

OFFICIAL STATEMENT

BANNING UTILITY AUTHORITY

| | | |
|--|------------|--|
| \$35,635,000 | | \$7,100,000 |
| Water Enterprise Revenue Bonds | and | Wastewater Enterprise Revenue Bonds |
| Refunding and Improvement Projects, 2005 Series | | Refunding and Improvement Projects, 2005 Series |

INTRODUCTION

This Official Statement of the Banning Utility Authority (the "Authority") sets forth certain information in connection with the sale by the Authority of its Water Enterprise Revenue Bonds, Refunding and Improvement Projects, 2005 Series (the "Water Bonds") and its Wastewater Enterprise Revenue Bonds, Refunding and Improvement Projects, 2005 Series (the "Wastewater Bonds" and together with the Water Bonds, the "Bonds"). This Introduction is not a summary of this Official Statement. It is only a brief description of and guide to, and is qualified by, more complete and detailed information contained in the entire Official Statement, including the appendices hereto, and the documents summarized or described herein. A full review should be made of the entire Official Statement. The offering of Bonds to potential investors is made only by means of the entire Official Statement. The capitalization of any word not conventionally capitalized or otherwise defined herein indicates that such word is defined in a particular agreement or other document and, as used herein, has the meaning given it in such agreement or document. See "APPENDIX C – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS" for a summary of certain of such definitions.

The Bonds

The Bonds are being issued pursuant to the Constitution and the laws of the State of California (the "State"), including the Marks-Roos Local Bond Pooling Act of 1985, constituting Article 4 of Chapter 5 of Division 7 of Title 1 (commencing with Section 6584) of the California Government Code, as amended (the "Bond Law"), and, as to the Water Bonds, pursuant to an Indenture of Trust, dated as of December 1, 2005 (the "Water Indenture"), by and between the Authority and U.S. Bank National Association, as trustee (the "Trustee"), and, as to the Wastewater Bonds, pursuant to an Indenture of Trust, dated as of December 1, 2005 (the "Wastewater Indenture" and, together with the Water Indenture, the "Indentures", and, each, an "Indenture", as applicable), by and between the Authority and the Trustee.

The Bonds are special obligations of the Authority, and are payable from, and are secured by a charge and lien on, Net Water Revenues or Net Wastewater Revenues, as applicable, and from amounts held from time to time in the funds and accounts established under the respective Indenture. See "SECURITY FOR THE BONDS" and "BONDOWNERS' RISKS."

Use of Proceeds

Proceeds of the Water Bonds will be used to (i) pay costs of certain capital improvements to the Water Enterprise; (ii) defease the 1986 Certificates (as defined herein), currently outstanding in the aggregate principal amount of \$2,475,000; (iii) defease the 1989 Water Certificates (as defined herein), currently outstanding in the aggregate principal amount of \$1,890,000; (iv) make an initial up-front lease payment to the City, which will be used to pay costs of certain capital improvements of City public facilities; (v) pay the insurance premium for the Water Bonds; (vi) purchase a reserve surety for the Water Bonds; and (vii) pay costs of issuance of the Water Bonds. Proceeds of the Wastewater Bonds will be used to (i) pay costs of certain capital improvements to the Wastewater Enterprise; (ii) defease the 1989 Wastewater Certificates (as defined herein), currently outstanding in the aggregate principal amount of \$1,895,000; (iii) pay the insurance premium for the Wastewater Bonds; (iv) purchase a reserve surety for

the Wastewater Bonds; and (v) pay costs of issuance of the Wastewater Bonds. See "PLAN OF FINANCE" and "ESTIMATED SOURCES AND USES OF FUNDS."

The Enterprises

Simultaneously with the delivery of the Bonds, the Authority will lease from the City the: (i) water system and facilities appurtenant (the "Water Enterprise"), pursuant to that certain Water Enterprise Lease Agreement, dated as of December 1, 2005 (the "Water Lease"); and (ii) wastewater system and facilities appurtenant (the "Wastewater Enterprise"), pursuant to that certain Wastewater Enterprise Lease Agreement, dated as of December 1, 2005 (the "Wastewater Lease"). See "THE WATER ENTERPRISE" and "THE WASTEWATER ENTERPRISE" herein.

Pursuant to the Water Enterprise Management Agreement, dated as of December 1, 2005 (the "Water Management Agreement"), the City will continue to operate and maintain the Water Enterprise on behalf of the Authority. In addition, pursuant to the Wastewater Enterprise Management Agreement, dated as of December 1, 2005 (the "Wastewater Management Agreement"), the City will continue to operate and maintain the Wastewater Enterprise on behalf of the Authority.

Further Information

Brief descriptions of the Bonds, the Water Indenture, the Wastewater Indenture, the Water Lease, the Wastewater Lease, the Bond Law, the Authority, the City, the Water Enterprise and the Wastewater Enterprise are included in this Official Statement. Such information does not purport to be comprehensive or definitive. All references herein to the Water Indenture, the Wastewater Indenture, the Water Lease, the Wastewater Lease, the Bond Law, the Constitution and the laws of the State, and the proceedings of the Authority and the City, are qualified in their entirety by reference to each such document, statute, constitution or proceedings. References herein to the Bonds are qualified in their entirety by reference to the form thereof included in the applicable Indenture. Copies of the Water Indenture, the Wastewater Indenture, the Water Lease and the Wastewater Lease are available for inspection at the office of the Authority.

THE AUTHORITY

The Authority is a joint powers agency organized and existing under and by virtue of Articles 1 through 4 of Chapter 5 of Division 7 of Title 1 (commencing with Section 6500) of the California Government Code, as amended. The City and the Community Redevelopment Agency of the City of Banning (the "Agency") entered into a Joint Exercise of Powers Agreement dated as of July 12, 2005 to establish the Authority. The Authority is governed by a Board of five Members comprised of the same individuals who comprise the City Council of the City. The Authority was created for the purpose, among other things, of providing financing relating to any Water or Wastewater utility system or service through the lease, acquisition or construction by the Authority of such public capital improvements. Under the Bond Law, the Authority has the power to issue bonds to pay the costs of public capital improvements.

THE BONDS

General

The Bonds will be issued in fully registered form without coupons in Authorized Denominations. The Bonds will initially be registered in the name of Cede & Co., as nominee of The Depository Trust Company of New York, New York ("DTC"), and will be evidenced by one Bond for each of the maturities in the principal amounts shown on the inside cover page of this Official Statement. DTC is the

depository for the Bonds, and registered ownership may not thereafter be transferred except as set forth in the Indenture. The Bonds will mature on November 1 in the years and in the amounts shown on the inside cover page of this Official Statement and will bear interest on each Interest Payment Date at the rates shown on the inside cover of this Official Statement.

Interest on the Bonds will be payable semi-annually on each May 1 and November 1, calculated based on a 360-day year of twelve (12) thirty-day months on each Interest Payment Date, commencing on May 1, 2006, to the person whose name appears on the registration books of the Trustee as the Owner thereof as of the Record Date immediately preceding each such Interest Payment Date, such interest to be paid by check of the Trustee mailed by first class mail to the Owner at the address of such Owner as it appears on the registration books; provided, however, that payment of interest or principal may be by wire transfer in immediately available funds to an account in the United States of America to any Owner of Bonds in the aggregate principal amount of \$1,000,000 or more who shall furnish written wire instructions to the Trustee prior to the applicable Record Date. Principal of any Bond will be paid by check or wire of the Trustee upon presentation and surrender thereof at the Trust Office. Principal of and interest on the Bonds will be payable in lawful money of the United States of America.

Each Bond will be dated as of the Delivery Date and will bear interest from the Interest Payment Date next preceding the date of authentication thereof, unless (a) it is authenticated after a Record Date and on or before the following Interest Payment Date, in which event it shall bear interest from such Interest Payment Date, or (b) unless it is authenticated on or before April 15, 2006, in which event it shall bear interest from the Closing Date; provided, however, that if, as of the date of authentication of any Bond, interest thereon is in default, such Bond will bear interest from the Interest Payment Date to which interest has previously been paid or made available for payment thereon.

Optional Redemption

Water Bonds. The Water Bonds maturing on or after November 1, 2017 shall be subject to optional redemption, as a whole or in part on any date prior to the maturity thereof, at the option of the Authority, on or after November 1, 2016, from funds derived by the Authority from any source, at the redemption price equal to the principal amount of the Water Bonds to be redeemed together with accrued but unpaid interest to the redemption date, without premium.

Wastewater Bonds. The Wastewater Bonds maturing on or after November 1, 2017 shall be subject to optional redemption, as a whole or in part on any date prior to the maturity thereof, at the option of the Authority, on or after November 1, 2016, from funds derived by the Authority from any source, at the redemption price equal to the principal amount of the Wastewater Bonds to be redeemed together with accrued but unpaid interest to the redemption date, without premium.

Mandatory Sinking Fund Redemption

Water Bonds. The Water Bonds that are Term Bonds (the "Water Term Bonds") maturing on November 1, 2030, and November 1, 2035 are subject to mandatory redemption, in part by lot, from Sinking Account payments set forth in the following schedules on November 1, in each year, commencing November 1, 2024, and November 1, 2031, respectively, at a redemption price equal to the principal amount thereof to be redeemed (without premium), together with interest accrued thereon to the date fixed for redemption; provided, however, that if some but not all of the Water Term Bonds have been redeemed pursuant to the Water Indenture, the total amount of Sinking Account payments to be made subsequent to such redemption shall be reduced in an amount equal to the principal amount of the Water Term Bonds so redeemed by reducing each such future Sinking Account payment on a pro rata basis (as nearly as practicable) in integral multiples of \$5,000, as shall be designated pursuant to written notice filed by the Authority with the Trustee.

Schedule of Mandatory Sinking Fund Payments
Water Term Bond Maturing November 1, 2030

| Redemption Date (November 1) | Principal Amount |
|---------------------------------|---------------------|
| 2024 | \$1,250,000 |
| 2025 | 1,315,000 |
| 2026 | 1,385,000 |
| 2027 | 1,455,000 |
| 2028 | 1,535,000 |
| 2029 | 1,615,000 |
| 2030 (maturity) | 1,700,000 |

Schedule of Mandatory Sinking Fund Payments
Water Term Bond Maturing November 1, 2035

| Redemption Date (November 1) | Principal Amount |
|---------------------------------|---------------------|
| 2031 | \$1,785,000 |
| 2032 | 1,880,000 |
| 2033 | 1,980,000 |
| 2034 | 2,085,000 |
| 2035 (maturity) | 2,195,000 |

In lieu of such redemption, the Trustee may apply amounts in the Sinking Account to the purchase of Water Term Bonds at public or private sale, as and when and at such prices (including brokerage and other charges, but excluding accrued interest, which is payable from the Interest Account) as may be directed by the Authority, except that the purchase price (exclusive of accrued interest) may not exceed the redemption price then applicable to the Water Term Bonds, as set forth in a Written Request of the Authority. The par amount of Water Term Bonds so purchased by the Authority in any twelve month period immediately preceding any mandatory Sinking Account payment date in the table above will be credited towards and will reduce the principal amount of Water Term Bonds required to be redeemed on the succeeding Principal Payment Date.

Wastewater Bonds. The Wastewater Bonds that are Term Bonds (the "Wastewater Term Bonds") maturing on November 1, 2025, and November 1, 2035 are subject to mandatory redemption, in part by lot, from Sinking Account payments set forth in the following schedules on November 1, in each year, commencing November 1, 2023, and November 1, 2026, respectively, at a redemption price equal to the principal amount thereof to be redeemed (without premium), together with interest accrued thereon to the date fixed for redemption; provided, however, that if some but not all of the Wastewater Term Bonds have been redeemed pursuant to the Wastewater Indenture, the total amount of Sinking Account payments to be made subsequent to such redemption shall be reduced in an amount equal to the principal amount of the Wastewater Term Bonds so redeemed by reducing each such future Sinking Account payment on a pro rata basis (as nearly as practicable) in integral multiples of \$5,000, as shall be designated pursuant to written notice filed by the Authority with the Trustee.

Schedule of Mandatory Sinking Fund Payments
Wastewater Term Bond Maturing November 1, 2025

| Redemption Date (November 1) | Principal Amount |
|---------------------------------|---------------------|
| 2023 | \$220,000 |
| 2024 | 230,000 |
| 2025 (maturity) | 240,000 |

Schedule of Mandatory Sinking Fund Payments
Wastewater Term Bond Maturing November 1, 2035

| Redemption Date (November 1) | Principal Amount |
|---------------------------------|---------------------|
| 2026 | \$250,000 |
| 2027 | 265,000 |
| 2028 | 275,000 |
| 2029 | 290,000 |
| 2030 | 300,000 |
| 2031 | 315,000 |
| 2032 | 330,000 |
| 2033 | 345,000 |
| 2034 | 360,000 |
| 2035 (maturity) | 375,000 |

In lieu of such redemption, the Trustee may apply amounts in the Sinking Account to the purchase of Wastewater Term Bonds at public or private sale, as and when and at such prices (including brokerage and other charges, but excluding accrued interest, which is payable from the Interest Account) as may be directed by the Authority, except that the purchase price (exclusive of accrued interest) may not exceed the redemption price then applicable to the Wastewater Term Bonds, as set forth in a Written Request of the Authority. The par amount of Wastewater Term Bonds so purchased by the Authority in any twelve month period immediately preceding any mandatory Sinking Account payment date in the table above will be credited towards and will reduce the principal amount of Wastewater Term Bonds required to be redeemed on the succeeding Principal Payment Date.

Special Mandatory Redemption From Insurance or Condemnation Proceeds

The Bonds shall also be subject to redemption as a whole or in part on any date, pro rata by maturity and by lot within a maturity (in a manner determined by the Trustee) from moneys deposited in the applicable Redemption Fund to the extent insurance proceeds received with respect to the Water Enterprise or the Wastewater Enterprise, as applicable, are not used to repair, rebuild or replace the applicable Enterprise pursuant to the applicable Indenture, or to the extent of condemnation proceeds received with respect to the applicable Enterprise and elected by the Authority to be used for such purpose pursuant to applicable Indenture, or to the extent excess funds remain upon abandonment or completion of improvements to the Water Enterprise or the Wastewater Enterprise pursuant to the applicable Indenture, at a redemption price equal to the principal amount thereof plus interest accrued thereon to the date fixed for redemption.

Notice of Redemption

When redemption is authorized or required, pursuant to the applicable Indenture, the Trustee is required to give written notice of the redemption of Bonds to the Owners of Bonds designated for redemption at their addresses appearing on the bond registration books, to certain Securities Depositories, and to one or more Information Services, all as provided in the applicable Indenture, by first class mail, postage prepaid, no less than thirty (30) nor more than sixty (60) days prior to the date fixed for redemption. Neither failure to receive such notice nor any defect in the notice so mailed will affect the sufficiency of the proceedings for redemption of such Bonds or the cessation of accrual of interest on the redemption date.

Selection of Bonds for Redemption

Whenever provision is made in either Indenture for the redemption of less than all of the Bonds secured thereunder, the Trustee shall select the Bonds to be redeemed from all Bonds or such given portion thereof not previously called for redemption, pro rata by maturity or, at the election of the Authority set forth in a Written Request of the Authority, filed with the Trustee, from such maturities as the Authority shall determine, and by lot within a maturity in any manner which the Trustee in its sole discretion shall deem appropriate and fair. Any such determination shall be deemed conclusive. For purposes of such selection, the Trustee shall treat each Bond as consisting of separate \$5,000 portions and each such portion shall be subject to redemption as if such portion were a separate Bond.

Effect of Redemption

Once notice of redemption has been duly given as described above, and moneys for payment of the redemption price of, together with interest accrued to the date fixed for redemption on, the Bonds (or portions thereof) so called for redemption are held by the Trustee, on the redemption date designated in such notice, the Bonds (or portions thereof) so called for redemption shall become due and payable, interest on the Bonds so called for redemption shall cease to accrue, said Bonds (or portions thereof) shall cease to be entitled to any benefit or security under the Indenture, and the Owners of said Bonds shall have no rights in respect thereof except to receive payment of the redemption price thereof.

All Bonds redeemed pursuant to the provisions of either the Water Indenture or the Wastewater Indenture, as applicable, shall be canceled by the Trustee upon surrender thereof and destroyed.

Book-Entry Only System

DTC will act as securities depository for the Bonds. The Bonds will be issued as fully-registered bonds registered in the name of Cede & Co. (DTC's partnership nominee). One fully-registered Bond will be issued for each maturity of the Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC. Ultimate purchasers of Bonds will not receive physical certificates representing their interest in the Bonds. Payment of the principal of and interest on the Bonds will be made directly to DTC, or its nominee, Cede & Co., by the Trustee so long as DTC or Cede & Co. is the registered owner of the Bonds. Disbursement of such payments to DTC's Participants is the responsibility of DTC and disbursement of such payments to the Beneficial Owners is the responsibility of DTC's Participants and Indirect Participants. See "APPENDIX E - BOOK-ENTRY ONLY SYSTEM."

PLAN OF FINANCE

Water Bonds

On or after the Closing Date, the proceeds from the sale of the Water Bonds will be applied as follows:

(i) *Water Project Fund.* A portion of the proceeds of the Water Bonds will be deposited into the Water Project Fund for use as follows:

- a. In connection with the Water CIP described herein, or other capital projects of the Water Enterprise;
- b. The amount of \$17,000,000 will be transferred as an initial up-front lease payment to the City under the Water Lease. Said amount will be used to finance certain public capital improvements including, but not limited to the following: (A) construction of a new two-story police facility anticipated to consist of approximately 41,306 square feet of space and 53 secure parking spaces; (B) completion of a public swimming pool anticipated to have a bather capacity of 254 people to be located within Repplier Park and to be owned and operated by the City; (C) construction of a one-stop permitting center consisting of the rehabilitation and retrofit of an existing City-owned structure to construct new office space and meeting rooms to house the City's development related functions; (D) construction of a concrete, open air, lighted public skating park with a skating surface anticipated to be approximately 10,000 square feet which is to be owned by the City; and (E) upgrading and replacement of certain air conditioning units at City Hall;

(ii) *Defeasance of 1986 Certificates.* A portion of the proceeds of the Water Bonds in the amount of \$2,189,246.50 will be used, together with funds currently held by the 1986 Trustee (as defined below), to defease the City's installment payment obligations relating to the City's \$4,055,000 Certificates of Participation (Water System Improvement Project) currently outstanding in the aggregate principal amount of \$2,475,000 (the "1986 Certificates"). The Authority will direct U.S. Bank National Association, in its capacity as trustee for the 1986 Certificates (the "1986 Trustee") to establish an Escrow Fund (the "1986 Certificates Escrow Fund") to be held by the 1986 Trustee in trust as an irrevocable escrow securing the payment of the 1986 Certificates and the City's obligations with respect thereto. Amounts on deposit in the 1986 Certificates Escrow Fund will be used to purchase certain governmental obligations, the principal of and interest on which, together with amounts held as cash in the 1986 Certificates Escrow Fund, if any, will be sufficient to prepay the outstanding 1986 Certificates on May 1, 2006 at a prepayment price of 100% of the purchase amount represented thereby plus interest accrued with respect thereto, without premium. Upon such deposit, the 1986 Certificates will no longer be deemed to be outstanding and the City's obligation to make installment payments under that certain Installment Sale Agreement dated as of November 1, 1986, and relating to the 1986 Certificates, will be discharged. All cash and governmental obligations in the Escrow Fund will be irrevocably pledged as a special fund for the payment of the principal and interest represented by the 1986 Certificates in accordance with the documents under which the 1986 Certificates were delivered. The sufficiency of the deposits and investment earnings for those purposes will be verified by a verification agent to be selected by the Authority. See "VERIFICATION OF MATHEMATICAL COMPUTATIONS" below.

(iii) *Defeasance of 1989 Water Certificates.* A portion of the proceeds of the Water Bonds in the amount of \$1,989,364.91 will be used, together with funds currently held by the 1989 Trustee (as defined below), to defease the City's installment payment obligations relating to the City's \$2,585,000 Certificates of Participation (Water System Improvement Project) currently outstanding in the aggregate principal amount of \$1,890,000 (the "1989 Water Certificates"). The Authority will direct U.S. Bank

National Association, in its capacity as trustee for the 1989 Wastewater Certificates and the 1989 Water Certificates (the "1989 Trustee") to establish an Escrow Fund (the "1989 Water Certificates Escrow Fund") to be held by the 1989 Trustee in trust as an irrevocable escrow securing the payment of the 1989 Water Certificates and the City's obligations with respect thereto. Amounts on deposit in the 1989 Water Certificates Escrow Fund will be used to purchase certain governmental obligations, the principal of and interest on which, together with amounts held as cash in the 1989 Water Certificates Escrow Fund, if any, will be sufficient to pay the principal and interest on the 1989 Water Certificates as it becomes due. Upon such deposit, the 1989 Water Certificates will no longer be deemed to be outstanding and the City's obligation to make installment payments under that certain Installment Sale Agreement dated as of November 1, 1989, and relating to the 1989 Water Certificates, will be discharged. All cash and governmental obligations in the Escrow Fund will be irrevocably pledged as a special fund for the payment of the principal and interest represented by the 1989 Water Certificates in accordance with the documents under which the 1989 Water Certificates were delivered. The sufficiency of the deposits and investment earnings for those purposes will be verified by a verification agent to be selected by the Authority. See "VERIFICATION OF MATHEMATICAL COMPUTATIONS" below.

(iv) *Water Reserve Fund.* A portion of the proceeds of the Water Bonds will be used to purchase a reserve surety for the Water Bonds, as provided under the Water Indenture.

(v) *Water Cost of Issuance Fund.* A portion of the proceeds of the Water Bonds will be used to fund the cost of issuance fund for the Water Bonds.

Wastewater Bonds

On or after the Closing Date, the proceeds from the sale of the Wastewater Bonds will be applied as follows:

(i) *Wastewater Project Fund.* A portion of the proceeds will be deposited into the Wastewater Project Fund for use in connection with the Wastewater Capital Improvement projects described herein.

(ii) *Defeasance of 1989 Wastewater Certificates.* A portion of the proceeds of the Wastewater Bonds in the amount of \$1,664,172.10 will be used, together with funds currently held by the 1989 Trustee, to defease the City's installment payment obligations relating to the City's \$3,740,000 Certificates of Participation (Wastewater System Refunding and Improvement Project), Series 1989, currently outstanding in the aggregate principal amount of \$1,895,000 (the "1989 Wastewater Certificates"). The Authority will direct the 1989 Trustee to establish an Escrow Fund (the "1989 Wastewater Certificates Escrow Fund") to be held by the 1989 Trustee in trust as an irrevocable escrow securing the payment of the 1989 Certificates and the City's obligations with respect thereto. Amounts on deposit in the 1989 Wastewater Certificates Escrow Fund will be used to purchase certain governmental obligations, the principal of and interest on which, together with amounts held as cash in the 1989 Wastewater Certificates Escrow Fund, if any, will be sufficient to pay the principal and interest on the 1989 Wastewater Certificates as it becomes due. Upon such deposit, the 1989 Wastewater Certificates will no longer be deemed to be outstanding and the City's obligation to make installment payments under that certain Installment Sale Agreement dated as of November 1, 1989, and relating to the 1989 Wastewater Certificates, will be discharged. All cash and governmental obligations in the Escrow Fund will be irrevocably pledged as a special fund for the payment of the principal and interest represented by the 1989 Wastewater Certificates in accordance with the documents under which the 1989 Wastewater Certificates were delivered. The sufficiency of the deposits and investment earnings for those purposes will be verified by a verification agent to be selected by the Authority. See "VERIFICATION OF MATHEMATICAL COMPUTATIONS" below.

(iii) *Wastewater Reserve Fund.* A portion of the proceeds of the Wastewater Bonds will be used to purchase a reserve surety for the Wastewater Bonds, as provided under the Wastewater Indenture.

(iv) *Wastewater Cost of Issuance Fund.* A portion of the proceeds of the Wastewater Bonds will be used to fund the cost of issuance fund for the Wastewater Bonds.

CAPITAL IMPROVEMENT PROJECTS

The following paragraphs discuss and describe the anticipated uses of Bond proceeds for capital improvement projects and provide some information concerning the additional capital needs of the Water Enterprise and the Wastewater Enterprise.

Water Capital Improvement Program

The City has developed a comprehensive Capital Improvement Program for the Water Enterprise (the "Water CIP"). The Water CIP is intended to address current and future needs of the Water Enterprise. The Water CIP projects anticipated to be funded with proceeds of the Water Bonds are included in the following table.

WATER ENTERPRISE CIP PROJECTS

| Construction Project | Estimated Costs to be Paid from Bond Proceeds |
|--|--|
| Construction of the Brinton Reservoir (8.0 MG) | \$5,000,000 |
| Construction of Three Major Water Transmission Lines | 7,000,000 |
| Replacement of 20" Transmission Line in Banning Canyon | 3,000,000 |

In addition to the Water CIP projects listed above, the Water CIP project list includes the following projects for which most of the funding sources have been identified and which the City plans to complete in the next 5 to 8 years:

1. Construction of two water wells in the Beaumont Basin. The City has entered into an agreement with the Beaumont Cherry Valley Water District to construct two new water wells jointly within the Beaumont groundwater sub-basin. Each entity will be responsible for 50% of the cost. The wells are anticipated to produce 3,000 gallons per minute per well. Construction of this project is already in progress and the City has already contributed a large portion of its share of the estimated \$6,000,000 of costs for the project. It is anticipated that the additional cost of constructing this project, currently estimated in the amount of \$1,920,000, will be funded from reserves of the Water Enterprise;
2. Construction of two additional wells. In addition to the wells described above, the Authority plans to construct two additional wells within the eastern boundary of the City solely for the Authority's use. These two wells are needed to provide relief of over draft of the Beaumont sub-basin and to accommodate future development. The Water Enterprise has reserves of approximately \$3,075,000, but may need an additional \$1,525,000, to fund this project;
3. Construction of an Irrigation Water System. The Irrigation Water System would consist of the installation of 5.3 miles of 16" transmission pipeline from the Wastewater Treatment Plant (WWTP) and the R-1 well site to the intersection of Highland Home Road and Sun Lakes Blvd,

four pump stations, and one storage tank. Once the tertiary facilities are installed at the WWTP, recycled water will supplement irrigation water utilizing the proposed irrigation system.

The Water CIP also includes some projects which the Authority plans to complete as soon as funding becomes available. Such projects include the construction of another eight million gallon (8.0 MG) reservoir, surface water run-off recharge facilities and the construction of a third well within the Beaumont Basin pursuant to the City's agreement with the Beaumont Cherry Valley Water District.

Wastewater Capital Improvement Program

The City has developed a comprehensive Capital Improvement Program for the Wastewater Enterprise (the "Wastewater CIP"). The Wastewater CIP is intended to address current and future needs of the Wastewater Enterprise. The Wastewater CIP project anticipated to be funded with proceeds of the Wastewater Bonds is included in the following table.

WASTEWATER ENTERPRISE CIP PROJECT

| Construction Project | Estimated Costs to be Paid from Bond Proceeds |
|----------------------------------|--|
| 1.5 MGD Tertiary Treatment Plant | \$5,000,000 |

The estimated cost of the tertiary treatment plant identified above is \$9,000,000. It is anticipated that the additional \$4,000,000 required for this project will be funded from undesignated reserves of the Wastewater Enterprise. The Authority plans to expand the tertiary treatment facilities in phases to accommodate the future needs for recycled water. The project identified above is the first phase expansion required to accommodate planned development within the City.

One other project the Authority anticipates funding from reserves of the Wastewater Enterprise is the construction of a sewer trunk line to be known as the Deutsch Sewer Trunk Line. This line will be needed to serve several proposed developments in the north and west areas of the City. The estimated cost of this project is \$4,000,000.

ESTIMATED SOURCES AND USES OF FUNDS

The following tables set forth the estimated sources and uses of funds related to the issuance of the Bonds.

SOURCES AND USES – WATER BONDS

SOURCES:

| | |
|---|------------------------|
| Principal Amount of Water Bonds | \$35,635,000.00 |
| Less Underwriter's Discount | (391,985.00) |
| Net Original Issue Premium | 1,516,074.15 |
| 1986 Certificates Reserve Fund | 335,065.00 |
| 1989 Water Certificates Debt Service Fund | 155,600.00 |
| 1989 Water Certificates Reserve Fund | <u>233,027.00</u> |
| Total Sources | \$37,482,781.15 |

USES:

| | |
|--|------------------------|
| Deposit to Costs of Issuance Fund ⁽¹⁾ | \$ 580,477.74 |
| Deposit to Escrow Fund for 1986 Certificates | 2,524,311.50 |
| Deposit to Escrow Fund for 1989 Water Certificates | 2,377,991.91 |
| Deposit to Water Project Fund ⁽²⁾ | <u>32,000,000.00</u> |
| Total Uses | \$37,482,781.15 |

⁽¹⁾ Costs of issuance include fees and expenses of the Financial Advisor, Bond Counsel, Disclosure Counsel, the Trustee, Trustee's counsel, bond insurance premium, surety bond premium, printing expenses and other costs of issuing the Water Bonds.

⁽²⁾ A portion of the amounts deposited to the Water Project Fund will be used to make an initial up-front lease payment to the City in the amount of \$17,000,000, which will be used to pay costs of certain capital improvements of City public facilities.

SOURCES AND USES - WASTEWATER BONDS

SOURCES:

| | |
|--|-----------------------|
| Principal Amount of Wastewater Bonds | \$7,100,000.00 |
| Less Underwriter's Discount | (78,100.00) |
| Original Issue Discount | (126,492.25) |
| 1989 Wastewater Certificates Debt Service Fund | 270,800.00 |
| 1989 Wastewater Certificates Reserve Fund | <u>317,462.00</u> |
| Total Sources | \$7,483,669.75 |

USES:

| | |
|---|-----------------------|
| Deposit to Wastewater Costs of Issuance Fund ⁽¹⁾ | \$ 231,235.65 |
| Deposit to Escrow Fund for 1989 Wastewater Certificates | 2,252,434.10 |
| Deposit to Wastewater Project Fund | <u>5,000,000.00</u> |
| Total Uses | \$7,483,669.75 |

⁽¹⁾ Costs of issuance include fees and expenses of the Financial Advisor, Bond Counsel, Disclosure Counsel, the Trustee, Trustee's counsel, bond insurance premium, surety bond premium, printing expenses and other costs of issuing the Wastewater Bonds.

BOND DEBT SERVICE

The following table sets forth the annual debt service schedule for the Water Bonds.

| <u>Bond Year Ending</u> | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|-------------------------|------------------|-----------------|----------------|
| 2006 | \$ 830,000 | \$1,478,086.46 | \$2,308,086.46 |
| 2007 | 620,000 | 1,689,512.50 | 2,309,512.50 |
| 2008 | 640,000 | 1,667,812.50 | 2,307,812.50 |
| 2009 | 665,000 | 1,645,412.50 | 2,310,412.50 |
| 2010 | 685,000 | 1,622,137.50 | 2,307,137.50 |
| 2011 | 715,000 | 1,594,737.50 | 2,309,737.50 |
| 2012 | 740,000 | 1,566,137.50 | 2,306,137.50 |
| 2013 | 770,000 | 1,536,537.50 | 2,306,537.50 |
| 2014 | 805,000 | 1,505,737.50 | 2,310,737.50 |
| 2015 | 840,000 | 1,469,512.50 | 2,309,512.50 |
| 2016 | 875,000 | 1,433,837.50 | 2,308,837.50 |
| 2017 | 910,000 | 1,398,837.50 | 2,308,837.50 |
| 2018 | 945,000 | 1,362,437.50 | 2,307,437.50 |
| 2019 | 985,000 | 1,323,456.26 | 2,308,456.26 |
| 2020 | 1,025,000 | 1,280,950.00 | 2,305,950.00 |
| 2021 | 1,080,000 | 1,229,700.00 | 2,309,700.00 |
| 2022 | 1,135,000 | 1,175,700.00 | 2,310,710.00 |
| 2023 | 1,190,000 | 1,118,950.00 | 2,308,950.00 |
| 2024 | 1,250,000 | 1,059,450.00 | 2,309,450.00 |
| 2025 | 1,315,000 | 993,825.00 | 2,308,825.00 |
| 2026 | 1,385,000 | 924,787.50 | 2,309,787.50 |
| 2027 | 1,455,000 | 852,075.00 | 2,307,075.00 |
| 2028 | 1,535,000 | 775,687.50 | 2,310,687.50 |
| 2029 | 1,615,000 | 695,100.00 | 2,310,100.00 |
| 2030 | 1,700,000 | 610,312.50 | 2,310,312.50 |
| 2031 | 1,785,000 | 521,062.50 | 2,306,062.50 |
| 2032 | 1,880,000 | 427,350.00 | 2,307,350.00 |
| 2033 | 1,980,000 | 328,650.00 | 2,308,650.00 |
| 2034 | 2,085,000 | 224,700.00 | 2,309,700.00 |
| 2035 | 2,195,000 | 115,237.50 | 2,310,237.50 |

The following table sets forth the annual debt service schedule for the Wastewater Bonds and the SRF Loan.

| <u>Year</u> | <u>Wastewater Bonds</u> | | | <u>SRF Loan</u> | | | <u>Total Debt Service</u> |
|-------------|-------------------------|-----------------|----------------------|------------------|-----------------|----------------------|---------------------------|
| | <u>Principal</u> | <u>Interest</u> | <u>Total P&I</u> | <u>Principal</u> | <u>Interest</u> | <u>Total P&I</u> | |
| 2006 | \$ 265,000 | \$258,526.02 | \$523,526.02 | \$207,050.09 | \$97,238.62 | \$304,288.71 | \$827,814.73 |
| 2007 | 240,000 | 291,876.26 | 531,876.26 | 212,433.40 | 91,855.31 | 304,288.71 | 836,164.97 |
| 2008 | 245,000 | 284,076.26 | 529,076.26 | 217,956.66 | 86,332.05 | 304,288.71 | 833,364.97 |
| 2009 | 250,000 | 275,991.26 | 525,991.26 | 223,623.54 | 80,665.17 | 304,288.71 | 830,279.97 |
| 2010 | 265,000 | 267,491.26 | 532,491.26 | 229,437.75 | 74,850.96 | 304,288.71 | 836,779.97 |
| 2011 | 135,000 | 258,216.26 | 393,216.26 | 235,403.13 | 68,885.58 | 304,288.71 | 697,504.97 |
| 2012 | 140,000 | 253,288.76 | 393,288.76 | 241,523.61 | 62,765.10 | 304,288.71 | 697,577.47 |
| 2013 | 145,000 | 248,038.76 | 393,038.76 | 247,803.23 | 56,485.48 | 304,288.71 | 697,327.47 |
| 2014 | 155,000 | 242,456.26 | 397,456.26 | 254,246.11 | 50,042.60 | 304,288.71 | 701,744.97 |
| 2015 | 160,000 | 236,333.76 | 396,333.76 | 260,856.51 | 43,432.20 | 304,288.71 | 700,622.47 |
| 2016 | 165,000 | 229,853.76 | 394,853.76 | 267,638.78 | 36,649.93 | 304,288.71 | 699,142.47 |
| 2017 | 170,000 | 223,006.26 | 393,006.26 | 274,597.39 | 29,691.32 | 304,288.71 | 697,294.97 |
| 2018 | 180,000 | 216,206.26 | 396,206.26 | 281,736.92 | 22,551.79 | 304,288.71 | 700,494.97 |
| 2019 | 185,000 | 208,781.26 | 393,781.26 | 289,062.08 | 15,226.63 | 304,288.71 | 698,069.97 |
| 2020 | 195,000 | 201,150.00 | 396,150.00 | 296,577.61 | 7,711.02 | 304,288.63 | 700,438.63 |
| 2021 | 200,000 | 193,106.26 | 393,106.26 | --- | --- | --- | 393,106.26 |
| 2022 | 210,000 | 184,106.26 | 394,106.26 | --- | --- | --- | 394,106.26 |
| 2023 | 220,000 | 174,656.26 | 394,656.26 | --- | --- | --- | 394,656.26 |
| 2024 | 230,000 | 164,756.26 | 394,756.26 | --- | --- | --- | 394,756.26 |
| 2025 | 240,000 | 154,406.26 | 394,406.26 | --- | --- | --- | 394,406.26 |
| 2026 | 250,000 | 143,606.26 | 393,606.26 | --- | --- | --- | 393,606.26 |
| 2027 | 265,000 | 132,043.76 | 397,043.76 | --- | --- | --- | 397,043.76 |
| 2028 | 275,000 | 119,787.50 | 394,787.50 | --- | --- | --- | 394,787.50 |
| 2029 | 290,000 | 107,068.76 | 397,068.76 | --- | --- | --- | 397,068.76 |
| 2030 | 300,000 | 93,656.26 | 393,656.26 | --- | --- | --- | 393,656.26 |
| 2031 | 315,000 | 79,781.26 | 394,781.26 | --- | --- | --- | 394,781.26 |
| 2032 | 330,000 | 65,212.50 | 395,212.50 | --- | --- | --- | 395,212.50 |
| 2033 | 345,000 | 49,950.00 | 394,950.00 | --- | --- | --- | 394,950.00 |
| 2034 | 360,000 | 33,993.76 | 393,993.76 | --- | --- | --- | 393,993.76 |
| 2035 | 375,000 | 17,343.76 | 392,343.76 | --- | --- | --- | 392,343.76 |

SECURITY FOR THE WATER BONDS

Pursuant to the Water Indenture, the Water Bonds are payable from Net Water Revenues and other amounts held under the Water Indenture and investment earnings thereon, all as set forth in the Water Indenture. The Net Water Revenues pledged to the payment of the Water Bonds are calculated by deducting from the Gross Water Revenues (as defined below) in each Fiscal Year the amounts required for operation and maintenance of the Water System, as described below. See "SECURITY FOR THE WATER BONDS – Application of Revenues" below.

The Net Water Revenues are pledged solely for the Water Bonds and do not secure and are not pledged for the Wastewater Bonds.

The Water Bonds are not secured by, and the Owners of Water Bonds have no security interest in or mortgage on the property of the Water Enterprise, the Wastewater Enterprise or of the Authority. Default by the Authority will not result in loss of any property. Should the Authority default, the Trustee may declare all unpaid principal, together with accrued interest at the rate or rates specified on the respective outstanding Water Bonds from the immediately preceding Interest Payment Date on which payment was made, to be immediately due and payable, whereupon the same shall become due and payable, and take whatever action at law or in equity may appear necessary or desirable to accelerate the principal of the Outstanding Water Bonds, or enforce performance and observance of any obligation, agreement or covenant of the Authority under the Water Indenture. See "BONDOWNERS' RISKS - Limited Recourse on Default."

Rates and Charges

Pursuant to the Water Indenture, the Authority covenants to fix, prescribe, revise and collect (or cause to be fixed, prescribed, revised and collected, as necessary and applicable) rates, fees and charges for the Water Enterprise, for the services and improvements furnished by said enterprise during each Fiscal Year, which are at least sufficient, after making allowances for contingencies and error in the estimates, to yield revenues (the "Gross Water Revenues") from the Water Enterprise sufficient to pay the following amounts in the following order of priority:

- (a) Water Operation and Maintenance Expenses estimated by the Authority to become due and payable in such Fiscal Year;
- (b) Debt Service payments on the Water Bonds as they become due and payable during such Fiscal Year, without preference or priority, except to the extent such Debt Service payments are payable from the proceeds of the Water Bonds or from any other source of legally available funds of the Authority that have been deposited with the Trustee for such purpose prior to the commencement of such Fiscal Year;
- (c) the amount, if any, required to restore the balance in the Water Reserve Account to the full amount of the Water Reserve Requirement; and
- (d) other payments required to meet any other obligations of the Authority that are charges, liens, encumbrances upon, or which are otherwise payable, from Gross Water Revenues during such Fiscal Year.

The Authority also covenants under the Water Indenture to cause to be fixed, prescribed, revised and collected, rates, fees and charges for the services and improvements furnished by the Water Enterprise during each Fiscal Year that are sufficient to yield Net Water Revenues that are at least equal

to one hundred fifteen percent (115%) of the Debt Service payments coming due and payable in such Fiscal Year under the Water Indenture.

Pursuant to the Water Lease, the City has covenanted to the Authority that the City will, upon receipt of a request from the Authority documenting the need to fix, prescribe, revise, or collect certain rates, fees or charges, take the necessary actions to ensure that the Authority is able to meet its obligations as specified above.

Application of Revenues

There is established under the Water Indenture a Water Fund, such fund to be held separately and maintained in trust by the Authority, into which funds Gross Water Revenues will be deposited, to be applied as follows:

- (a) after payment of all Water Operation and Maintenance Expenses (including amounts reasonably required to be set aside in contingency reserves for Water Operation and Maintenance Expenses the payment of which is not then immediately required) as they become due and payable, to the Trustee, on or before the tenth (10th) Business Day preceding each Interest Payment Date, provided no Event of Default has occurred and is continuing, for deposit into the Bond Fund for the Water Bonds the amount equal to (i) the aggregate amount of interest coming due and payable on the Water Bonds on the next succeeding Interest Payment Date, plus (ii) one-half of the aggregate amount of the principal coming due and payable on the next succeeding Principal Payment Date, which payments shall be made on a parity basis with any outstanding Parity Obligations; and
- (b) to the Trustee for deposit in the Reserve Account for the Water Bonds, the amount, if any, required to restore the balance in said Reserve Account to the Reserve Requirement, the notice of which deficiency shall have been given by the Trustee to the Authority pursuant to the Water Indenture.

Amounts remaining in the Water Fund immediately after making the transfers required to be made under the Water Indenture shall be released to the Authority free and clear of the lien of said Indenture, to be used by the Authority for any lawful purpose including but not limited to making lease payments pursuant to the Water Lease, as applicable.

Reserve Accounts

A Reserve Account is established under the Water Indenture to be held in trust by the Trustee. The Reserve Requirement for the Water Bonds, means, as of any date of calculation, an amount not to exceed the least of: (i) one hundred percent (100%) of the Maximum Annual Debt Service; (ii) one hundred twenty-five percent (125%) of average Annual Debt Service for the then current and every subsequent Bond Year; and (iii) ten percent (10%) of the issue price (as defined pursuant to section 148 of the Code).

Amounts in the Reserve Account for the Water Bonds are to be used solely (a) to pay interest on or principal of the Water Bonds when due and payable to the extent the amounts in the Interest Account or Principal Account, respectively, are insufficient for such purpose, (b) to pay redemption price of Water Term Bonds to be redeemed pursuant to the Water Indenture, if any, and (c) to make final payments of principal of and interest on the Water Bonds.

Pursuant to the terms of the Water Indenture, the Reserve Requirement may be satisfied by crediting to the Reserve Account moneys or a Qualified Reserve Account Credit Instrument or any

combination thereof, which in the aggregate make funds available in the Reserve Account in an amount equal to the Reserve Requirement. For additional information on the Reserve Account and the provisions of the Wastewater Indenture in connection with the Reserve Requirement and the Qualified Reserve Account Credit Instrument, refer to "APPENDIX C – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Qualified Reserve Account Credit Instrument

Concurrently with the issuance of the Bonds, Financial Guaranty Insurance Company ("Financial Guaranty") will issue its Municipal Bond Debt Service Reserve Fund Policy (the "Reserve Policy"). The Reserve Policy unconditionally guarantees the payment of that portion of the principal or accreted value (if applicable) of and interest on the Water Bonds which has become due for payment, but shall be unpaid by reason of nonpayment by the Authority, provided that the aggregate amount paid under the Reserve Policy may not exceed the maximum amount set forth in the Reserve Policy, \$2,310,737.50. Financial Guaranty will make such payments to the paying agent (the "Paying Agent") for the Water Bonds on the later of the date on which such principal or accreted value (if applicable) and interest is due or on the business day next following the day on which Financial Guaranty shall have received telephonic or telegraphic notice subsequently confirmed in writing or written notice by registered or certified mail from the Paying Agent of the nonpayment of such amount by the Issuer. The term "nonpayment" in respect of a Water Bond includes any payment of principal, accreted value or interest (as applicable) made to an owner of a Water Bond which has been recovered from such owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final nonappealable order of a court having competent jurisdiction.

The Reserve Policy is non-cancelable and the premium will be fully paid at the time of delivery of the Bonds. The Reserve Policy covers failure to pay principal or accreted value (if applicable) of the Bonds on their respective stated maturity dates, or dates on which the same shall have been called for mandatory sinking fund redemption, and not on any other date on which the Water Bonds may have been accelerated, and covers the failure to pay an installment of interest on the stated date for its payment. The Reserve Policy shall terminate on the earlier of the scheduled final maturity date of the Water Bonds or the date on which no Water Bonds are outstanding under the authorizing document.

Generally, in connection with its issuance of a Reserve Policy, Financial Guaranty requires, among other things, (i) that, so long as it has not failed to comply with its payment obligations under the Reserve Policy, it be granted the power to exercise any remedies available at law or under the authorizing document other than (A) acceleration of the Water Bonds or (B) remedies which would adversely affect holders in the event that the issuer fails to reimburse Financial Guaranty for any draws on the Reserve Policy; and (ii) that any amendment or supplement to or other modification of the principal legal documents be subject to Financial Guaranty's consent. The specific rights, if any, granted to Financial Guaranty in connection with its issuance of the Reserve Policy are set forth in the Water Indenture. Reference should be made as well to such Indenture for a discussion of the circumstances, if any, under which the issuer of the Water Bonds is required to provide additional or substitute credit enhancement, and related matters.

The Reserve Policy is not covered by the Property/Casualty Insurance Security Fund specified in Article 76 of the New York Insurance Law.

The Reserve Policy is not covered by the California Insurance Guaranty Association (California Insurance Code, Article 14.2).

Financial Guaranty Insurance Company. Certain financial and other relevant information concerning Financial Guaranty is included below under the caption "Insurance for the Water Bonds" which should be read in its entirety. See "BOND INSURANCE – Insurance for the Water Bonds."

SECURITY FOR THE WASTEWATER BONDS

Pursuant to the Wastewater Indenture, the Wastewater Bonds are payable from Net Wastewater Revenues and other amounts held under the Wastewater Indenture and investment earnings thereon, all as set forth in the Wastewater Indenture. In each Fiscal Year, the Net Wastewater Revenues pledged to the payment of the Wastewater Bonds are calculated by deducting from Gross Wastewater Revenues (as defined below) the amounts required for operation and maintenance of the Wastewater System, as described below. See "SECURITY FOR THE WASTEWATER BONDS – Application of Revenues" below.

The Net Wastewater Revenues are pledged solely for the Wastewater Bonds and do not secure and are not pledged for the Water Bonds.

The Wastewater Bonds are not secured by, and the Owners of Wastewater Bonds have no security interest in or mortgage on the property of the Water Enterprise, the Wastewater Enterprise or of the Authority. Default by the Authority will not result in loss of any property. Should the Authority default, the Trustee may declare all unpaid principal, together with accrued interest at the rate or rates specified on the respective outstanding Wastewater Bonds from the immediately preceding Interest Payment Date on which payment was made, to be immediately due and payable, whereupon the same shall become due and payable, and take whatever action at law or in equity may appear necessary or desirable to accelerate the principal of the Outstanding Wastewater Bonds, or enforce performance and observance of any obligation, agreement or covenant of the Authority under the Wastewater Indenture. See "BONDOWNERS' RISKS - Limited Recourse on Default."

Rates and Charges

Pursuant to the Wastewater Indenture, the Authority covenants to fix, prescribe, revise and collect (or cause to be fixed, prescribed, revised and collected, as necessary and applicable) rates, fees and charges for the Wastewater Enterprise, for the services and improvements furnished by said enterprise during each Fiscal Year, which are at least sufficient, after making allowances for contingencies and error in the estimates, to yield revenues (the "Gross Wastewater Revenues") from the Wastewater Enterprise sufficient to pay the following amounts in the following order of priority:

- (a) Wastewater Operation and Maintenance Expenses estimated by the Authority to become due and payable in such Fiscal Year;
- (b) payments required under the SRF Loan and Debt Service payments as they become due and payable during such Fiscal Year, without preference or priority, except to the extent such Debt Service payments are payable from the proceeds of the Wastewater Bonds or from any other source of legally available funds of the Authority that have been deposited with the Trustee for such purpose prior to the commencement of such Fiscal Year;
- (c) the amount, if any, required to restore the balance in the Wastewater Reserve Account to the full amount of the Wastewater Reserve Requirement; and
- (d) Other payments required to meet any other obligations of the Authority that are charges, liens, encumbrances upon, or which are otherwise payable, from Gross Wastewater Revenues during such Fiscal Year.

The Authority also covenants under the Wastewater Indenture to cause to be fixed, prescribed, revised and collected, rates, fees and charges for the services and improvements furnished by the Wastewater Enterprise during each Fiscal Year that are sufficient to yield Net Wastewater Revenues that are at least equal to one hundred fifteen percent (115%) of the Debt Service payments coming due and payable in such Fiscal Year. Such Net Wastewater Revenues must also, after all frontage charges and connection fees are excluded, be equal to at least one hundred percent (100%) of total Debt Service payment coming due on the Wastewater Bonds.

Pursuant to the Wastewater Lease, the City has covenanted to the Authority that the City will, upon receipt of a request from the Authority documenting the need to fix, prescribe, revise, or collect certain rates, fees or charges, take the necessary actions to ensure that the Authority is able to meet its obligations as specified above.

Application of Revenues

There is established under the Wastewater Indenture a Wastewater Fund, such fund to be held separately and maintained in trust by the Authority, into which funds Gross Wastewater Revenues will be deposited, to be applied as follows:

- (a) after payment of all Wastewater Operation and Maintenance Expenses (including amounts reasonably required to be set aside in contingency reserves for Water Operation and Maintenance Expenses the payment of which is not then immediately required) as they become due and payable, to the Trustee, on or before the tenth (10th) Business Day preceding each Interest Payment Date, provided no Event of Default has occurred and is continuing, for deposit into the Bond Fund for the Wastewater Bonds the amount equal to (i) the aggregate amount of interest coming due and payable on the Wastewater Bonds on the next succeeding Interest Payment Date, plus (ii) one-half of the aggregate amount of the principal coming due and payable on the next succeeding Principal Payment Date, which payments shall be made on a parity basis with any outstanding Parity Obligations; and
- (b) to the Trustee for deposit in the Reserve Account for the Wastewater Bonds, the amount, if any, required to restore the balance in said Reserve Account to the Reserve Requirement, the notice of which deficiency shall have been given by the Trustee to the Authority pursuant to the Wastewater Indenture.

Amounts remaining in the Wastewater Fund immediately after making the transfers required to be made under the Wastewater Indenture shall be released to the Authority free and clear of the lien of said Indenture, to be used by the Authority for any lawful purpose including but not limited to making lease payments pursuant to the Wastewater Lease, as applicable.

Reserve Account

A Reserve Account is established under the Wastewater Indenture to be held in trust by the Trustee. The Reserve Requirement for the Wastewater Bonds, pursuant to the Wastewater Indenture, means, as of any date of calculation, an amount not to exceed the least of: (i) one hundred percent (100%) of the Maximum Annual Debt Service; (ii) one hundred twenty-five percent (125%) of average Annual Debt Service for the then current and every subsequent Bond Year; and (iii) ten percent (10%) of the issue price (as defined pursuant to section 148 of the Code).

Amounts in the Reserve Account for the Wastewater Bonds are to be used solely (a) to pay interest on or principal of the Wastewater Bonds when due and payable to the extent the amounts in the

Interest Account or Principal Account, respectively, are insufficient for such purpose, (b) to pay redemption price of Wastewater Term Bonds to be redeemed pursuant to the Wastewater Indenture, if any, and (c) to make final payments of principal of and interest on the Wastewater Bonds.

Pursuant to the terms of the Wastewater Indenture, the applicable Reserve Requirement may be satisfied by crediting to the Reserve Account moneys or a Qualified Reserve Account Credit Instrument or any combination thereof, which in the aggregate make funds available in the Reserve Account in an amount equal to the Reserve Requirement. For additional information on the Reserve Account and the provisions of the Wastewater Indenture in connection with the Reserve Requirement and the Qualified Reserve Account Credit Instrument, refer to "APPENDIX C – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Qualified Reserve Account Credit Instrument

Application has been made to Ambac Assurance Corporation ("Ambac Assurance") for the issuance of a Surety Bond (the "Surety Bond"), constituting a Qualified Reserve Account Credit Instrument, for the purpose of funding the Reserve Requirement for the Wastewater Bonds as authorized by the Wastewater Indenture. The Wastewater Bonds will only be delivered upon the issuance of such Surety Bond. The premium on the Surety Bond is to be fully paid at or prior to the issuance and delivery of the Wastewater Bonds. The Surety Bond provides that upon the later of (i) one (1) day after receipt by Ambac Assurance of a demand for payment executed by the Trustee for the Wastewater Bonds certifying that provision for the payment of principal of or interest on the Wastewater Bonds when dues has not been made or (ii) the interest payment date specified in the Demand for Payment submitted to Ambac Assurance, Ambac Assurance will promptly deposit funds with the Trustee sufficient to enable the Trustee to make such payments due on the Wastewater Bonds, but in no event exceeding the Surety Bond Coverage, as defined in the Surety Bond.

Pursuant to the terms of the Surety Bond, the Surety Bond Coverage is automatically reduced to the extent of each payment made by Ambac Assurance under the terms of the Surety Bond and the Authority is required to reimburse Ambac Assurance for any draws under the Surety Bond with interest at a market rate. Upon such reimbursement, the Surety Bond is reinstated to the extent of each principal reimbursement up to but not exceeding the Surety Bond Coverage. The reimbursement obligation of the Authority is subordinate to the Authority's obligations with respect to the Wastewater Bonds.

In the event the amount on deposit, or credited to the Reserve Account for the Wastewater Bonds exceeds the amount of the Surety Bond, any draw on the Surety Bond shall be made only after all the funds in the Debt Service Reserve Fund have been expended. In the event that the amount on deposit in, or credited to, the Reserve Account, in addition to the amount available under the Surety Bond, includes amounts available under a letter of credit, insurance policy, Surety Bond or other such funding instrument (the "Additional Funding Instrument"), draws on the Surety Bond and the Additional Funding Instrument shall be made on a pro rata basis to fund the insufficiency. The Wastewater Indenture provides that the Reserve Account shall be replenished in the following priority; (i) principal and interest on the Surety Bond and on the Additional Funding Instrument shall be paid from first available revenues on a pro rata basis; (ii) after all such amounts are paid in full, amounts necessary to fund the Reserve Account to the Reserve Requirement, after taking into account the amounts available under the Surety Bond and the Additional Funding Instrument shall be deposited from next available revenues.

The Surety Bond does not insure against nonpayment caused by the insolvency or negligence of the Trustee or the Paying Agent.

In the event that Ambac Assurance were to become insolvent, any claims arising under the Surety Bond would be excluded from coverage by the California Insurance Guaranty Association, established pursuant to the laws of the State of California.

Ambac Assurance Corporation. Certain financial and other relevant general information concerning Ambac Assurance is included below under the caption "Insurance for the Wastewater Bonds" which should be read in its entirety. See "BOND INSURANCE – Insurance for Wastewater Bonds."

PARITY OBLIGATIONS

The Authority covenants that no bonds or other indebtedness shall be issued or incurred that are payable in whole or in part out of the Net Water Revenues or Net Wastewater Revenues on a basis senior to the Water Bonds or Wastewater Bonds. Additional obligations may be issued on a parity with the Water Bonds or the Wastewater Bonds under the applicable Indenture or on a basis subordinate to the Water Bonds or Wastewater Bonds to the extent required.

A State Revolving Fund loan (the "SRF Loan") has been obtained by the City to fund certain costs of project construction for the Wastewater Enterprise, generally consisting of headworks, a sludge digester, sludge drying beds and a chemical addition facility for the existing primary clarifiers. In connection with the SRF Loan, the City adopted Resolution No. 1998-89 authorizing the establishment of a dedicated source or revenue and a special fund designated as the capital reserve fund into which the City has committed to deposit a portion of the monthly charges collected by the City from the users of the Wastewater System. Resolution 1998-89 also provided that the dedicated source of revenues will remain in effect until the SRF Loan is fully discharged. The current balance due on the SRF Loan is amount of approximately \$3,739,946.81. The Wastewater Bonds will be secured and payable on a parity with the SRF Loan from Net Wastewater Revenues.

Issuance of Additional Parity Obligations

Except for obligations incurred to prepay or post a security deposit for the payment of the Water Bonds or the Wastewater Bonds, as applicable, the Authority may issue or incur Parity Obligations under the respective Indenture, during the term of the Bonds only if:

Water Bonds

- (a) no Event of Default has occurred and is continuing under the Water Indenture;
- (b) the Net Water Revenues, calculated in accordance with generally accepted accounting principles, as shown by the books of the Authority for the most recent completed Fiscal Year for which audited financial statements are available, or for any more recent consecutive twelve (12) month period selected by the Authority, in either case verified by a certificate or opinion of an independent accountant or financial consultant, are at least equal to 120% of the amount of Maximum Annual Debt Service, plus maximum annual debt service on all Parity Obligations then Outstanding (including the Parity Obligations then proposed to be issued); and

Either or both of the following items may be added to such Net Water Revenues for the purpose of applying the restriction contained in this paragraph (b):

- 1. An allowance for revenues from any additions to or improvements or extensions of the Water Enterprise to be constructed with the proceeds of such additional obligations, and also for net revenues from any such additions, improvements or

extensions which have been from moneys from any source but which, during all or any part of such Fiscal Year, were not in service, all in an amount equal to 70% of the estimated additional average annual Net Water Revenues to be derived from such additions, improvements and extensions for the first 36-month period following closing of the proposed Parity Obligation, all as shown by the certificate or opinion of a qualified independent consultant employed by the Authority, may be added to such Net Water Revenues for the purpose of applying the restriction contained in this paragraph (b).

2. An allowance for earnings arising from any increase in the charges made for service from the Water Enterprise which has become effective prior to the incurring of such additional obligations but which, during all or any part of such Fiscal Year, was not in effect, in an amount equal to 100% of the amount by which the Net Water Revenues would have been increased if such increase in charges had been in effect during the whole of such Fiscal Year and any period prior to the incurring of such additional obligations, as shown by the certificate or opinion of a qualified independent engineer employed by the Authority.

- (c) upon the issuance of such Parity Obligations a reserve fund shall be established for such Parity Obligations in an amount equal to the reserve requirement with respect to such Parity Obligations.

Wastewater Bonds

- (a) no Event of Default has occurred and is continuing under the Wastewater Indenture;
- (b) the Net Wastewater Revenues (excluding therefrom, however, frontage charges and connection fees), calculated in accordance with generally accepted accounting principles, as shown by the books of the Authority for the most recent completed Fiscal Year for which audited financial statements are available, or for any more recent consecutive twelve (12)-month period selected by the Authority, in either case verified by a certificate or opinion of an independent accountant or financial consultant, are at least equal to 100% of the amount of Maximum Annual Debt Service, plus maximum annual debt service on all Parity Obligations then Outstanding (including the Parity Obligations then proposed to be issued);
- (c) the Net Wastewater Revenues, calculated in accordance with generally accepted accounting procedures, as shown by the books of the Authority for the most recent completed Fiscal Year for which audited financial statements are available, or for any more recent consecutive twelve (12) month period selected by the Authority, in either case verified by a certificate or opinion of an independent accountant or financial consultant, are at least equal to 120% of the amount of Maximum Annual Debt Service, plus maximum annual debt service on all Parity Obligations then Outstanding (including the Parity Obligations then proposed to be issued);
- (d) upon the issuance of such Parity Obligations a reserve fund shall be established for such Parity Obligations in an amount at least equal to the lesser of (i) maximum annual debt service on such Parity Obligations, or (ii) the maximum amount then permitted under the Code; and

Either or both of the following items may be added to such Net Wastewater Revenues for the purpose of applying the restriction contained in paragraphs (b) and (c) above:

1. An allowance for revenues from any additions to or improvements or extensions of the Wastewater Enterprise to be constructed with the proceeds of such additional obligations, and also for net revenues from any such additions, improvements or extensions which have been from moneys from any source but which, during all or any part of such Fiscal Year, were not in service, all in an amount equal to 70% of the estimated additional average annual Net Wastewater Revenues to be derived from such additions, improvements and extensions for the first 36-month period following closing of the proposed Parity Obligation, all as shown by the certificate or opinion of a qualified independent consultant employed by the Authority, may be added to such Net Wastewater Revenues for the purpose of applying the restriction contained in paragraphs (b) and (c) above.

2. An allowance for earnings arising from any increase in the charges made for service from the Wastewater Enterprise which has become effective prior to the incurring of such additional obligations but which, during all or any part of such Fiscal Year, was not in effect, in an amount equal to 100% of the amount by which the Net Wastewater Revenues would have been increased if such increase in charges had been in effect during the whole of such Fiscal Year and any period prior to the incurring of such additional obligations, as shown by the certificate or opinion of a qualified independent engineer employed by the Authority.

BOND INSURANCE

Concurrently with the issuance of the Water Bonds, Financial Guaranty Insurance Company will issue its Municipal Bond New Issue Insurance Policy for the Water Bonds (the "Water Bonds Policy"). The Water Bonds Policy guarantees the scheduled payment of principal of and interest on the Water Bonds when due as set forth in the form of the Water Bonds Policy included as Appendix G-1 to this Official Statement.

Concurrently with the issuance of the Wastewater Bonds, Ambac Assurance Corporation will issue its Financial Guaranty Insurance Policy for the Wastewater Bonds (the "Wastewater Bonds Policy"). The Wastewater Bonds Policy guarantees the scheduled payment of principal of and interest on the Wastewater Bonds when due as set forth in the form of the Wastewater Bonds Policy included as Appendix G-2 to this Official Statement

Insurance for the Water Bonds

Financial Guaranty Insurance Company has supplied the following information for inclusion in this Official Statement. No representation is made by the issuer or the underwriter as to the accuracy or completeness of this information.

Payments Under the Policy. Concurrently with the issuance of the Water Bonds, Financial Guaranty Insurance Company, doing business in California as FGIC Insurance Company ("Financial Guaranty"), will issue its Municipal Bond New Issue Insurance Policy for the Water Bonds (the "Water Bonds Policy"). The Water Bonds Policy unconditionally guarantees the payment of that portion of the principal or accreted value (if applicable) of and interest on the Water Bonds which has become due for payment, but shall be unpaid by reason of nonpayment by the issuer of the Water Bonds (the "Issuer"). Financial Guaranty will make such payments to U.S. Bank Trust National Association, or its successor as its agent (the "Fiscal Agent"), on the later of the date on which such principal, accreted value or interest (as applicable) is due or on the business day next following the day on which Financial Guaranty shall have received notice (in accordance with the terms of the Water Bonds Policy) from an owner of Water Bonds or the trustee or paying agent (if any) of the nonpayment of such amount by the Issuer. The Fiscal Agent will disburse such amount due on any Water Bond to its owner upon receipt by the Fiscal Agent of

evidence satisfactory to the Fiscal Agent of the owner's right to receive payment of the principal, accreted value or interest (as applicable) due for payment and evidence, including any appropriate instruments of assignment, that all of such owner's rights to payment of such principal, accreted value or interest (as applicable) shall be vested in Financial Guaranty. The term "nonpayment" in respect of a Water Bond includes any payment of principal, accreted value or interest (as applicable) made to an owner of a Water Bond which has been recovered from such owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction.

Once issued, the Water Bonds Policy is non-cancellable by Financial Guaranty. The Water Bonds Policy covers failure to pay principal (or accreted value, if applicable) of the Water Bonds on their stated maturity dates and their mandatory sinking fund redemption dates, and not on any other date on which the Water Bonds may have been otherwise called for redemption, accelerated or advanced in maturity. The Water Bonds Policy also covers the failure to pay interest on the stated date for its payment. In the event that payment of the Water Bonds is accelerated, Financial Guaranty will only be obligated to pay principal (or accreted value, if applicable) and interest in the originally scheduled amounts on the originally scheduled payment dates. Upon such payment, Financial Guaranty will become the owner of the Bond, appurtenant coupon or right to payment of principal or interest on such Bond and will be fully subrogated to all of the Bondholder's rights thereunder.

The Water Bonds Policy does not insure any risk other than Nonpayment by the Issuer, as defined in the Water Bonds Policy. Specifically, the Water Bonds Policy does not cover: (i) payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity; (ii) payment of any redemption, prepayment or acceleration premium; or (iii) nonpayment of principal (or accreted value, if applicable) or interest caused by the insolvency or negligence or any other act or omission of the trustee or paying agent, if any.

As a condition of its commitment to insure Water Bonds, Financial Guaranty may be granted certain rights under the Water Bond documentation. The specific rights, if any, granted to Financial Guaranty in connection with its insurance of the Water Bonds may be set forth in the description of the principal legal documents appearing elsewhere in this Official Statement, and reference should be made thereto.

The Water Bonds Policy is not covered by the California Insurance Guaranty Association (California Insurance Code, Article 14.2).

Financial Guaranty Insurance Company. Financial Guaranty, a New York stock insurance corporation, is a direct, wholly-owned subsidiary of FGIC Corporation, a Delaware corporation, and provides financial guaranty insurance for public finance and structured finance obligations. Financial Guaranty is licensed to engage in financial guaranty insurance in all 50 states, the District of Columbia, the Commonwealth of Puerto Rico and, through a branch, in the United Kingdom.

On December 18, 2003, an investor group consisting of The PMI Group, Inc. ("PMI"), affiliates of The Blackstone Group L.P. ("Blackstone"), affiliates of The Cypress Group L.L.C. ("Cypress") and affiliates of CIVC Partners L.P. ("CIVC") acquired FGIC Corporation (the "FGIC Acquisition") from a subsidiary of General Electric Capital Corporation ("GE Capital"). PMI, Blackstone, Cypress and CIVC acquired approximately 42%, 23%, 23% and 7%, respectively, of FGIC Corporation's common stock. FGIC Corporation paid GE Capital approximately \$284.3 million in pre-closing dividends from the proceeds of dividends it, in turn, had received from Financial Guaranty, and GE Capital retained approximately \$234.6 million in liquidation preference of FGIC Corporation's convertible participating preferred stock and approximately 5% of FGIC Corporation's common stock. Neither FGIC Corporation

nor any of its shareholders is obligated to pay any debts of Financial Guaranty or any claims under any insurance policy, including the Policy, issued by Financial Guaranty.

Financial Guaranty is subject to the insurance laws and regulations of the State of New York, where it is domiciled, including Article 69 of the New York Insurance Law ("Article 69"), a comprehensive financial guaranty insurance statute. Financial Guaranty is also subject to the insurance laws and regulations of all other jurisdictions in which it is licensed to transact insurance business. The insurance laws and regulations, as well as the level of supervisory authority that may be exercised by the various insurance regulators, vary by jurisdiction, but generally require insurance companies to maintain minimum standards of business conduct and solvency, to meet certain financial tests, to comply with requirements concerning permitted investments and the use of policy forms and premium rates and to file quarterly and annual financial statements on the basis of statutory accounting principles ("SAP") and other reports. In addition, Article 69, among other things, limits the business of each financial guaranty insurer, including Financial Guaranty, to financial guaranty insurance and certain related lines.

For the nine months ended September 30, 2005, and the years ended December 31, 2004, and December 31, 2003, Financial Guaranty had written directly or assumed through reinsurance, guaranties of approximately \$58.5 billion, \$59.5 billion and \$42.4 billion par value of securities, respectively (of which approximately 55%, 56% and 79%, respectively, constituted guaranties of municipal bonds), for which it had collected gross premiums of approximately \$312.5 million, \$323.6 million and \$260.3 million, respectively. For the nine months ended September 30, 2005, Financial Guaranty had reinsured, through facultative and excess of loss arrangements, approximately 7.8% of the risks it had written.

As of September 30, 2005, Financial Guaranty had net admitted assets of approximately \$3.401 billion, total liabilities of approximately \$2.246 billion, and total capital and policyholders' surplus of approximately \$1.155 billion, determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities.

The unaudited financial statements of Financial Guaranty as of September 30, 2005, the audited financial statements of Financial Guaranty as of December 31, 2004, and the audited financial statements of Financial Guaranty as of December 31, 2003, which have been filed with the Nationally Recognized Municipal Securities Information Repositories ("NRMSIRs"), are hereby included by specific reference in this Official Statement. Any statement contained herein under the heading "BOND INSURANCE – Insurance for the Water Bonds," or in any documents included by specific reference herein, shall be modified or superseded to the extent required by any statement in any document subsequently filed by Financial Guaranty with such NRMSIRs, and shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement. All financial statements of Financial Guaranty (if any) included in documents filed by Financial Guaranty with the NRMSIRs subsequent to the date of this Official Statement and prior to the termination of the offering of the Water Bonds shall be deemed to be included by specific reference into this Official Statement and to be a part hereof from the respective dates of filing of such documents.

Financial Guaranty also prepares quarterly and annual financial statements on the basis of generally accepted accounting principles. Copies of Financial Guaranty's most recent GAAP and SAP financial statements are available upon request to: Financial Guaranty Insurance Company, 125 Park Avenue, New York, NY 10017, Attention: Corporate Communications Department. Financial Guaranty's telephone number is (212) 312-3000.

Financial Guaranty's Credit Ratings. The financial strength of Financial Guaranty is rated "AAA" by Standard & Poor's, a Division of The McGraw-Hill Companies, Inc., "Aaa" by Moody's Investors Service, and "AAA" by Fitch Ratings. Each rating of Financial Guaranty should be evaluated independently. The ratings reflect the respective ratings agencies' current assessments of the insurance

financial strength of Financial Guaranty. Any further explanation of any rating may be obtained only from the applicable rating agency. These ratings are not recommendations to buy, sell or hold the Water Bonds, and are subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of the Water Bonds. Financial Guaranty does not guarantee the market price or investment value of the Water Bonds nor does it guarantee that the ratings on the Water Bonds will not be revised or withdrawn.

Neither Financial Guaranty nor any of its affiliates accepts any responsibility for the accuracy or completeness of the Official Statement or any information or disclosure that is provided to potential purchasers of the Bonds, or omitted from such disclosure, other than with respect to the accuracy of information with respect to Financial Guaranty or the Water Bonds Policy under the headings "SECURITY FOR THE WATER BONDS - Qualified Reserve Account Credit Instrument," and "BOND INSURANCE - Insurance for the Water Bonds." In addition, Financial Guaranty makes no representation regarding the Bonds or the advisability of investing in the Bonds.

Insurance for the Wastewater Bonds

Payment Pursuant to Financial Guaranty Insurance Policy. Ambac Assurance has made a commitment to issue a financial guaranty insurance policy (the "Financial Guaranty Insurance Policy") relating to the Wastewater Bonds effective as of the date of issuance of the Wastewater Bonds. Under the terms of the Financial Guaranty Insurance Policy, Ambac Assurance will pay to The Bank of New York, in New York, New York or any successor thereto (the "Insurance Trustee") that portion of the principal of and interest on the Wastewater Bonds which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor (as such terms are defined in the Financial Guaranty Insurance Policy). Ambac Assurance will make such payments to the Insurance Trustee on the later of the date on which such principal and interest becomes Due for Payment or within one business day following the date on which Ambac Assurance shall have received notice of Nonpayment from the Trustee. The insurance will extend for the term of the Wastewater Bonds and, once issued, cannot be canceled by Ambac Assurance.

The Financial Guaranty Insurance Policy will insure payment only on stated maturity dates and on mandatory sinking fund installment dates, in the case of principal, and on stated dates for payment, in the case of interest. If the Wastewater Bonds become subject to mandatory redemption and insufficient funds are available for redemption of all outstanding Wastewater Bonds, Ambac Assurance will remain obligated to pay principal of and interest on outstanding Wastewater Bonds on the originally scheduled interest and principal payment dates including mandatory sinking fund redemption dates. In the event of any acceleration of the principal of the Wastewater Bonds, the insured payments will be made at such times and in such amounts as would have been made had there not been an acceleration.

In the event the Trustee has notice that any payment of principal of or interest on a Wastewater Bond which has become Due for Payment and which is made to a Holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from its registered owner pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such registered owner will be entitled to payment from Ambac Assurance to the extent of such recovery if sufficient funds are not otherwise available.

The Financial Guaranty Insurance Policy does **not** insure any risk other than Nonpayment, as defined in the Policy. Specifically, the Financial Guaranty Insurance Policy does **not** cover:

1. payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity.

2. payment of any redemption, prepayment or acceleration premium.
3. nonpayment of principal or interest caused by the insolvency or negligence of any Trustee, Paying Agent or Bond Registrar, if any.

If it becomes necessary to call upon the Financial Guaranty Insurance Policy, payment of principal requires surrender of Wastewater Bonds to the Insurance Trustee together with an appropriate instrument of assignment so as to permit ownership of such Wastewater Bonds to be registered in the name of Ambac Assurance to the extent of the payment under the Financial Guaranty Insurance Policy. Payment of interest pursuant to the Financial Guaranty Insurance Policy requires proof of Holder entitlement to interest payments and an appropriate assignment of the Holder's right to payment to Ambac Assurance.

Upon payment of the insurance benefits, Ambac Assurance will become the owner of the Wastewater Bond, appurtenant coupon, if any, or right to payment of principal or interest on such Wastewater Bond and will be fully subrogated to the surrendering Holder's rights to payment.

In the event that Ambac Assurance were to become insolvent, any claims arising under the Policy would be excluded from coverage by the California Insurance Guaranty Association, established pursuant to the laws of the State of California.

Ambac Assurance Corporation. Ambac Assurance Corporation ("Ambac Assurance") is a Wisconsin-domiciled stock insurance corporation regulated by the Office of the Commissioner of Insurance of the State of Wisconsin and licensed to do business in 50 states, the District of Columbia, the Territory of Guam, the Commonwealth of Puerto Rico and the U.S. Virgin Islands, with admitted assets of approximately **\$8,645,000,000** (unaudited) and statutory capital of approximately **\$5,403,000,000** (unaudited) as of **September 30, 2005**. Statutory capital consists of Ambac Assurance's policyholders' surplus and statutory contingency reserve. Standard & Poor's Credit Markets Services, a Division of The McGraw-Hill Companies, Moody's Investors Service and Fitch Ratings have each assigned a triple-A financial strength rating to Ambac Assurance.

Ambac Assurance has obtained a ruling from the Internal Revenue Service to the effect that the insuring of a Wastewater Bond by Ambac Assurance will not affect the treatment for federal income tax purposes of interest on such Wastewater Bond and that insurance proceeds representing maturing interest paid by Ambac Assurance under policy provisions substantially identical to those contained in its financial guaranty insurance policy shall be treated for federal income tax purposes in the same manner as if such payments were made by the Obligor of the Wastewater Bonds.

Ambac Assurance makes no representation regarding the Wastewater Bonds or the advisability of investing in the Wastewater Bonds and makes no representation regarding, nor has it participated in the preparation of, the Official Statement other than the information supplied by Ambac Assurance and presented under the headings "SECURITY FOR THE WASTEWATER BONDS – Qualified Reserve Account Credit Instrument" and "BOND INSURANCE – Insurance for the Wastewater Bonds".

Available Information. The parent company of Ambac Assurance, Ambac Financial Group, Inc. (the "Company"), is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and in accordance therewith files reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). These reports, proxy statements and other information can be read and copied at the SEC's public reference room at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. The SEC maintains an internet site at <http://www.sec.gov> that contains reports, proxy and information statements and other information regarding companies that file

electronically with the SEC, including the Company. These reports, proxy statements and other information can also be read at the offices of the New York Stock Exchange, Inc. (the "NYSE"), 20 Broad Street, New York, New York 10005.

Copies of Ambac Assurance's financial statements prepared in accordance with statutory accounting standards are available from Ambac Assurance. The address of Ambac Assurance's administrative offices and its telephone number are One State Street Plaza, 19th Floor, New York, New York 10004 and (212) 668-0340.

Incorporation of Certain Documents by Reference. The following documents filed by the Company with the SEC (File No. 1-10777) are incorporated by reference in this Official Statement:

1. The Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2004 and filed on March 15, 2005;
2. The Company's Current Report on Form 8-K dated April 5, 2005 and filed on April 11, 2005;
3. The Company's Current Report on Form 8-K dated and filed on April 20, 2005;
4. The Company's Current Report on Form 8-K dated May 3, 2005 and filed on May 5, 2005;
5. The Company's Quarterly Report on Form 10-Q for the fiscal quarterly period ended March 31, 2005 and filed on May 10, 2005;
6. The Company's Current Report on Form 8-K dated and filed on July 20, 2005;
7. The Company's Current Report on Form 8-K dated July 28, 2005 and filed on August 2, 2005;
8. The Company's Quarterly Report on Form 10-Q for the fiscal quarterly period ended June 30, 2005 and filed on August 9, 2005;
9. The information furnished and deemed to be filed under Item 2.02 contained in the Company's Current Report on Form 8-K dated and filed on October 19, 2005;
10. The Company's Quarterly Report on Form 10-Q for the fiscal quarterly period ended September 30, 2005 and filed on November 9, 2005; and
11. The Company's Current Report on Form 8-K dated November 29, 2005 and filed on December 5, 2005.

All documents subsequently filed by the Company pursuant to the requirements of the Exchange Act after the date of this Official Statement will be available for inspection in the same manner as described above in "Available Information".

THE WATER ENTERPRISE

General

Pursuant to the Water Lease, the Water Enterprise consists of all properties and assets, real or personal, tangible and intangible, of the water system of the City now or hereafter existing, used or pertaining to the production, transmission, distribution and sale of water, including all additions, extensions, expansions, improvements and betterments thereto, and equipments thereof; provided, however, that to the extent the City is not the sole owner of an asset or property, only the City's ownership interest in such asset or property shall be considered a part of the Water Enterprise. See "THE WATER ENTERPRISE – The Water System" below, for more information on the Water Enterprise.

Service Area. The City is the sole provider of water service for residential, commercial, industrial and agricultural users within most of the City. The only exception is a small portion on the northern part of the City that is serviced by the Banning Heights Mutual Water Company. Before the City started providing water service to its residents, the old Banning Water Company, incorporated in 1884, provided that service. The City acquired the assets of the Banning Water Company in 1967. The City also purchased the Mountain Water Company, which supplied water to its customers from groundwater wells within the City and in the unincorporated portion of the County of Riverside, in 1997. The City has provided water service to all other residents for over 37 years.

Background. The State of California does not have a statewide program to manage groundwater or a mandatory groundwater management statute. Groundwater management is a local responsibility accomplished under the authority of the California Water Code and a number of court decisions. There are six possible methods for groundwater management under present law. Groundwater management is achieved by a combination of one or more of the following methods: (i) overlying rights; (ii) local agencies; (iii) adjudicated basins; (iv) formation of special act districts with groundwater management authority; (v) assembly bill 3030; or (vi) local groundwater ordinances.

The City is underlain by the San Gorgonio Pass and Banning Canyon Groundwater Basins. Within the City boundary, the San Gorgonio Pass Basin is subdivided into a series of storage units: the Banning Bench, Banning, Beaumont, and Cabazon storage unit. The Banning Canyon Groundwater Basin in turn consists of three storage units known as the Upper, Middle, and Lower Banning Canyon storage units.

The groundwater basins are naturally recharged through the percolation of runoff, direct precipitation, subsurface inflow, and artificial recharge. The Banning Canyon area receives water from the percolation of canyon flows through the gravelly soils of the canyon bottom. The San Gorgonio River running southerly through the Banning Canyon provides intake areas for distributing water to spreading ditches that interconnect with spreading ponds to enhance percolation. The San Gorgonio Basin is recharged naturally with runoff from the adjacent San Jacinto and San Bernardino Mountains.

Water Sources and Supply. The San Gorgonio Pass divides two major watersheds, the Santa Ana River Watershed to the west and the Salton Sea Watershed to the east. The majority of the City drains towards the Salton Sea Watershed. The San Gorgonio River cuts through the southern area of the City's water planning area forming Banning Canyon. A portion of the City overlies the adjudicated Beaumont Basin, which is the main source of water for the City.

The first recorded claims to the waters of the Banning Canyon date back to 1875. The Banning Water Company was incorporated in 1884 to provide for the delivery of domestic irrigation water to various customers of the City. In 1913 the Banning Water Company entered into an agreement with the Consolidated Reservoir and Power Company for the delivery of 13.26 cubic feet per second of water from the headwaters of the Whitewater River. The Banning Heights Mutual Water Company and the City now receive a portion of that water. In that same year, the Banning Water Company began to operate as a public utility under the rules of the Railroad Commission (now the Public Utilities Commission). In 1957, an order was issued establishing rates for both general metered services and measured irrigation services. The City acquired the Banning Water Company in 1967. In 1997, the City purchased the Mountain Water Company, which supplied water to its customers from groundwater wells located in the City and in the unincorporated portion of the County of Riverside.

In 2003, the City and other major water suppliers in the area developed a stipulated agreement with the San Timoteo Watershed Management Authority adjudicating pumping and storage rights in the Beaumont Basin. Also in 2003, the City and the Beaumont Cherry Valley Water District, another local major water producer, entered into a cooperative agreement to jointly own, operate and construct three

new production wells, to build a water treatment facility and to interconnect their existing potable water distribution systems and recycled water systems. This agreement arose out of the need to implement the groundwater management plan for the shared use and interest in the Beaumont Basin.

In February of 2004 a stipulated judgment (the "Judgment") adjudicating the groundwater pumping and storage rights in the Beaumont Basin was approved by the Superior Court of California. The Judgment establishes pumping rights among the two classes of pumpers: overlying and appropriator. The City is classified as an appropriator. Under the Judgment, the overlying pumpers were assigned fixed rights to 8,650 acre feet per year ("AFY"), which is considered a safe yield, with some flexibility to vary their maximum use during any five-year period. As an appropriator, the City's rights are stated as the percentage or fraction of the 8,650 AFY that is not used by the overlying pumpers. In addition, the Judgment provides that if the City provides water service to the land of an overlying pumper, said pumper must assign its water rights to the City. The City anticipates that, after such assignments, the City will have rights to a minimum of 400 AFY from the safe yield.

The City has the right under the Judgment to pump 5,910 AFY for ten (10) years from the date of the Judgment. The Judgment provides that the safe yield will be re-determined every 10 years. Finally, the Judgment authorizes the City to pump sufficient water from the Beaumont Basin to meet its water demand. If the demand exceeds the City's rights, the Beaumont Basin watermaster has an obligation to replenish the overproduction.

The amount of groundwater in storage within the City, including the portion of the Beaumont Storage Unit located within the City, is estimated to be between 1.4 and 2.6 million acre-feet. The recommended safe yield for the storage units, as calculated in the *Determination of Maximum Perennial Yield for the City of Banning* (Geoscience, 2003), are presented in Table No. 1, below. In the Geoscience report, the maximum perennial yield was determined by subunit and not by storage unit, however, the subunits used in that report are comparable to the storage units identified in the table below. The two exceptions are the Banning Bench Storage Unit and the Cabazon Storage Unit. The Cabazon Storage Unit lies partially within the southern portions of the Hathaway and Portero subunits.

The following table reflects the current groundwater sources for the City and the recommended range of yield.

**TABLE NO. 1
SOURCES OF CITY WATER**

| Sources | Perennial Yield (AFY) |
|--------------------------------------|--------------------------|
| Banning Canyon/Banning Bench Storage | 4,000-6,000 |
| West Banning Storage Unit | 300-400 |
| East Banning Storage Unit | 900-1,200 ⁽¹⁾ |
| Beaumont Storage Unit | 400-6,300 ⁽²⁾ |
| Hathaway | 600-1,000 |
| Portero | 700-1,800 |
| Grand Total | 6,900-16,700 |

Source: City of Banning.

(1) Values do not include wastewater recharge that can be recovered for future potable and non-potable uses

(2) City's allocation of operating yield under the Judgment

Groundwater management is a local responsibility and the City plans to manage its groundwater sources within the recommended range of the maximum perennial yield. In California, some local agencies use groundwater mining, which is the deliberate extraction of groundwater in excess of the recharge of the basin from which the water is extracted, as part of a strategy for overall management.

Under the City's groundwater management plan, the City may choose to mine groundwater when the need arises.

The City's existing and planned water supply sources are reflected in the table below. In addition to the sources described above, the City also plans to purchase 6,574 AFY of State Water Project from the San Geronio Pass Water Agency and an additional 5,780 AFY from the Department of Water Resources of the State of California or other entities. State Water Project water is anticipated to be available starting in 2007. With the exception of the Beaumont Storage Unit, the groundwater supplies for each storage unit in Table No. 2, below reflects the mid-value within the range indicated in Table No. 1 above.

**TABLE NO. 2
EXISTING AND PLANNED WATER SOURCES OF THE CITY**

| Water Supply Source | 2005 | 2010 | 2015 | 2020 | 2025 | 2030 |
|--------------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Banning Canyon/Banning Bench Storage | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 |
| Beaumont Storage Unit | 5,900 | 1,000 | 400 | 400 | 2,500 | 5,000 |
| Cabazon Storage Unit | 0 | 2,050 | 2,050 | 2,050 | 2,050 | 2,050 |
| East Banning Storage Unit | 1,050 | 1,050 | 1,050 | 1,050 | 1,050 | 1,050 |
| West Banning Storage Unit | 350 | 350 | 350 | 350 | 350 | 350 |
| Recycled Water Use | 0 | 1,504 | 1,832 | 2,160 | 2,488 | 2,816 |
| Return Flows from Irrigation | 1,128 | 1,309 | 1,564 | 1,822 | 2,077 | 2,330 |
| State Water Project | 0 | 3,500 | 7,000 | 9,092 | 9,092 | 9,092 |
| Total | 13,428 | 15,763 | 19,246 | 21,924 | 24,607 | 27,688 |

Source: City of Banning.

Recycled water supplies are reflected in Table No. 2, above, as being equal to projected irrigation demand. Recycled water production is anticipated to exceed demand and to be applied in other beneficial ways. Water used for irrigation purposes and not utilized by the plants percolates to the groundwater and is available for future use. That volume of water is known as return flow. Return flows from irrigation were calculated from current and projected demands. If a consumptive factor of 0.75 is used in groundwater quality modeling, the return flows are equal to twenty-five percent (25%) of the total amount of water used for irrigation plus the portion of residential water used for outdoor irrigation, which equals fifty percent (50%) in the City and surrounding areas. Any irrigation occurring in the industrial, commercial or public sector was not included in the return flow calculations.

Storage and Distribution Systems. The water system consists of groundwater wells, reservoirs and a distribution line covering approximately 23 square miles and servicing approximately 28,000 people via approximately 10,500 metered connections.

The City operates and maintains 22 potable groundwater production wells. Half of the wells are located in Banning Canyon and the remaining ones are located in the Banning Bench, East Banning, West Banning and Beaumont storage units. The 22 wells have a total design capacity of approximately 28,450 gallons per minute ("gpm"). During dry years, the capacity of the Canyon and Banning Bench wells decrease in response to decreased precipitation and subsequent recharge. In 2002, a recent dry year, the total capacity of the wells was estimated to be 18,950 gpm. The following table shows a summary of the City's wells and their current capacities by storage unit.

**TABLE NO. 3
WELL CAPACITIES BY STORAGE UNIT**

| Wells by Storage Unit | Well Design Capacity | | Dry Year Capacity | |
|-----------------------|----------------------|--------|-------------------|--------|
| | gpm | AFY | gpm | AFY |
| Upper Banning Canyon | 3,800 | 6,130 | 1,600 | 2,580 |
| Middle Banning Canyon | 7,000 | 11,290 | 1,600 | 2,580 |
| Banning Bench | 3,500 | 5,650 | 1,600 | 2,580 |
| East Banning | 1,000 | 1,610 | 1,000 | 1,610 |
| West Banning | 4,450 | 7,180 | 4,450 | 7,180 |
| Beaumont | 8,700 | 14,030 | 8,700 | 14,030 |

Source: City of Banning.

Water Treatment & Regulatory Compliance

The City uses two simple methods for disinfection of the water circulated through the Water Enterprise. Chlorine tablets are pushed into the water stream by mechanical equipment and commercial grade chlorine bleach injected by pumps into the water stream at the various well sites. These methods of disinfection are in compliance with the water treatment requirements of the State of California Department of Health Services.

Currently, the Water Enterprise operates under Permit No. 3310006 issued by the State of California Department of Health Services on November 1, 1968, as amended (the "Water Permit"). The City is in full compliance with the regulations and requirements of the Water Permit. There are no known water quality or other issues concerning the Water Enterprise or the Water Permit that could cause financial hardship to the Water Enterprise.

Water Rates and Charges

Water Rates. Water rates have traditionally been set by the City Council and are not subject to review by any state or local government agency. Pursuant to the Water Lease, the City has agreed to take all steps necessary to validate the water rates determined by the Authority to be required in order to ensure collection of sufficient revenues to ensure that sufficient Net Water Revenues will be available for payment of the debt service on the Water Bonds when due. The most recent revision to the City's water rate structure was approved by the City Council on July 8, 2003 and includes water rates increases to become effective annually from 2004 to and including August 7, 2006. The most recent revised rates and charges pursuant to such rate structure became effective on August 7, 2005 and are summarized in the following table:

| Meter Size (Inches) | Customer Charge | Commodity Charge (Rate Plan 0-9 CCF) | Commodity Charge (Rate Plan 10-29 CCF) | Commodity Charge (Rate Plan 30+ CCF) |
|--------------------------------|----------------------------|---|---|---|
| 5/8 | \$ 15.97 | \$1.09 per CCF | \$1.28 per CCF | \$1.44 per CCF |
| ¾ | 15.97 | 1.09 per CCF | 1.28 per CCF | 1.44 per CCF |
| 1 | 24.42 | 1.09 per CCF | 1.28 per CCF | 1.44 per CCF |
| 1½ | 44.64 | 1.09 per CCF | 1.28 per CCF | 1.44 per CCF |
| 2 | 69.06 | 1.09 per CCF | 1.28 per CCF | 1.44 per CCF |
| 3 | 126.32 | 1.09 per CCF | 1.28 per CCF | 1.44 per CCF |
| 4 | 203.01 | 1.09 per CCF | 1.28 per CCF | 1.44 per CCF |
| 6 | 411.81 | 1.09 per CCF | 1.28 per CCF | 1.44 per CCF |
| 8 | 656.04 | 1.09 per CCF | 1.28 per CCF | 1.44 per CCF |

The Authority has also covenanted under the Water Indenture to have in effect rules and regulations requiring each consumer or customer connected with the Water Enterprise to pay the rates and charges applicable to the Water Enterprise and providing for the billing thereof and for a due date and a delinquency date for each bill. This covenant includes the obligation not to permit any entity or person (including governmental entities) to receive services from the Water Enterprise free of charge.

Water Connection Fee. The City charges a one-time connection fee for each new connection to the water system. Commencing on January 2005, the approved water connection fee being collected is \$7,232 per equivalent dwelling unit ("EDU"). For Fiscal Year 2004-05, the approved water connection fee was \$4,390 per EDU. The revised water connection fee takes into account the cost of acquiring rights to new water sources, constructing a treatment plant to treat said water and constructing other facilities to serve new users.

Water Frontage Fees. The City also collects a frontage fee equal to \$25.00 per foot to new development that abuts a street or easement that contains an existing pipe. The frontage fee is paid only by those developments for which prior owners have not paid a share of the infrastructure.

Demand and Sales

The following tables set forth past, current and projected water demand within the City by major categories, in acre-feet per year ("AFY") at five year intervals from 1990 to 2010, but including last year's usage. In 1990 water demand was 4,096 acre-feet. In the Fiscal Year ending ("FYE") June 30, 2005, water demand was 9,484 acre-feet. According to this table, for the last full year of operations, residential uses comprised approximately sixty percent (60%) of total consumption. However, as indicated on Table No. 5, below, the largest residential user of the Water Enterprise accounts only for thirty-seven tenths of one percent (0.37%) of the percent of consumption and only approximately thirty two tenths of one percent (0.32%) of the revenues during the same year.

TABLE NO. 4
HISTORIC AND PROJECTED WATER CONSUMPTION SALES
For FYE June 30,

| <u>Category</u> | <u>1990</u> | <u>1995</u> | <u>2000</u> | <u>2004</u> | <u>2005⁽¹⁾</u> | <u>2010⁽²⁾</u> |
|-----------------|--------------|--------------|--------------|--------------|---------------------------|---------------------------|
| | <u>(AFY)</u> | <u>(AFY)</u> | <u>(AFY)</u> | <u>(AFY)</u> | <u>(AFY)</u> | <u>(AFY)</u> |
| Residential | 2,319 | 3,431 | 4,745 | 5,263 | 5,724 | 8,031 |
| Commercial | 1,300 | 1,861 | 2,161 | 2,289 | 2,349 | 2,649 |
| Industrial | 0 | 77 | 83 | 136 | 151 | 226 |
| Public | 96 | 16 | 6 | 83 | 84 | 91 |
| Irrigation | 381 | 845 | 1,037 | 1,110 | 1,176 | 1,504 |
| Total | 4,096 | 6,230 | 8,032 | 8,881 | 9,484 | 12,501 |

Source: City of Banning

⁽¹⁾ Unaudited results.

⁽²⁾ Projected values.

The ten largest water users, which are listed in the table below, account for approximately 24 percent of the annual water consumption. During the last Fiscal Year, the largest private user, Sun Lakes, accounted for approximately 13 percent of the total usage. Sun Lakes is a development consisting of approximately 3,818 residences, one 18 hole championship golf course, one 18 hole executive course and other amenities. A large percentage of the water consumed by Sun Lakes is used for irrigation of the golf courses located within, and primarily serving, the development.

TABLE NO. 5
TEN LARGEST USERS OF WATER
12 Months Ended June 30, 2005⁽¹⁾

| Customers | Business Type | 12 Month Consumption (AFY) | Percent of System Consumption | Percent of System Revenue |
|---------------------------------|---------------------------|----------------------------------|----------------------------------|------------------------------|
| Sun Lakes | Commercial ⁽²⁾ | 1,218.36 | 12.85% | 10.94% |
| Banning Unified School District | Government | 269.76 | 2.84 | 2.40 |
| City of Banning | Government | 244.72 | 2.58 | 2.18 |
| Smith Correctional Facility | Government | 139.67 | 1.47 | 1.25 |
| Robertsons Ready Mix | Construction | 123.10 | 1.30 | 1.10 |
| High Valley Water District | Utility | 97.74 | 1.03 | .87 |
| Cal Trans | Government | 74.18 | .78 | .66 |
| Deutsch Company | Manufacturing | 64.56 | .68 | .58 |
| Mountain Air Mobile Estates | Residential | 35.48 | .37 | .32 |
| American Linen | Commercial | 35.17 | .37 | .31 |
| TOTAL | | 2,302.74 | 24.27% | 20.61% |

Source: City of Banning

⁽¹⁾ Unaudited results.

⁽²⁾ The residential customers within Sun Lakes are connected to the Water Enterprise on an individual basis and their respective consumption is not reflected on this table. The Sun Lakes development is a large customer of the Water Enterprise and its water consumption is primarily for the golf courses and other common areas.

The City's projected water supply for the current year and each five years through the year 2020 is shown in the following table.

TABLE NO. 6
PROJECTED WATER SUPPLY AND DEMAND COMPARISON BASED ON POPULATION GROWTH
For the FYE June 30,

| <u>Category</u> | <u>2005</u> <u>(AFY)</u> | <u>2010</u> <u>(AFY)</u> | <u>2015</u> <u>(AFY)</u> | <u>2020</u> <u>(AFY)</u> |
|--------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| Total Water Supply | 13,428 | 15,763 | 19,246 | 21,924 |
| Total Demand | 11,313 | 12,651 | 15,002 | 17,380 |
| Projected Supply Surplus | 2,115 | 3,112 | 4,244 | 4,544 |

Source: City of Banning.

Collection Procedures

Customers being provided water, wastewater and electric services by the City receive a single monthly bill. If payment is not received by the City on or prior to the 20th day following the mailing of the original bill, accounts are considered delinquent. Customers are given an extra 10 days grace period to pay their bills before a notice is posted on their door stating that if no payment is received within 48 hours service will be discontinued due to non-payment. The City does not usually post notices or discontinue service where the amounts due are less than \$30.00. If the City does post a notice, the customer's bill will reflect a \$12.00 notice charge. If the customer fails to pay by the date indicated in the notice and service to an account is discontinued, the customer must pay a re-connection fee to reestablish service.

TABLE NO. 7
HISTORIC WATER COLLECTIONS – METERED SALES
For the FYE June 30,

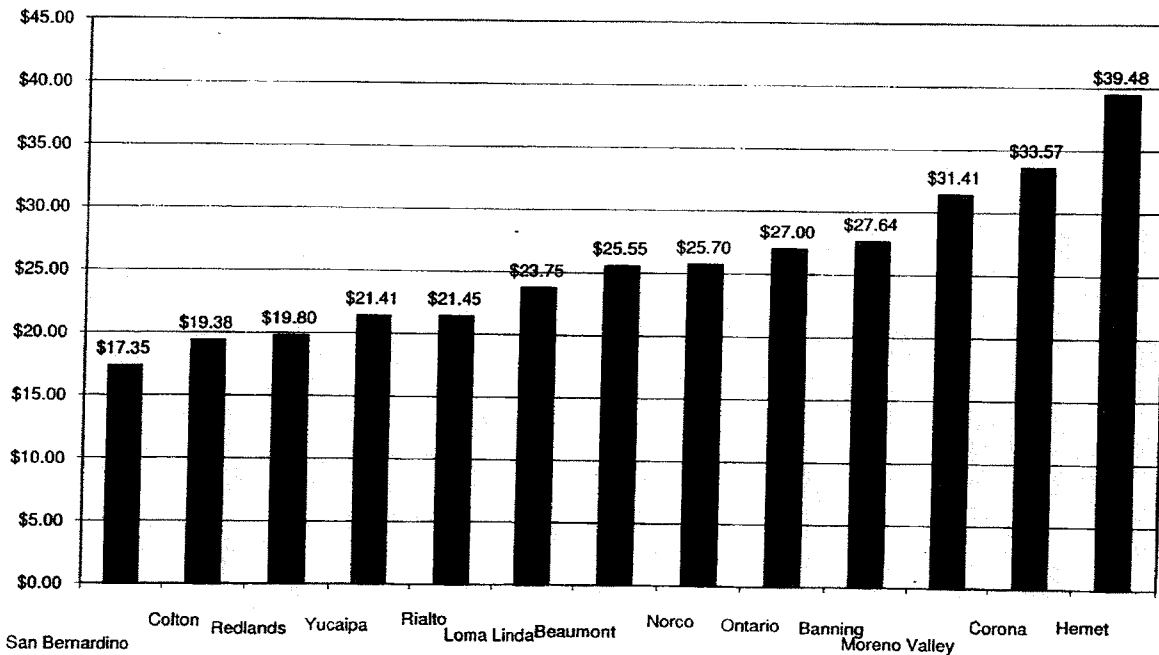
| <u>Category</u> | <u>2000</u> | <u>2001</u> | <u>2002</u> | <u>2003</u> | <u>2004</u> |
|-----------------|--------------------|--------------------|--------------------|--------------------|--------------------|
| Residential | \$2,674,054 | \$2,644,248 | \$2,872,410 | \$2,882,629 | \$3,727,369 |
| Commercial | 1,033,112 | 1,062,727 | 1,156,476 | 1,242,343 | 1,542,292 |
| Industrial | 32,449 | 32,715 | 32,524 | 41,021 | 60,675 |
| Public | 4,924 | 5,071 | 4,107 | 4,336 | 11,222 |
| Irrigation | 428,415 | 415,303 | 453,629 | 258,795 | 555,523 |
| Total | \$4,172,954 | \$4,160,064 | \$4,519,146 | \$4,429,124 | \$5,897,081 |

Source: City of Banning.

Table No. 7, above, reflects the amounts collected by the City only from metered sales of water from the Water Enterprise. In addition to metered charges, a customer's bill may reflect charges related to the operation of the water system that are not included in the amounts shown in the above table but which are reflected in the amounts shown as Water Sales in Table No. 8, below.

The following chart reflects the comparison of a typical monthly bill for consumers of the Water System and consumers in the surrounding communities:

Comparison of Monthly Water Charges 15 hcf per month for 5/8 meter



Source: City of Banning.

Historic Water Enterprise Operating Results

The following table presents the operating results of the Water Enterprise for the last five Fiscal Years. These results have been extracted from the City's financial statements. The City's auditor, Lance, Soll & Lunghard, LLP (the "Auditor"), has prepared the City's audited financial statements for FYE June 30, 2004, which include the operation of the Water Enterprise, are attached to this Official Statement as Appendix B and should be reviewed in their entirety.

In August 2003 the City started collecting frontage fees, which were misclassified as operating revenue on the City's 2004 financials. On September 13, 2005, the Auditor issued a letter to the City reflecting the reclassification of the frontage fees as Non-Operating Revenues under the miscellaneous income line. See "APPENDIX B – Audited Financial Statements of the City for FYE June 30, 2004."

The amounts reflected as Water Sales and Service Charges in the following table include metered sales, turn-on fees, reconnection fees, backflow charges and other operational charges that are regularly or from time to time invoiced to customers of the Water Enterprise. For the amounts concerning only metered water sales, please refer to Table 7, above. Table 8, below, shows a slight decrease in water sales revenue for FYE 2003 followed by a substantial increase of those same revenues for FYE 2004. The increase is primarily attributed to a water rate increase implemented by the City. The decrease in those revenues during FYE 2003 is attributed by the City to several factors, including the establishment of a water conservation program within the City. During 2002, the prolonged draught affecting Southern California led to declining water levels in the Banning Canyon. In late June, 2002 two critical pumps in the Banning Canyon shut off due to a power outage. The wells were inoperative for a few hours but were brought back in service as soon as power was restored. As a result of the power outage, some customers were left without water service for a few hours and others suffered a decrease in water pressure. To correct this situation and avoid similar situations in the future, the City installed one additional back-up generator in Banning Canyon, placed three additional wells in service by installing pumping facilities in existing but non-operational wells, installed an inter-tie with a neighboring water district to purchase water during emergency situations, installed a telemetry system on the Banning Canyon water wells to have effective operational controls. Additionally, the City increased water rates to offset operational costs and increased its connection fees to defray costs of capital improvements.

TABLE NO. 8
HISTORIC OPERATING RESULTS FOR THE WATER ENTERPRISE
(For FYE June 30)

| | <u>2001</u> | <u>2002</u> | <u>2003</u> | <u>2004</u> | <u>2005</u> ⁽¹⁾ |
|--|--------------------|--------------------|--------------------|----------------------------|----------------------------|
| Operating Revenue | | | | | |
| Water Sales and Service Charges | \$4,222,304 | \$4,585,223 | \$4,520,837 | \$6,014,318 ⁽²⁾ | \$6,353,367 |
| Connection Fees ⁽³⁾ | <u>49,879</u> | <u>84,359</u> | <u>157,149</u> | <u>47,407</u> | <u>67,871</u> |
| Total Operating Revenue | \$4,272,183 | \$4,669,582 | \$4,677,986 | \$6,061,725 | \$6,421,238 |
| Operating Expenses | | | | | |
| Salaries and Benefits | \$ 608,071 | \$ 709,332 | \$ 810,409 | \$ 874,646 | \$1,077,482 |
| Supplies and Services | 2,522,541 | 2,649,739 | 2,822,938 | 2,489,174 | 2,616,974 |
| Repairs and Maintenance | 2,237 | 3,441 | 1,958 | 3,894 | 4,146 |
| Amortization | 17,589 | 17,589 | 17,589 | 17,589 | 17,589 |
| Depreciation | <u>635,384</u> | <u>630,466</u> | <u>650,679</u> | <u>743,902</u> | <u>795,975</u> |
| Total Operating Expenses | \$3,785,822 | \$4,010,567 | \$4,303,573 | \$4,129,205 | \$4,512,166 |
| Operating Income (Loss) | \$486,361 | \$659,015 | \$374,413 | \$1,932,520 | \$1,909,072 |
| Non-Operating Revenue (Expenses) | | | | | |
| Interest Revenue | \$ 285,314 | \$ 175,370 | \$ 131,872 | \$ 63,454 | \$ 169,047 |
| Interest Expense | (434,360) | (380,947) | (368,225) | (354,644) | (340,205) |
| Gain (Loss) on Disposal of Fixed Assets | | (136,743) | | | |
| Miscellaneous Income ⁽⁴⁾ | <u>1,107,790</u> | <u>1,314,594</u> | <u>2,711,453</u> | <u>1,671,992</u> | <u>1,649,735</u> |
| Total Non-Operating Revenue (Expense) | \$ 958,744 | \$ 972,274 | \$2,475,100 | \$1,380,802 | \$1,478,577 |
| Income (Loss) Before Transfers | \$1,445,105 | \$1,631,289 | \$2,849,513 | \$3,313,322 | \$3,387,649 |

Source: City of Banning

⁽¹⁾ Unaudited results.

⁽²⁾ In August of 2003, the City implemented a 20% water rate increase which accounts for the increase in water sales revenue in FYE 2004.

⁽³⁾ Connection fees consist of the amount charged per meter installation. A customer pays \$185 for a standard residential meter. The connection fees do not include capital charges for connection fees. Those amounts are included in the miscellaneous income line, below.

⁽⁴⁾ Miscellaneous income includes certain miscellaneous items and connection fees for FYE 2001, 2002 and 2003, and commencing with FYE 2004 miscellaneous income also includes frontage fees. The proceeds of the frontage fees collected in 2004 were misclassified as Operating Revenue in the City's 2004 Financial Statements. On September 13, 2005, the City's auditor, Lance, Soll & Lunghard, LLP, issued a letter to the City reflecting the reclassification of the frontage fees as Non-Operating Revenues under the miscellaneous income line. See "APPENDIX B - Audited Financial Statements of the City for FYE June 30, 2004."

Projected Operating Results and Coverage Ratio for the Water Enterprise

The City's projected operating results and coverage ratio for the Water Enterprise for the next five Fiscal Years, calculated under the provisions of the Water Indenture, are set forth below. These projections are based on the City's judgment as to the most probable occurrence of certain future events. The assumptions and footnotes set forth beneath the table are material to the projections and variations in the assumptions could produce substantially different financial results. Actual revenues and expenses may vary materially from these projections.

TABLE NO. 9
PROJECTED OPERATING RESULTS AND COVERAGE RATIO FOR THE WATER ENTERPRISE
(For FYE June 30)

| | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> | <u>2010</u> |
|--|--------------------|--------------------|---------------------|---------------------|---------------------|
| Gross Water Revenues | | | | | |
| Water Sales | \$6,647,500 | \$7,080,000 | \$7,185,000 | \$7,311,000 | \$7,437,000 |
| Connection Fees | 50,000 | 50,000 | 50,000 | 50,000 | 50,000 |
| Interest Revenue | 153,600 | 160,000 | 160,000 | 160,000 | 160,000 |
| Miscellaneous Income ⁽¹⁾ | <u>2,060,000</u> | <u>2,450,000</u> | <u>2,750,000</u> | <u>2,906,200</u> | <u>3,112,000</u> |
| Total Gross Water Revenues | \$8,911,100 | \$9,740,000 | \$10,145,000 | \$10,427,200 | \$10,759,000 |
| Operation and Maintenance Expenses | | | | | |
| Salaries and Benefits ⁽²⁾ | \$1,327,659 | \$1,400,000 | \$1,500,000 | \$1,650,000 | \$1,815,000 |
| Supplies and Services ⁽³⁾ | 2,262,495 | 2,550,000 | 2,850,000 | 3,135,000 | 3,448,500 |
| Repairs and Maintenance | <u>19,500</u> | <u>20,000</u> | <u>21,000</u> | <u>21,000</u> | <u>21,000</u> |
| Total Water Operation and Maintenance Expenses ⁽⁴⁾ | \$3,609,654 | \$3,970,000 | \$4,371,000 | \$4,806,000 | \$5,284,500 |
| Net Water Revenues | \$5,301,446 | \$5,770,000 | \$5,774,000 | \$5,621,200 | \$5,474,500 |
| Debt Service | | | | | |
| Water Bonds ⁽⁵⁾ | \$619,843 | \$2,533,000 | \$2,298,663 | \$2,296,613 | \$2,298,775 |
| 1986 Certificates ⁽⁵⁾ | 236,550 | | | | |
| 1989 Water Certificates ⁽⁵⁾ | <u>75,600</u> | | | | |
| Total Debt Service | \$931,993 | \$2,533,000 | \$2,298,663 | \$2,296,613 | \$2,298,775 |
| Coverage Ratio | 5.69 | 2.28 | 2.51 | 2.45 | 2.38 |

Source: City of Banning

⁽¹⁾ Includes capital facilities fees and capital frontage fees. These projections are, however, net of any lease payments which were included in prior years in connection with the 1986 Certificates and the 1989 Water Certificates.

⁽²⁾ The City estimates, based on projected increases in salaries, retirement costs and related benefits, that the increase in Salaries and Benefits, from the previous Fiscal Year, will be approximately 23.2% in FYE 2006, 5.45% in FYE 2007, 7.1% in FYE 2008, 10% in FYE 2009 and 10% in FYE 2010.

⁽³⁾ The City estimates, based on a combination of estimated inflation costs and anticipated new programs for the Water Enterprise, that the cost of Supplies and Services will increase by approximately 9.5% during FYE 2006, 12.7% in FYE 2007, 11.7% in FYE 2008, 10% in FYE 2009 and 10% in FYE 2010. These projections are, however, net of any lease payments which were included in prior years in connection with the 1986 Certificates and the 1989 Water Certificates, which accounts for the decrease in the Supplies and Services related expenses relative to FYE 2005.

⁽⁴⁾ Pursuant to the Water Indenture, Water Operation and Maintenance Expenses do not include debt service or similar payments on Parity Debt, depreciation or amortization of intangibles or other bookkeeping entries of similar nature.

⁽⁵⁾ Actual debt service.

Additional assumptions:

1. FY 2006 projected 250 new permits and the capital facilities and/or frontage fees amounts anticipated to be collected are included in the Miscellaneous Income projections, above.
2. FY 2007 assumed a five percent (5%) water rate increase from FY 2006 water rate
3. FY 2007 assumed 250 new homes x \$35.00 consumption x 12 months = \$105,000
4. FY 2008 assumed 250 new homes x \$35.00 consumption x 12 months = \$105,000
5. FY 2009 assumed 300 new homes x \$35.00 consumption x 12 months = \$126,000
6. FY 2010 assumed 300 new homes x \$35.00 consumption x 12 months = \$126,000

THE WASTEWATER ENTERPRISE

General

Pursuant to the Wastewater Lease, the Wastewater Enterprise consists of all properties and assets, real and personal, tangible and intangible, of the wastewater system City now or hereafter existing, used or pertaining to the collection, transmission, treatment and disposal of sewage and wastewater, including all additions, extensions, expansions, improvements and betterments thereto, and equipments thereof; provided, however, that to the extent the City is not the sole owner of an asset or property, only the City's ownership interest in such asset or property shall be considered a part of its Wastewater Enterprise.

As of June 30, 2005, the Wastewater Enterprise included a total of approximately 10,690 connections, including approximately 10,057 residential service connections and approximately 633 industrial and commercial services connections. The collection system consists of approximately 110 miles of six to thirty inch sewers constructed of vitrified clay pipe (VCP) and pvc plastic materials.

Wastewater Treatment and Regulatory Compliance

Sewerage flows collected by the existing sewer collection system are treated at a rural 126 acre City-owned treatment plant located on Charles Street and adjacent to Smith Creek east of Hathaway Street. The City has operated a treatment plant at this site since 1925, incrementally expanding various process components as necessary to keep pace with development. The plant facilities have a design capacity of 3.6 MGD for secondary wastewater treatment with the present flows at an average of 2.9 MGD.

The treatment processes includes headworks/vortex-type grit chamber, primary clarifiers, fixed-media secondary treatment, high-rate solids digestion, dewatering and chemical applications for disinfection, trickling filters, secondary clarification, percolation ponds, and sludge drying beds. The secondary treated effluent from the plant is percolated into the Banning East Groundwater Sub-basin for recharge and replenishment of the basin.

The City currently contracts with a private company, United Water Services, Inc., a California corporation, for the operation and maintenance of the wastewater treatment plant facilities and five lift stations. The contract provides for the payment to the company of a flat monthly fee, currently in the amount of approximately \$46,000, which is adjusted on July 1st of each year to reflect changes in the consumer price index for the Los Angeles-Long Beach metropolitan area. The contract is a 10 year contract currently due to expire on September 30, 2013. The contract can be renewed if written notice of intent to renew is given at least 120 days prior to the expiration date. The contract may be terminated at the option of either party upon 120 days notice.

The WWTP and Wastewater Collection and Disposal Systems operate under Board Order No. 01-022 issued on May 9, 2001, by the California Regional Water Quality Control Board – Colorado River Basin Region for waste discharge requirements. There are no known compliance issues or citations affecting the operation of the WWTP, which the City believes to be operating within the permitted conditions and provisions of the Board Order or discharge requirements.

Wastewater Rates and Charges

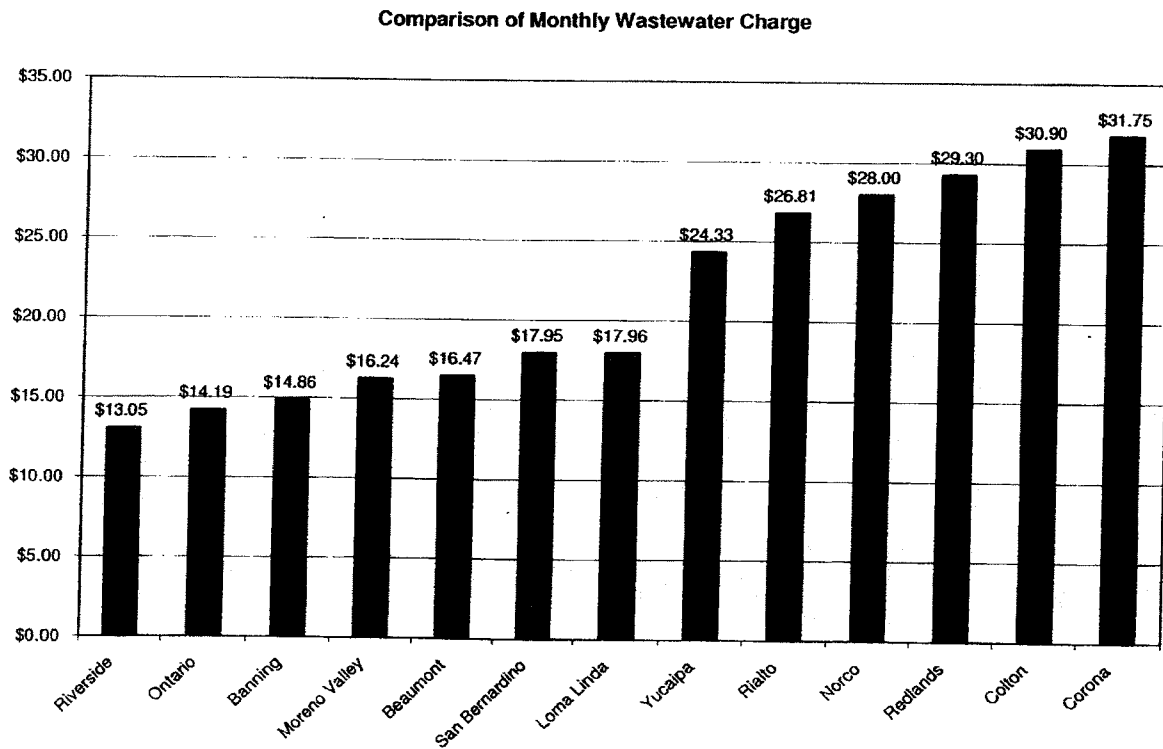
The Wastewater Enterprise rates have traditionally been set by the City and are not subject to review by any other governmental agency. In the past, the wastewater rates have been enacted based upon the recommendation of the City's director of public works or a private consultant. Pursuant to the Wastewater Lease, the City has covenanted to assist the Authority to set and collect wastewater rates in an

amount sufficient to ensure that enough Net Wastewater Revenues will be available for the payment of debt service on the Wastewater Bonds when due.

The Authority has also covenanted under the Wastewater Indenture to have in effect rules and regulations requiring each consumer or customer connected to the Wastewater Enterprise to pay the rates and charges applicable to the Wastewater Enterprise and providing for the billing thereof and for a due date and a delinquency date for each bill. This covenant includes the obligation not to permit any entity or person (including governmental entities other than the City) to receive services from the Wastewater Enterprise free of charge.

The approved charge for sewer service, established in June of 2003 and effective since August 7, 2003, is \$12.86 per month per EDU. The City also collects a \$2.00 tertiary treatment facilities surcharge per month per EDU. In addition to those service charges, the City collects a connection fee for each new connection to the Wastewater Enterprise. The connection fee approved by the City in December of 2004 and currently in effect is \$2,786.00. The City or the Authority may determine to increase this amount as necessary to cover the reasonable costs of the sewer service. In addition, upon City Council approval, the City may charge a special frontage fee or other fees to certain parcels receiving special services.

The following chart reflects the comparison of a typical monthly bill for consumers of the Wastewater Enterprise and consumers in the surrounding communities:



Source: City of Banning.

Demand and Users

The following tables present a summary of the connections of the Wastewater Enterprise for the most recent five Fiscal Years and the City's projection of such connections for the current and next City's projection of meter connections for the next two Fiscal Years.

TABLE NO. 10
HISTORIC AND PROJECTED WASTEWATER CONNECTIONS

| <u>FYE June 30</u> | <u>Number of Connections</u> | <u>Percent Increase</u> |
|---------------------|------------------------------|-------------------------|
| 2001 | 9,070 | 3.3% |
| 2002 | 9,558 | 5.4 |
| 2003 | 10,054 | 5.2 |
| 2004 | 10,500 | 4.4 |
| 2005 | 10,690 | 1.8 |
| 2006 ⁽¹⁾ | 10,990 | 2.8 |
| 2007 ⁽¹⁾ | 11,290 | 2.7 |

Source: City of Banning.

⁽¹⁾ Projected.

The five largest users of the Wastewater Enterprise account for approximately nineteen percent (19%) of the total revenues of the Wastewater Enterprise. As shown on the table below, with the exception of the three largest users, no single user accounts for more than one percent (1%) of the revenue of the Water Enterprise. In addition, the percent revenue derived from any single user drops off rapidly, with the fifth largest user accounting for only fifty-five tenths of one percent (.55%) of total revenues. The following are the top five users of the Wastewater Enterprise and no other user's use equals or exceeds the use of San Gorgonio Memorial Hospital:

TABLE NO. 11
FIVE LARGEST USERS OF THE WASTEWATER SYSTEM
12 Months Through June 30, 2004

| <u>Customer</u> | <u>Business Type</u> | <u>Annual Revenue</u> | <u>Percent of Total Revenue</u> |
|---------------------------------|----------------------|-----------------------|---------------------------------|
| Deutsch Company | Manufacturing | \$164,425 | 6.60% |
| Smith Correctional Facility | Government | 144,295 | 5.79 |
| American Linen | Commercial | 108,775 | 4.70 |
| Banning Unified School District | Governmental | 21,933 | .94 |
| San Gorgonio Memorial Hospital | Health | 12,839 | .55 |
| TOTAL | | \$452,267 | 18.58% |

Source: City of Banning.

Collection Procedures

Customers being provided water, wastewater and electric services by the City receive a single monthly bill. See "THE WATER ENTERPRISE – Collection Procedures."

Historic Wastewater Enterprise Operating Results

The following table is a summary of the operating results of the Wastewater Enterprise for the last five Fiscal Years. These results have been extracted from the City's financial statements. This table has not been reviewed by the Auditor. The City's audited financial statement for FYE June 30, 2004, which includes the operations of the Wastewater Enterprise, is attached to this Official Statement as Appendix B and should be reviewed in its entirety.

TABLE NO. 12
HISTORIC OPERATING RESULTS FOR THE WASTEWATER ENTERPRISE
(For FYE June 30)

| | <u>2001</u> | <u>2002</u> | <u>2003</u> | <u>2004</u> | <u>2005</u> |
|---|--------------------|--------------------|--------------------|------------------------------|--------------------|
| Operating Revenues | | | | | |
| Wastewater Sales and Service Charges | <u>\$1,922,705</u> | <u>\$2,013,111</u> | <u>\$2,066,636</u> | <u>\$2,239,220</u> | <u>\$2,332,396</u> |
| Total Operating Revenues | \$1,922,705 | \$2,013,111 | \$2,066,636 | \$2,239,220 | \$2,332,396 |
| Operating Expenses | | | | | |
| Salaries and Benefits | 64,872 | 68,541 | 86,689 | 102,373 | 111,149 |
| Supplies and Services | 1,422,870 | 1,333,969 | 1,360,594 | 1,417,840 | 1,417,068 |
| Repairs and Maintenance | 25,385 | 44,024 | 49,169 | 27,683 | 34,482 |
| Amortization | 5,473 | 5,473 | 5,473 | 5,473 | 5,473 |
| Depreciation | <u>749,564</u> | <u>817,579</u> | <u>822,484</u> | <u>827,079</u> | <u>831,579</u> |
| Total Operating Expenses | \$2,268,164 | \$2,269,586 | \$2,324,409 | \$2,380,448 | \$2,399,751 |
| Operating Income (Loss) | (\$345,459) | (\$256,475) | (\$257,773) | (\$141,228) | (67,355) |
| Non-Operating Revenue (Expenses) | | | | | |
| Interest Revenue | \$ 286,047 | \$ 201,305 | \$ 158,904 | \$ 94,838 | \$ 221,315 |
| Interest Expense | (206,435) | (416,230) | (302,512) | (278,794) | (266,600) |
| Gain (Loss) on Disposal of Fixed Assets | | (17,348) | | | |
| Miscellaneous Income ⁽¹⁾ | 783,335 | 995,304 | 2,453,129 | 950,201 ⁽²⁾ | 693,004 |
| Miscellaneous Income – surcharge ⁽²⁾ | | | | <u>290,015⁽²⁾</u> | <u>361,482</u> |
| Total Non-Operating Revenue (Expense) | \$ 862,947 | \$ 763,031 | \$2,309,521 | \$1,056,260 | \$1,009,201 |
| Income (Loss) Before Transfers | \$517,488 | \$506,556 | \$2,051,748 | \$915,032 | \$941,846 |

Source: City of Banning

⁽¹⁾ Miscellaneous income includes items such as insurance proceeds, capital frontage fees and connection fees.

⁽²⁾ Commencing in FY 2003-04, the City collects surcharge amounts to fund costs related to the conversion of the treatment plant to a tertiary treatment facility. Said amounts are shown separately on this Table No. 12, but are included in the Miscellaneous Income line of the City's audited financials. The proceeds of the surcharge collected in 2004 were misclassified as Operating Revenue in the City's 2004 Financial Statements. On September 13, 2005, the City's auditor, Lance, Soll & Lunghard, LLP, issued a letter to the City reflecting the reclassification of the proceeds of the surcharge as Non-Operating Revenues under the miscellaneous income line. See "APPENDIX B – Audited Financial Statements of the City for Fiscal Year Ended June 30, 2004."

Projected Operating Results and Coverage Ratio for the Wastewater Enterprise

The City's projected operating results and coverage ratio for the Wastewater Enterprise for the next five Fiscal Years, calculated under the provisions of the Wastewater Indenture, are set forth below. These projections are based on the City's judgment as to the most probable occurrence of certain future events. The assumptions and footnotes set forth beneath the table are material to the projections and variations in the assumptions could produce substantially different financial results. Actual revenues and expenses may vary materially from these projections.

TABLE NO. 13
PROJECTED OPERATING RESULTS AND COVERAGE RATIO FOR THE
WASTEWATER ENTERPRISE
(For FYE June 30)

| | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> | <u>2010</u> |
|--|--------------------|--------------------|--------------------|--------------------|--------------------|
| Gross Wastewater Revenues | | | | | |
| Wastewater Charges | \$2,427,000 | \$2,465,500 | \$2,504,000 | \$2,558,600 | \$2,613,200 |
| Interest Revenue | 211,481 | 215,000 | 215,000 | 215,000 | 215,000 |
| Miscellaneous Income ⁽¹⁾ | 725,000 | 757,200 | 790,000 | 968,300 | 1,056,100 |
| Miscellaneous Income - Surcharge ⁽¹⁾ | <u>367,500</u> | <u>373,500</u> | <u>379,500</u> | <u>386,700</u> | <u>393,900</u> |
| Total Gross Wastewater Revenues | \$3,730,981 | \$3,811,200 | \$3,888,500 | \$4,128,600 | \$4,278,200 |
| Wastewater Operation and Maintenance Expenses | | | | | |
| Salaries and Benefits ⁽²⁾ | \$ 295,347 | \$ 350,000 | \$ 395,000 | \$ 434,500 | \$ 477,950 |
| Supplies and Services ⁽³⁾ | 1,273,616 | 1,369,137 | 1,471,822 | 1,619,005 | 1,780,905 |
| Repairs and Maintenance | <u>55,500</u> | <u>60,000</u> | <u>70,000</u> | <u>70,000</u> | <u>70,000</u> |
| Total Wastewater Operation and Maintenance Expenses⁽⁴⁾ | \$1,624,463 | \$1,779,137 | \$1,936,822 | \$2,123,505 | \$2,328,855 |
| Net Wastewater Revenues | \$2,106,518 | \$2,032,063 | \$1,951,678 | \$2,005,095 | \$1,949,345 |
| Debt Service | | | | | |
| SRF Loan ⁽⁵⁾ | \$ 304,300 | \$ 304,300 | \$ 304,300 | \$ 304,300 | \$ 304,300 |
| Wastewater Bonds ⁽⁵⁾ | 108,414 | 561,050 | 527,976 | 525,034 | 521,741 |
| 1989 Wastewater Certificates ⁽⁵⁾ | <u>75,800</u> | | | | |
| Total Debt Service | \$488,514 | \$865,350 | \$832,276 | \$829,334 | \$826,041 |
| Coverage Ratio | 4.31 | 2.35 | 2.34 | 2.42 | 2.36 |

Source: City of Banning

⁽¹⁾ Includes capital frontage fees. These projections are, however, net of any lease payments that were included in prior years in connection with the 1989 Wastewater Certificates.

⁽²⁾ The City estimates, based on projected increases in salaries, retirement costs, health care costs and related benefits, that the increase in Salaries and Benefits, from the previous Fiscal Year, will be approximately 18.5% in FYE 2007, 12.9% in FYE 2008, 10% in FYE 2009 and 10% in FYE 2010. In FYE 2006, the increase is estimated at approximately 166% taking into account, in addition to those other costs, the direct funding of one additional employee. However a significant portion of the increase is offset by a reduction in operating transfers to other funds.

⁽³⁾ The City estimates, based on a combination of estimated inflation costs and anticipated new programs for the Wastewater Enterprise, that the cost of Supplies and Services will increase by approximately 25% during FYE 2006, 7.57% in FYE 2007, 7.57% in FYE 2008, 10% in FYE 2009 and 10% in FYE 2010. These projections are, however, net of any lease payments that were included in prior years in connection with the 1989 Wastewater Certificates, which accounts for the decrease in the Supplies and Services related expenses relative to FYE 2005.

⁽⁴⁾ Pursuant to the Wastewater Indenture, Wastewater Operation and Maintenance Expenses do not include debt service or similar payments on Parity Debt, depreciation or amortization of intangibles or other bookkeeping entries of similar nature.

⁽⁵⁾ Actual approximate debt service. For scheduled debt service payments on the SRF Loan, refer to the appropriate table under the Section "DEBT SERVICE" herein.

Additional assumptions:

1. Proceeds of the Wastewater Bonds will be used to build a portion of the tertiary improvements. Therefore, Miscellaneous Income includes amounts collected as a surcharge imposed for the purpose of constructing a tertiary wastewater treatment plant.
2. To project FY 2007 and FY 2008 wastewater charges, the City assumed that 250 new homes would receive service for 12 months at a monthly charge of \$12.86 per home, resulting in an increase of \$38,500 over the prior year.

FINANCIAL STATEMENTS

Financial information regarding the Water Enterprise and the Wastewater Enterprise for the fiscal year ended June 30, 2004, is set forth in a portion of the City's audited financial statements included in

Appendix B hereto. The City's audited financial statements have been audited by Lance Soll & Lunghard LLP, Certified Public Accountants (the "Auditor"), as stated in the financial statements included as Appendix B hereto. On September 13, 2005, the Auditor provided the City with a letter stating that the amounts collected in frontage fees in connection with the Water System and the proceeds of a surcharge collected for costs related to the conversion of a plant into a tertiary treatment plant for the wastewater system had been misclassified as Operating Income in the City's audited financials for Fiscal Year 2004. Together with its September 13, 2005 correspondence, the Auditor provided the City with corrected Statements of Revenues, Expenses and Charges in Fund Net Assets Proprietary Funds. See "Appendix B - Audited Financial Statements of the City for Fiscal Year Ended June 30, 2004". The City has not requested nor did the City obtain permission from the Auditor to include the audited financial statements as an appendix to this Official Statement. Accordingly, the Auditor has not performed any post-audit work on the financial statements. The City is not obligated in any manner to pay principal of or interest on the Bonds or to cure any delinquency or default on the Bonds.

BONDOWNERS' RISKS

PURCHASE OF THE BONDS INVOLVES CERTAIN RISKS. EACH PROSPECTIVE INVESTOR IN THE BONDS IS ENCOURAGED TO READ THIS OFFICIAL STATEMENT IN ITS ENTIRETY. PARTICULAR ATTENTION SHOULD BE GIVEN TO THE FACTORS DESCRIBED BELOW WHICH, AMONG OTHERS, COULD AFFECT THE MARKET PRICE OF THE BONDS TO AN EXTENT THAT CANNOT BE DETERMINED. HOWEVER, THEY DO NOT PURPORT TO BE AN EXHAUSTIVE LISTING OF RISKS AND OTHER CONSIDERATIONS WHICH MAY BE RELEVANT TO AN INVESTMENT IN THE BONDS. IN ADDITION, THE ORDER IN WHICH THE FOLLOWING FACTORS ARE PRESENTED IS NOT INTENDED TO REFLECT THE RELATIVE IMPORTANCE OF ANY SUCH RISKS.

Bonds are Limited Obligations

NEITHER THE BONDS NOR THE PAYMENT OF THE PRINCIPAL OR ANY PART THEREOF NOR ANY INTEREST THEREON CONSTITUTE A DEBT, LIABILITY OR OBLIGATION OF THE CITY, THE AGENCY, THE COUNTY OF RIVERSIDE, THE STATE OF CALIFORNIA OR ANY OF ITS POLITICAL SUBDIVISIONS, OTHER THAN THE AUTHORITY, AND NONE OF THE CITY, THE AGENCY, SAID COUNTY, SAID STATE OR ANY OF ITS POLITICAL SUBDIVISIONS (OTHER THAN THE AUTHORITY) IS LIABLE THEREFOR.

No Liability of the Authority to the Bondowners

Except as expressly provided in the Indentures, the Authority will not have any obligation or liability to the Bondowners with respect to the observance or performance of other agreements, conditions, covenants and terms required to be observed or performed by the City under the Water Lease, the Wastewater Lease, the Water Management Agreement, the Wastewater Management Agreement or any related documents or with respect to the performance by the Trustee of any duty required to be performed by it under the respective Indentures.

Limitations on Remedies Available to Owners of the Bonds and the Trustee

The enforceability of the rights and remedies of the Owners of the Bonds and the Trustee, and the obligations incurred by the City, the Authority, and each Enterprise, may be subject to the following: the federal bankruptcy code and applicable bankruptcy, insolvency, reorganization, moratorium or similar laws relating to or affecting the enforcement of creditors' rights generally, now or hereafter in effect; usual equity principles which may limit the specific enforcement under state law of certain remedies; the exercise by the United States of America of the powers delegated to it by the Federal Constitution; and

the reasonable and necessary exercise, in certain exceptional situations, of the police power inherent in the sovereignty of the State of California and its governmental bodies in the interest of serving a significant and legitimate public purpose. Bankruptcy proceedings, or the exercise of powers by the federal or state government, if initiated, could subject the Owners of the Bonds to judicial discretion and interpretation of their rights in bankruptcy or otherwise, and consequently may entail risks of delay, limitations or modification of their rights. Remedies may be limited since the Water Enterprise and the Wastewater Enterprise serve essential public purposes.

Limited Recourse on Default

If the Authority defaults on its obligations to make debt service payments on the Bonds, pursuant to either Indenture, the Trustee, as assignee of the Authority, has the right to accelerate the total unpaid principal amount of the Bonds. However, in the event of a default and such acceleration, there can be no assurance that the Trustee will have sufficient moneys available for payment of the Water Bonds or the Wastewater Bonds, as applicable.

Loss of Tax Exemption

As discussed under the caption "TAX EXEMPTION" herein, interest with respect to the Bonds could fail to be excluded pursuant to section 103(a) of the Code from the gross income of the owners thereof for purposes of federal income taxation retroactive to the date of the execution and delivery of the Bonds as a result of future acts or omissions of the Authority in violation of its covenants contained in the applicable Indenture. Should such an event of taxability occur, the Bonds are not subject to special redemption or any increase in interest rate, and will remain outstanding until maturity or until redeemed under one of the redemption provisions contained in the applicable Indenture.

Secondary Market

There can be no guarantee that there will be a secondary market for the Bonds or, if a secondary market exists, that the Bonds can be sold for any particular price. Occasionally, because of general market conditions or because of adverse history or economic prospects connected with a particular issue, secondary marketing practices in connection with a particular issue are suspended or terminated. Additionally, prices of issues for which a market is being made will depend upon then prevailing circumstances. Such prices could be substantially different from the original purchase price.

Forecasts

Although the Authority and the City believe that the projections herein of future operating results of the Water Enterprise and the Wastewater Enterprise are reasonable, there can be no assurance that operating results will match the projections due to changes in general economic conditions and similar factors. In addition, the Water Enterprise and the Wastewater Enterprise and economic development within the service area of the City are subject to federal, State and local regulations. There can be no assurance that the Water Enterprise or the Wastewater Enterprise will not be adversely affected by future economic conditions, governmental policies or other factors beyond the control of the City and the Authority.

Enterprise Expenses And Collections

There can be no assurance that the expenses for either the Water Enterprise or the Wastewater Enterprise will remain at the levels described in this Official Statement. Changes in technology, energy or other expenses would reduce the Net Water Revenues or the Net Wastewater Revenues and could require substantial increases in the applicable rates or charges. Such rate increases could increase the

likelihood of nonpayment, and could also decrease demand. Although the Authority has covenanted to fix, prescribe, revise and collect rates, fees and charges of the Water Enterprise and the Wastewater Enterprise at certain levels, there can be no assurance that such amounts will be collected in the amounts and at the time necessary to make timely payments with respect to the Water Bonds or the Wastewater Bonds, as applicable.

Casualty Risk; Earthquakes

Any natural disaster or other physical calamity, including earthquake, may have the effect of reducing Revenues through damage to the Water Enterprise or the Wastewater Enterprise and/or adversely affecting the economy of the surrounding area. The Indentures, the Water Lease and the Wastewater Lease require the Authority to maintain insurance or self-insurance, but only if and to the extent available at reasonable cost from reputable insurers, and the Authority is not expressly required to provide earthquake insurance. The State of California, including the Riverside County area, is a seismically active region. In the event of total loss of either, the Water Enterprise or Wastewater Enterprise, there can be no assurance that insurance proceeds will be adequate to redeem all outstanding Water Bonds or Wastewater Bonds, as applicable, or that losses in excess of the insured amount will not occur.

California Constitution Article XIIC and Article XIID

On November 5, 1996, the voters of the State approved "Proposition 218", known as the "Right to Vote on Taxes Act." Proposition 218 added Articles XIIC and XIID to the State Constitution, which contain a number of provisions affecting the ability of the Authority to impose and collect both existing and future fees and charges. Such provisions could adversely affect the financial condition of the Water Enterprise or the Wastewater Enterprise and the ability of the Authority to comply with covenants under the Water Indenture, the Wastewater Indenture, the Water Lease or the Wastewater Lease and/or its ability to pay debt service on the Water Bonds or the Wastewater Bonds, as applicable. In such event, there can be no assurance that remedies will be available to fully protect the interests of Bondowners.

Article XIID contains several new provisions affecting the ability of local governments to impose or increase "fees" and "charges," defined for purposes of Article XIID to mean "any levy other than an ad valorem tax, a special tax, or an assessment, imposed by a local government upon a parcel or upon a person as an incident of property ownership, including a user fee or charge for a property related service." "Property related service" means a public service having a direct relationship to property ownership (which term includes tenancies where tenants are directly liable to pay the assessment, fee or charge in question). All new and existing property related fees and charges must conform to requirements prohibiting, among other things, fees and charges which (i) generate revenues exceeding the funds required to provide the property related service, (ii) are used for any purpose other than those for which the fees and charges are imposed, (iii) with respect to any parcel or person exceed the proportional cost of the service attributable to the parcel, (iv) are for a service not only used by, or immediately available to, the owner of the property in question, or (v) are used for general governmental services, including police, fire, ambulance or library services, where the service is available to the public at large in substantially the same manner as it is to property owners.

The Authority does not believe that its water and sewer charges are fees or charges imposed as an incident of property ownership within the meaning of Article XIID, although no assurance can be given that a court would not determine otherwise. The Authority believes that the water and sewer charges, even if considered a "fee" or "charge" for purposes of Article XIID, would satisfy all of these requirements. However, in any legal action contesting the validity of a fee or charge, the Authority would have the burden of proving compliance with Article XIID, and no assurance can be given that a court would not determine otherwise. Before any property related fee or charge may be imposed or increased,

written notice must be given to the record owner of each parcel of land affected by such fee or charge. The Authority must then hold a hearing upon the proposed imposition or increase, and if written protests against the proposal are presented by a majority of the owners of the identified parcels, the Authority may not impose or increase the fee and charge, including any increase in its water and sewer charges.

Article XIID states that, beginning July 1, 1997, all "fees" or "charges" must comply with its provisions. It is unclear how the provisions of Article XIID will be applied to fees or charges established prior to such date. The Authority does not plan to conduct any new hearings, elections or other proceedings with respect to any of its existing fees or charges for water and sewer service.

In addition to the provisions described above, Article XIIC removes limitations on the initiative power in matters of local taxes, assessments, fees and charges. Consequently, the voters within the City's jurisdiction could, by future initiative, repeal, reduce or prohibit the future imposition or increase of any local tax, assessment, fee or charge. "Assessment," "fee" and "charge" are not defined in Article XIIC and it is unclear whether the definitions of such terms contained in Article XIID (which are generally property related as described above) apply with respect to Article XIIC. No assurance can be given that such voters will not, in the future, approve initiatives which repeal, reduce or prohibit the future imposition or increase of assessments, fees or charges. The Authority believes that the initiative power cannot be used to alter covenants in the Indenture or either the Water Lease or Wastewater Lease concerning the imposition of the Authority's water and sewer charges or reduce or repeal such charges to the extent that the Authority could not meet its obligations.

The interpretation and application of Article XIIC and Article XIID will ultimately be determined by the courts with respect to a number of the matters discussed above, and it is not possible to predict the outcome of such determination.

The foregoing discussion of Article XIIC and Article XIID should not be considered an exhaustive or authoritative treatment of the issues. The Authority and the City do not expect to be in a position to control the consideration or disposition of these issues and cannot predict the timing or outcome of any judicial or legislative activity in this regard. Interim rulings, final decisions, legislative proposals and legislative enactments may all affect the impact of Article XIIC and Article XIID on the Bonds as well as the market for the Bonds. Legislative and court calendar delays and other factors may prolong any uncertainty regarding the effects of Article XIIC and Article XIID.

In February 2004, in *Richmond et al. v. Shasta Community Services District* the California Supreme Court upheld a Court of Appeal decision that water connection fees were not property related fees and charges subject to Article XIID. Subsequently, the Fourth District Court of Appeal held, in *Bighorn-Desert View Water Agency v. Beringson* that usage-based water rates are not property related as provided under Proposition 218, or, if property related, then exempt from Proposition 218 as fees or charges for water services. On October 27, 2004, the California Supreme Court granted a petition for review of the *Bighorn* decision. It is unclear at this time what impact these and future court decisions may have on the applicability of Proposition 218 to fees and charges collected by the Authority.

The ability of the Authority to comply with the covenants under the Water Indenture, Wastewater Indenture, Water Lease and Wastewater Lease and to generate Net Water Revenues and Net Wastewater Revenues sufficient to insure that an adequate amount of Net Water Revenues and Net Wastewater Revenues are available pay debt service on the Bonds in a timely manner may be adversely affected by actions and events outside of the control of the Authority and may be adversely affected by actions taken (or not taken) by voters, property owners, taxpayers or payers of assessments, fees and charges. Furthermore, any remedies available to the Bondowners upon the occurrence of an Event of Default under the Indenture are in many respects dependent upon judicial actions which are often subject to discretion and delay and could prove both expensive and time consuming to obtain.

Voter Initiatives -- State Constitutional Amendment

California's voter initiative process allows measures which qualify for the ballot to be approved or disapproved by voters in a State of California statewide election. From time to time initiative measures could be adopted which adversely affect the ability of the Authority to generate Net Water Revenues or Net Wastewater Revenues.

FORWARD-LOOKING STATEMENTS

This Official Statement contains certain "forward-looking statements" concerning the Authority's operations, the Water Enterprise, the Wastewater Enterprise, and the operations, performance and financial condition of the City, the Authority, the Water Enterprise and the Wastewater Enterprise, including their future economic performance, plans and objectives and the likelihood of success in developing and expanding. These statements are based upon a number of assumptions and estimates which are subject to significant uncertainties, many of which are beyond the control of the Authority and City. The words "may," "would," "could," "will," "expect," "anticipate," "believe," "intend," "plan," "estimate" and similar expressions are meant to identify these forward-looking statements. Results may differ materially from those expressed or implied by these forward-looking statements.

UNDERWRITING

Kinsell, Newcomb & De Dios, Inc., the Underwriter, has agreed to purchase the Water Bonds at the purchase price of \$36,759,089.15, representing the aggregate principal amount of the Water Bonds, plus original issue premium of \$1,516,074.15 and less an Underwriter's discount of \$391,985.00, and to re-offer the Water Bonds pursuant to the terms and conditions set forth on the inside cover page of this Official Statement. The Underwriter will be obligated to take and pay for all of the Water Bonds if any Water Bond is purchased.

The Underwriter, has also agreed to purchase the Wastewater Bonds at the purchase price of \$6,895,407.75, representing the aggregate principal amount of the Wastewater Bonds, less original issue discount of \$126,492.25 and less an Underwriter's discount of \$78,100.00, and to re-offer the Wastewater Bonds pursuant to the terms and conditions set forth on the inside cover page of this Official Statement. The Underwriter will be obligated to take and pay for all of the Wastewater Bonds if any Wastewater Bond is purchased.

The Underwriter reserves the right to join with dealers and other underwriters in offering the Bonds to the public. The Underwriter may offer and sell the Bonds to the certain dealers (including dealers depositing Bonds into investment trusts) at prices lower than the public offering prices, and such dealers may realow any such discounts on sales to other dealers.

CERTAIN LEGAL MATTERS

Legal matters in connection with the authorization, execution, delivery and sale of the Bonds are subject to the approval of Fulbright & Jaworski L.L.P., Los Angeles, California, Bond Counsel. The form of the approving opinion of Bond Counsel is attached hereto as Appendix F. Burke, Williams & Sorensen, LLP, San Diego, California, is serving as Disclosure Counsel to the Authority. Certain legal matters will be passed upon for the City and the Authority by the City Attorney.

TAX EXEMPTION

The Internal Revenue Code of 1986 (the "Code"), imposes certain requirements that must be met subsequent to the issuance and delivery of the Bonds for interest thereon to be and remain excluded

pursuant to section 103(a) of the Code from the gross income of the owners thereof for federal income tax purposes. Noncompliance with such requirements could cause the interest on the Bonds to be included in the gross income of the owners thereof for federal income tax purposes retroactive to the date of issuance of the Bonds. The Authority and the City have covenanted to maintain the exclusion of the interest on the Bonds from the gross income of the owners thereof for federal income tax purposes.

In the opinion of Fulbright & Jaworski L.L.P., Bond Counsel, under existing law interest on the Bonds is exempt from personal income taxes of the State of California and, assuming compliance with the aforementioned covenant, interest on the Bonds is excluded pursuant to section 103(a) of the Code from the gross income of the owners thereof for federal income tax purposes. Bond Counsel is also of the opinion that, assuming compliance with the aforementioned covenant, the Bonds are not "specified private activity bonds" within the meaning of section 57(a)(5) of the Code and, therefore, the interest on the Bonds will not be treated as an item of tax preference for purposes of computing the alternative minimum tax imposed by section 55 of the Code. The receipt or accrual of interest on the Bonds owned by a corporation may affect the computation of its alternative minimum taxable income, upon which the alternative minimum tax is imposed, to the extent that such interest is taken into account in determining the adjusted current earnings of that corporation (75 percent of the excess, if any, of such adjusted current earnings over the alternative minimum taxable income being an adjustment to alternative minimum taxable income (determined without regard to such adjustment or to the alternative tax net operating loss deduction)).

To the extent that a purchaser of a Bond acquires that Bond at a price that exceeds the aggregate amount of payments (other than payments of qualified stated interest within the meaning of section 1.1273-1 of the Treasury Regulations) to be made on the Bonds (determined, in the case of a callable Bond, under the assumption described below), such excess will constitute "bond premium" under the Code. Section 171 of the Code, and the Treasury Regulations promulgated thereunder, provide generally that bond premium on a tax-exempt obligation must be amortized on a constant yield, economic accrual, basis; the amount of premium so amortized will reduce the owner's basis in such obligation for federal income tax purposes, but such amortized premium will not be deductible for federal income tax purposes. In the case of a purchase of a Bond that is callable, the determination whether there is amortizable bond premium, and the computation of the accrual of that premium, must be made under the assumption that the Bond will be called on the redemption date that would minimize the purchaser's yield on the Bond (or that the Bond will not be called prior to maturity if that would minimize the purchaser's yield). The rate and timing of the amortization of the bond premium and the corresponding basis reduction may result in an owner realizing a taxable gain when a Bond owned by such owner is sold or disposed of for an amount equal to or in some circumstances even less than the original cost of the Bond to the owner.

The excess, if any, of the stated redemption price at maturity of Bonds of a maturity over the initial offering price to the public of the Bonds of that maturity set forth on the cover of this Official Statement is "original issue discount" under the Code. Such original issue discount accruing on a Bond is treated as interest excluded from the gross income of the owner thereof for federal income tax purposes and exempt from California personal income tax to the same extent as would be stated interest on the Bond. Original issue discount on any Bond purchased at such initial offering price and pursuant to such initial offering will accrue on a semiannual basis over the term of the Bond on the basis of a constant yield method and, within each semiannual period, will accrue on a ratable daily basis. The amount of original issue discount on such a Bond accruing during each period is added to the adjusted basis of such Bond to determine taxable gain upon disposition (including sale, redemption or payment on maturity) of such Bond. The Code includes certain provisions relating to the accrual of original issue discount in the case of purchasers of Bonds who purchase such Bonds other than at the initial offering price and pursuant to the initial offering.

Any person considering purchasing a Bond at a price that includes bond premium should consult his or her own tax advisors with respect to the amortization and treatment of such bond premium, including, but not limited to, the calculation of gain or loss upon the sale, redemption or other disposition of the Bond. Any person considering purchasing a Bond of a maturity having original issue discount should consult his or her own tax advisors with respect to the tax consequences of ownership of Bonds with original issue discount, including the treatment of purchasers who do not purchase in the original offering and at the original offering price, the allowance of a deduction for any loss on a sale or other disposition, and the treatment of accrued original issue discount on such Bonds under federal individual and corporate alternative minimum taxes.

Bond Counsel has not undertaken to advise in the future whether any events after the date of issuance of the Bonds may affect the tax status of interest on the Bonds or the tax consequences of the ownership of the Bonds. No assurance can be given that future legislation, or amendments to the Code, if enacted into law, will not contain provisions that could directly or indirectly reduce the benefit of the exemption of interest on the Bonds from personal income taxation by the State of California or of the exclusion of the interest on the Bonds from the gross income of the owners thereof for federal income tax purposes. Furthermore, Bond Counsel expresses no opinion as to any federal, state or local tax law consequences with respect to the Bonds, or the interest thereon, if any action is taken with respect to the Bonds or the proceeds thereof predicated or permitted upon the advice or approval of bond counsel if such advice or approval is given by counsel other than Bond Counsel.

Although Bond Counsel is of the opinion that interest on the Bonds is exempt from state personal income tax and excluded from the gross income of the owners thereof for federal income tax purposes, an owner's federal, state or local tax liability may be otherwise affected by the ownership or disposition of the Bonds. The nature and extent of these other tax consequences will depend upon the owner's other items of income or deduction. Without limiting the generality of the foregoing, prospective purchasers of the Bonds should be aware that (i) section 265 of the Code denies a deduction for interest on indebtedness incurred or continued to purchase or carry the Bonds or, in the case of a financial institution, that portion of an owner's interest expense allocated to interest on the Bonds, (ii) with respect to insurance companies subject to the tax imposed by section 831 of the Code, section 832(b)(5)(B)(i) reduces the deduction for loss reserves by 15 percent of the sum of certain items, including interest on the Bonds, (iii) interest on the Bonds earned by certain foreign corporations doing business in the United States could be subject to a branch profits tax imposed by section 884 of the Code, (iv) passive investment income, including interest on the Bonds, may be subject to federal income taxation under section 1375 of the Code for Subchapter S corporations that have Subchapter C earnings and profits at the close of the taxable year if greater than 25% of the gross receipts of such Subchapter S corporation is passive investment income, (v) section 86 of the Code requires recipients of certain Social Security and certain Railroad Retirement benefits to take into account, in determining the taxability of such benefits, receipts or accruals of interest on the Bonds and (vi) under section 32(i) of the Code, receipt of investment income, including interest on the Bonds, may disqualify the recipient thereof from obtaining the earned income credit. Bond Counsel has expressed no opinion regarding any such other tax consequences.

Bond Counsel's opinion is not a guarantee of a result, but represents their legal judgment based upon their review of existing statutes, regulations, published rulings and court decisions and the covenants of the City and the Authority described above. No ruling has been sought from the Internal Revenue Service (the "Service") with respect to the matters addressed in the opinion of Bond Counsel, and Bond Counsel's opinion is not binding on the Service. The Service has an ongoing program of auditing the tax-exempt status of the interest on municipal obligations. If an audit of the Bonds is commenced, under current procedures the Service is likely to treat the Authority as the "taxpayer," and the owners would have no right to participate in the audit process. In responding to or defending an audit of the tax-exempt status of the interest on the Bonds, the Authority may have different or conflicting interests from the owners of the Bonds. Public awareness of any future audit of the Bonds could

adversely affect the value and liquidity of the Bonds during the pendency of the audit, regardless of the ultimate outcome.

VERIFICATION OF MATHEMATICAL COMPUTATIONS

The arithmetical accuracy of certain computations included in the schedules provided by the Authority relating to computation of forecasted receipts of principal and interest on amounts deposited with the trustee for the 1986 Certificates, the 1989 Water Certificates and the 1989 Wastewater Certificates, respectively, and the forecasted payments of principal and interest to redeem the 1986 Certificates, the 1989 Water Certificates and the 1989 Wastewater Certificates will be verified by a verification agent yet to be selected. Such computations are based solely upon assumptions and information supplied by the Authority.

NO LITIGATION

At the time of issuance of and payment for the Bonds, the Authority will certify that, except as disclosed herein, there is no action, suit, proceeding, inquiry or investigation, notice of which has been served on the Authority, at law or in equity before or by any court, government agency, public board or body, pending against the Authority, affecting the existence of the Authority or the titles of its officers to their respective offices, or affecting or seeking to prohibit, restrain or enjoin the sale, issuance or delivery of the Bonds or the pledge and lien on the Net Water Revenues or Net Wastewater Revenues pursuant to the Indentures, or contesting or affecting as to the Authority the validity or enforceability of the Bond Law, the Bonds, the Indentures, the Water Lease or the Wastewater Lease, or contesting the tax-exempt status of interest on the Bonds, or contesting the completeness or accuracy of this Official Statement, or contesting the powers of the Authority for the issuance of the Bonds, or the execution and delivery or adoption by the Authority of the Indentures, the Water Lease or the Wastewater Lease, or in any way contesting or challenging the consummation of the transactions contemplated hereby or thereby, wherein an unfavorable decision, ruling or finding would materially adversely affect the validity of the Bond Law, as to the Authority, or the authorization, execution, delivery or performance by the Authority of the Bonds, the Indentures, the Water Lease or the Wastewater Lease.

RATINGS

Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("S&P"), and Moody's Investor's Services ("Moody's") are expected to assign the Water Bonds the ratings of "AAA" and "Aaa, respectively, and to the Wastewater Bonds the ratings of "AAA" and Aaa, respectively, with the understanding that insurance policies securing the payment when due of the principal and interest on such bonds will be issued by FGIC, for and upon the issuance of the Water Bonds, and by Ambac Assurance, for and upon the issuance of the Wastewater Bonds. Such ratings reflect only the views of the entity issuing them and an explanation of the significance of such ratings may be obtained only from S&P and Moody's respectively.

S&P has also assigned to the Water Bonds an underlying rating of "A-" and to the Wastewater Bonds, and underlying rating of "A." Such ratings reflect only the view of the rating agency, and an explanation of the significance of such ratings may be obtained from S&P.

There is no assurance that the ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely by the rating agency, if in the judgment of the rating agency circumstances so warrant. Any such downward revision or withdrawal of the ratings may have an adverse effect on the market price of the Water Bonds or Wastewater Bonds, as applicable.

CONTINUING DISCLOSURE

The Authority has covenanted for the benefit of owners of the Bonds to provide certain financial information and operating data relating to the Authority, including each, the Water Enterprise and the Wastewater Enterprise, not later than 270 days following the end of the Authority's Fiscal Year (currently its Fiscal Year ends on June 30), commencing with the reports for Fiscal Year ended June 30, 2005 (each, an "Annual Report"), and to provide notices of the occurrences of certain enumerated events, if material. The Annual Report for each Enterprise will be filed by the applicable Dissemination Agent on behalf of the Authority with each Nationally Recognized Municipal Securities Information Repository and with the appropriate State information depository, if any. Any notices of material events will be filed by the Dissemination Agent on behalf of the Authority with the Municipal Securities Rulemaking Board (and with the appropriate State information depository, if any). The specific nature of information to be contained in each Annual Report or the notice of material events is set forth in "APPENDIX D – FORM OF CONTINUING DISCLOSURE AGREEMENTS." These covenants have been made by the Authority in order to assist the Underwriter in complying with Rule 15c2-12(b)(5) (the "Rule") promulgated by the Securities and Exchange Commission. The Authority has never failed to comply in all material respects with any previous undertakings with regard to said Rule to provide annual reports or notices of material events.

MISCELLANEOUS

This Official Statement does not constitute a contract with the purchasers of the Bonds.

All information included herein has been provided by the Authority, except where attributed to other sources. Any statements made in this Official Statement involving matters of opinion or of estimates, whether or not so expressly stated, are set forth as such and not as representations of fact, and no representation is made that any of the estimates will be realized.

All of the preceding descriptions and summaries of certain legal documents, other applicable legislation, agreements, reports and other documents are made subject to the provisions of such documents respectively, and do not purport to be complete statements of any or all of such provisions. Reference is hereby made to such documents available from the Underwriter and following issuance of the Bonds, on file at the offices of the Trustee in Los Angeles, California, for further information in connection therewith. The information contained herein has been compiled from official and other resources and, while not guaranteed by the Authority, is believed to be correct.

AUTHORIZATION OF OFFICIAL STATEMENT

The delivery of this Official Statement has been duly authorized by the Authority. At the time of delivery of the Bonds, an authorized officer of the Authority will furnish a certificate to the effect that such authorized officer has no knowledge or reason to believe that this Official Statement, as of its date and as of the date of issuance of the Bonds, contains any untrue statement of a material fact or omits to state a material fact necessary in order to make the statements made herein, in light of the circumstances under which they were made, not misleading.

BANNING UTILITY AUTHORITY

By: /s/ Randy Anstine
Executive Director