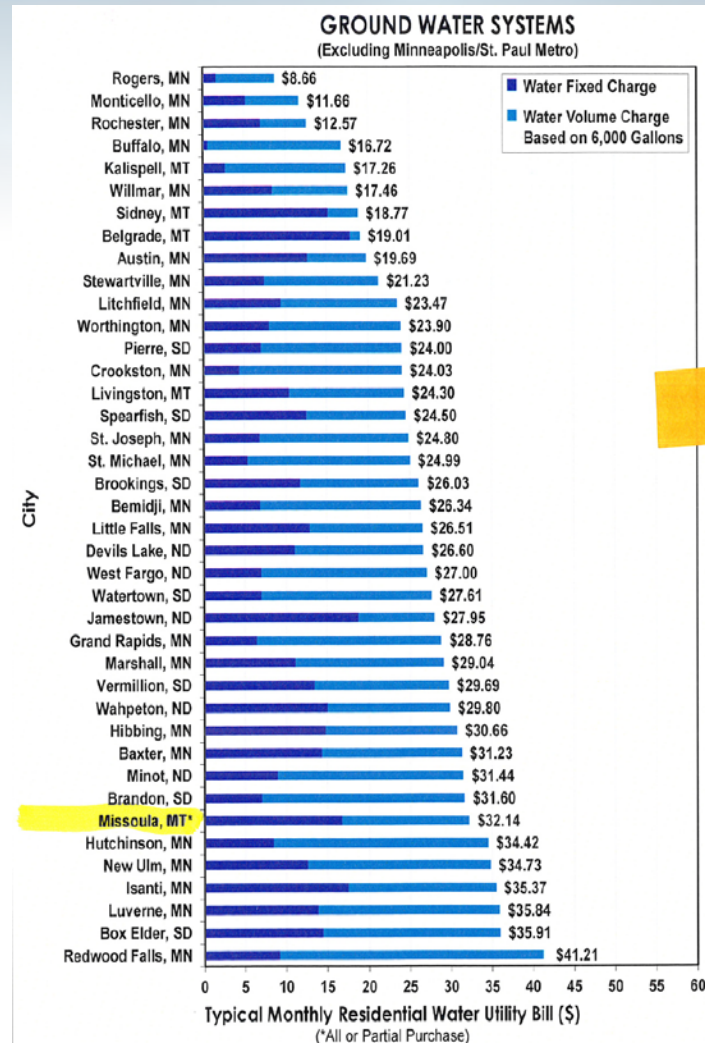
Why is this so important?

- Carlyle is not a long-term owner of the business and the City of Missoula is the best buyer and long-term owner. We have experience, resources, the right motives, direct accountability, long-term interest and vision and community support.
- We cannot allow water to become a commodity.
- We should not be the only water utility in the state's major cities in private hands.

Comparisons: Wastewater

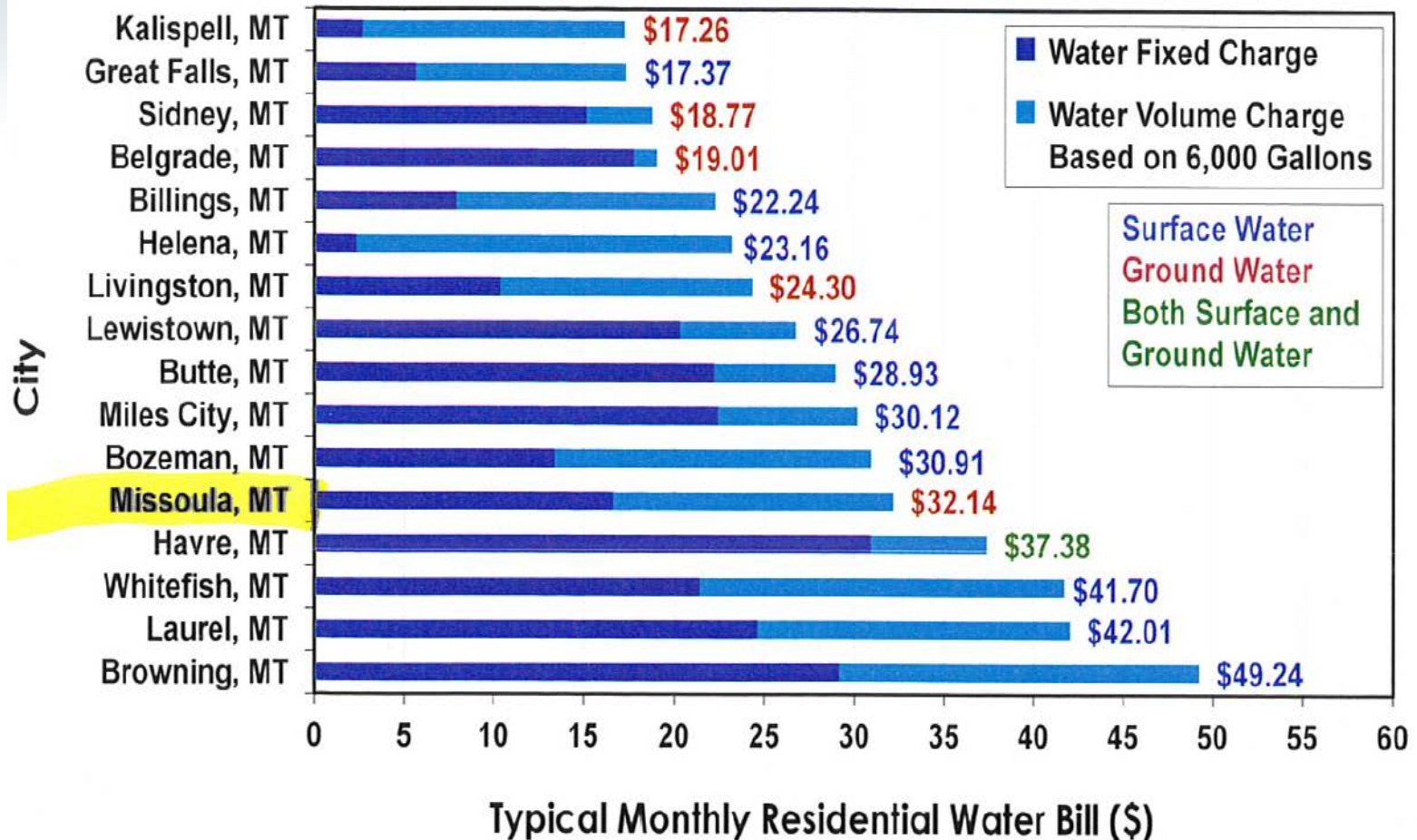


Comparisons: Water



Comparisons: Water

MONTANA



Questions

Questions and comments?