Financial Overview and Budgetary Issues

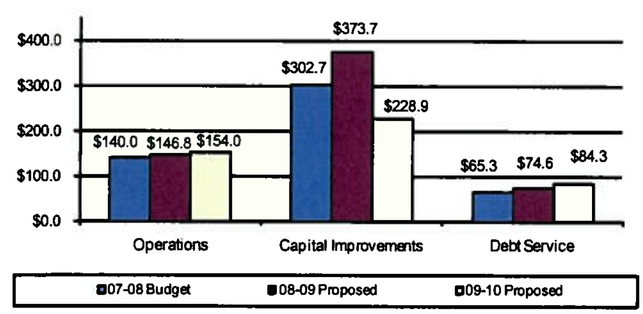
This section of the budget is a financial overview and an outline of issues affecting the development of the budget, as listed below:

- Proposed Consolidated Cash Flow Budget
- Proposed Operating Budget
- Proposed Capital Improvement Cash Outlay
- Debt Service Requirements
- Sewer Service Fees & Property Tax Revenues
- Budget Highlights
- Reserves
- Staffing
- Business Plan
- OCSD Long-Term Planning Process
- OCSD Fiscal Policies
- GFOA Recommended Practices

Proposed Consolidated Cash Flow Budget

The total proposed cash flow budget for FY 2008-09 is $601.0 million, a 17.1 percent increase over the prior year total cash flow budget of $513.2 million. The total proposed cash flow budget for FY 2009-10 is $467.3 million, a 22.2 percent decrease from the total proposed cash flow budget for FY 2008-09. The proposed decrease from FY 2008-09 to FY 2009-10 is primarily due to the $144.8 million or 38.7 percent decrease in the Capital Improvement Program (CIP), and is attributable to the timing of the construction schedule on the implementation of the overall 10-year $1.4 billion CIP program. The table below shows the comparisons of the FY 2007-08 Budget, FY 2008-09 Proposed, and the FY 2009-10 Proposed by major budget category.

Budget Comparison (in millions)

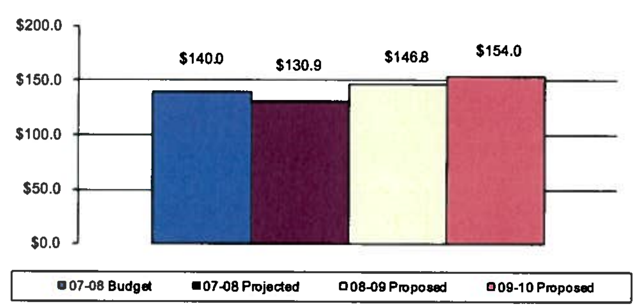


Proposed Operating Budget

The Operating program accounts for the costs to operate, maintain, and manage the District's two treatment plants, with a combined design capacity of 372 million gallons a day, and the 568 miles of collection systems. All the personnel costs for the District are initially recorded as an Operating cost. Costs chargeable to the capital improvement program are allocated for the work done through a job cost system. These charges are shown as reductions in the line item Operating program budget. Costs remaining in the Operating program are ultimately allocated to the two individual revenue areas that make up the District, the Consolidated Revenue Area and Revenue Area 14, based on flows.

Operational cost, comprised of collections, treatment plant, and disposal operations and maintenance, and administration, are projected to come in under the FY 2007-08 Budget by $9.1 million, or 6.5 percent. The FY 2008-09 Budget is being proposed with an increase of $6.8 million or 4.9 percent over the prior year budget, and the FY 2009-10 Budget is being proposed with an increase of $6.5 million, or 4.9 percent over the FY 2008-09 Proposed Budget.

Operations Budget Comparison (in millions)



Analysis on the year-to-year change is provided from three perspectives. First, the FY 2007-08 Budget is compared to the FY 2007-08 year-end projections. Secondly, the FY 2007-08 year-end projections are compared to the FY 2008-09 Proposed Budget, and lastly, the FY 2008-09 Proposed Budget is compared to the FY 2009-10 Proposed Budget.

<u>FY 2007-08 Operations – Budget vs. Projected</u>

As depicted by the chart above, Operating expenses are projected to come in under the FY 2007-08 Budget by $9.1 million, or 6.5 percent. The major categories that comprised the total short fall include chemicals, consisting of coagulants, odor control, and disinfection chemicals; utilities, consisting of electrical power, natural gas, and water; removal of residual solids from the rehabilitation of digesters; unused budgeted contingency; and in personnel cost savings.

Chemicals savings of $5.2 million, or 25.1 percent, are anticipated due to the optimization on the usage of anionic and cationic polymers, ferric chloride, hydrogen peroxide, caustic soda, and bleach throughout the treatment facilities that has resulted in decreased usage. An example of this optimization was achieved by reducing the bleach feed rate during the PM shift and maintaining constant feed during the AM shift, and in limiting the operation of three scrubbers to only two at Plant No. 1.

Utility costs are expected to come in under budget by $1.5 million, or 15.0 percent, due primarily to the decrease in electrical power of $1.9 million that is expected to be offset somewhat by an overage in natural gas of $400,000. Savings in electricity is the result of summer peak shavings that reduced usage and the lower than expected electrical rates as expected increases were not approved by the Public Utilities Commission. The summer peak shavings in electricity were obtained by the additional usage of natural gas generating the net overall savings in utilities.

Other waste disposal savings of $1.1 million, or 39.6 percent, are anticipated due to timing issues in rehabilitation of digesters along with complications arising in the cleaning of Digester "S" at Plant No. 1. These costs are now expected to occur in the following year.

Budgeted but unused operating contingencies are expected to save the District $700,000. Budgeted Personnel costs of $79.9 million are expected to come in under budget by $479,000, or by 0.6 percent.

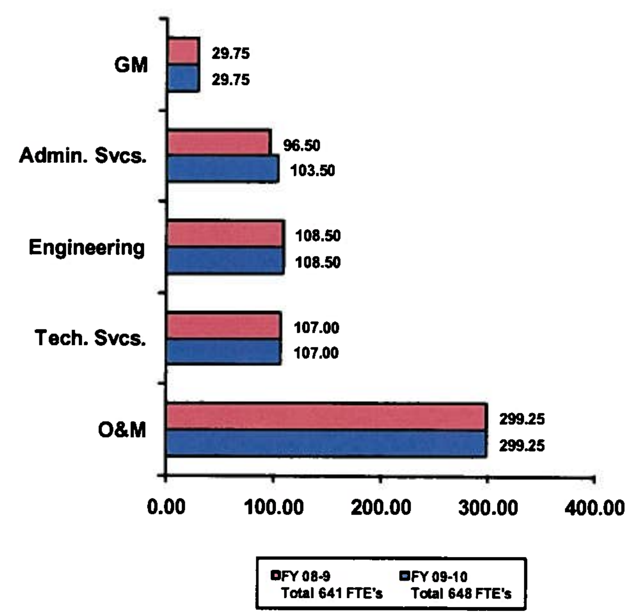
FY 2008-09 Proposed Operations Budget vs. FY 2007-08 Projected Operations Expense

Although the District continues to strive to be efficient and effective, staff is proposing a $15.8 million, or 10.8 percent increase over the FY 2007-08 projected operating requirements. Increases in the proposed operating requirements are primarily attributable to increases in contractual services, personnel costs, operating materials and supplies, and utilities.

Contractual services are being proposed to increase $8.6 million, or 43.4 percent, due primarily to a $5.6 million, or 39.1 percent increase in solids removal and a $2.7 million, or 165.5 percent increase in Other Waste Disposal. Biosolids production is estimated to increase at Plant No. 1 by 20 percent in FY 2008-09 due to the increase in treatment with the placement of Ellis Pump Station into service. Plant No. 2 Biosolids production is estimated to increase by 8 percent due to increases in secondary treatment following the completion of secondary treatment upgrade projects. In addition, the average unit removal cost is expected to increase 18 percent to $65 per ton as the EnerTech facility comes on line in early 2009 requiring a contracted 225 tons per day at a cost of $72.40 per ton plus fuel cost adjustments. The other waste disposal category includes disposal costs for grit and screening waste, digester cleaning waste, and hazardous materials. The FY 2008-09 proposed budget includes the cost of cleaning a total of 7 digesters for $3.6 million. This budget is reduced to $2.1 million in FY 2009-10 when only 4 digesters are scheduled to be cleaned. The proposed budget for disposal of grit, screenings and other waste is $730,000 in FY 2008-09 and $755,000 in FY 2009-10.

Personnel costs are being proposed at a 5.5 percent, or $4.4 million increase over the prior year projection. This increase is partially attributable to the increase of 7 full-time equivalent (FTE) employees proposed for FY 2008-09 over the prior year. The total FTE count is proposed to increase from 634 FTE's in FY 2008-09, to 641 FTE's in FY 2008-09, and by an additional 7 FTE's in FY 2009-10 to 648 FTE's.

Full Time Equivalent (FTE) Staff



Retirement premiums are being proposed at an increase of $1.3 million in FY 2008-09 over the prior year projected total as the District's required contribution rate has been increased by the Orange County Employees Retirement from 20.65 percent to 21.34 percent as a result of revised actuarial assumptions and lower than expected return on investments in prior years.

Operating materials and supplies are being proposed to increase $4.6 million, or 25.9 percent, over the prior year projected total due primarily to the combined increases in chemical coagulants, odor control, and disinfection totaling $4.4 million. Bleach alone is projected to increase $2.2 million over FY 2007-08 projected costs to $7.1 million due primarily to mandated construction shutdowns that will require the use of more bleach. The use of magnesium hydroxide, a chemical that reduces the formation of hydrogen sulfide that causes odor and corrosion within the sewer trunk lines, is proposed to increase $1.1 million in FY 2008-09 from the prior year projection. This increase is due to the addition of two treatment locations planned in FY 2008-09 that will require the total usage to increase from approximately 460,000 gallons in FY 2007-08 to 945,000 gallons in FY 2008-09.

Utility costs are being proposed to increase $1.3 million, or 15.7 percent, over the prior year projected total. As previously noted, there is a $1.9 million electric power savings projected in FY 2007-08 as compared to budget. The electric power budget is now being proposed in FY 2008-09 $1.1 million lower than the FY 2007-08 budget at $5.9 million. This is an increase of $846,000 over the prior year projected due to projected consumption and unit cost increases. Natural gas is being proposed in FY 2008-09 at a $393,000 increase over the prior year projected due primarily to the planned use of more gas to keep the three co-generation engines at Plant No. 2 running at minimum output levels..

FY 2009-10 Proposed Operations Budget vs. FY 2008-09 Proposed Operations Budget

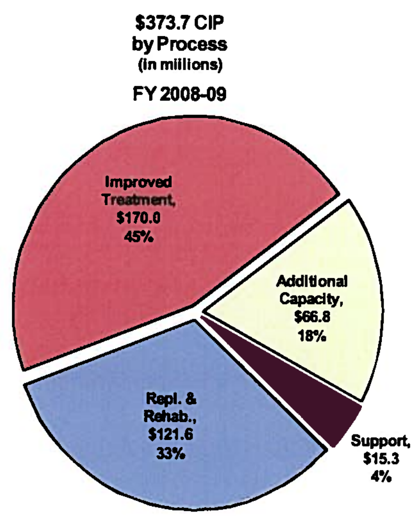
In FY 2009-10, the second year of this two-year operating budget, staff is proposing a $7.3 million, or 4.95 percent increase over the FY 2008-09 proposed operating requirements. Increases in the proposed operating requirements are primarily attributable to increases in personnel costs, capital grants to member cities, and operating materials and supplies that are partially offset by decreases in repairs and maintenance.

Personnel costs are being proposed at a 7.4 percent, or $6.1 million increase in FY 2009-10 over the FY 2008-09 proposed budget. This increase is partially attributable to the increase of 7 FTE employees proposed for FY 2009-10 over the total proposed staffing of 641 FTEs proposed for FY 2008-09. In addition, retirement premiums are proposed to increase $1.0 million, or 6.3 percent, and group insurance is being proposed to increase $784,000, or 10.7 percent.

Capital grants to member cities are proposed at an increase $1.8 million in FY 2009-10. This increase aligns with program contracts currently in place.

Operating materials and supplies are being proposed to increase $1.4 million, or 6.1 percent, due primarily to the combined increases in chemical coagulants, odor control, and disinfection totaling $1.3 million. These chemical increases are due mostly to projected quantity increases.

Repairs and maintenance is being proposed at a decrease of $1.2 million. This reduction is due to the timing and scheduling of major repair and maintenance projects.



Proposed Capital Improvement Cash Outlays

Proposed capital improvement outlays are more than one-half of the overall proposed budget and provide for the construction of facilities at the two treatment plants, including the utility systems, administrative facilities, and the ocean disposal system and the rehabilitation, replacement and expansion of the 568 miles of the collections system. Projects over

$35,000 require formal bidding per the California Public Works Construction Act, and any project over $100,000 requires Board approval in accordance with the District's procurement ordinance.
The budget has been prepared under assumptions included in the Strategic Plan adopted by the Board of Directors in the fall of 1999.

The FY 2007-08 projected cash outlay for the CIP is expected to reach 92.3 percent of budget, or $279.3 million. The FY 2008-09 proposed cash flow budget of $373.7 million is part of the overall remaining CIP budget of $1.4 billion identified within the Interim Strategic Plan Update completed in June 2002 and the recently completed Annual CIP Validation Study.

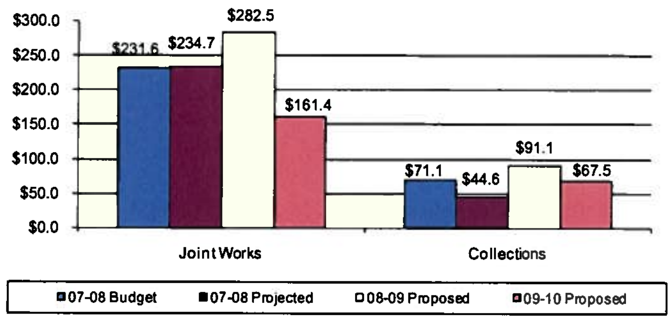
In October 1999, the District adopted a new Strategic Plan identifying the future capital infrastructure needs over the next 20 years, including projections through the assumed "build out" of the District's service area to the year 2050 for the purpose of meeting future wastewater quantity and quality requirements. An Interim Strategic Plan Update was completed in June 2002 for the purpose of updating critical factors such as population growth, new construction, the volume of wastewater delivered to the plants and viable water conservation and reclamation programs. In preparation of the FY 2006-07 Budget, the District completed the annual validation study of the CIP to ensure that the scope of the projects was appropriate, and that the cost estimates were accurate.

The validated CIP, excluding currently unplanned rehabilitation and replacement projects past 2012-013, identified 86 large capital projects and 28 special projects with a 15 year expenditure of $1.5 billion. This total represents a $149 million increase from the FY 2007-08 CIP estimate, and accounts for inflation of the estimated construction cost from 2008 dollars to the date when the project will be at the midpoint of construction. The 2008-09 validated CIP breaks down into the following project categories:

- 45% improved treatment
- 33% repair, rehabilitation and replacement
- 18% additional capacity
- 4% Support facilities

The CIP program consists of Joint Works, or Treatment Plant Construction, Collection System rehabilitation, replacement, and expansion, and Joint Works Equity Transfers between Revenue Areas of the District. Joint Works Equity Transfers are the annual reallocation of Joint Treatment Work assets between Revenue Areas based on the average of the most recent three years of sewage flows. On a consolidated basis, equity transfers are offsetting.

CIP Program Budget
(Net of Joint Works Equity Transfers)
(In millions)



Joint Works, or Treatment Plant Construction, projected outlay for FY 2007-08 is expected to reach 101.3 percent of the annual cash flow estimate, or $234.7 million. The FY 2008-09 and FY 2009-10 proposed cash flow budgets of $282.5 million and $161.4 million reflect the District's efforts to meet the consent decree secondary treatment standards by December 2012. Large secondary treatment projects include Secondary Treatment System at Plant No. 1, Trickling Filters at Plant No. 2, and Headwork Improvements at Plant No. 2 with proposed cash outlays in FY 2008-09 of $100.1 million, $73.7 million, and $25.8 million and proposed cash outlays in FY 2009-10 of $21.5 million, $56.9 million, and $13.2 million, respectively. Other treatment plant projects include the Primary Treatment Rehabilitation and Primary Sludge Feed System at Plant No. 2, and the Sludge Dewatering and Odor Control at Plant No. 1 with proposed outlays in FY 2008-09 of $16.4 million, $12.4 million and $7.6 million and proposed outlays in FY 2009-10 of $5.7 million, $3.8 million, and $2.1 million.

The Collection System Capital Program is being proposed to increase from the prior year cash outlay budget by $20.0 million, or 28.2 percent, to $91.1 million in FY 2008-09 and then decrease by $23.6 million, or 23.6 percent to $67.5 million in FY 2009-10. These proposed improvements are needed in order to keep the 568 miles of collection systems free from failure. Two large Collection System related projects include the Bitter Point Force Main Rehabilitation and the Replacement of the Rocky Point Pump Station with FY 2008-09 proposed cash outlays of $22.4 million and $1.7 million. The Bitter

Point Force Main is expected to be completed at the end of FY 2008-09, but Rocky Point Pump Station construction will continue into FY 2009-10. The Capital Improvement Program is described in more detail in Section 8 of this document.

Debt Service Requirements

The District's long-term debt fiscal policy restricts long-term borrowing to capital improvements that cannot be financed from current revenue. Before any new debt is issued, the impact of debt service payments on total annual fixed costs will be analyzed. In May 2008, the District issued $77.2 million of COP fixed rate debt to retire the outstanding amount owed on Series 1993. As the result of having a well-funded reserve policy, experienced management, and prudent planning, the District was able to secure "AAA" credit rating from Standard and Poors while maintaining "Aa' ratings from the other two rating agencies. Prior to this refunding, the District issued $300 million of new money COP fixed rate debt in December 2007 Series 2007B to fund current and future capital improvement expenditures. This two-year budget proposes to issue additional new money debt of $200 million in FY 2008-09 and $120 million in FY 2009-10, as a total of $550 million of debt financing is forecasted over the next five years to fund the $1.4 billion in capital improvement program requirements and $573 million in replacement, rehabilitation, and refurbishment projects anticipated over the next ten years. The FY 2008-09 debt service requirements are being proposed at $74.6 million, a $66.4 million decrease, from the prior year projected amount due to the refunding issue of $77.2 million and the retirement of $77.3 million in outstanding COP's from the Refunding Series of 1993. Following the issuance of an additional $200 million in FY 2008-09 and $120 million in FY 2009-10, total debt service requirements are expected to grow to $84.3 million in FY 2009-10, an increase of 13.0 percent over FY 2008-09. The District's Debt Financing Program is described in more detail in Section 9 of this budget.

Sewer Service Fees

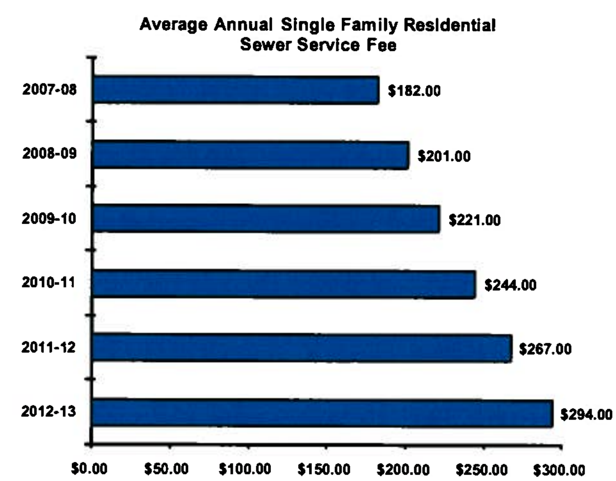
The Consolidated Revenue Area has an adopted Sanitary Sewer Service Fee to provide funding for operating the sewer systems in accordance with the Clean Water Act and the District's Revenue Program. Revenue Area No. 14 is funded through user fee charges to the Irvine Ranch Water District. Sewer service fees are set annually by the District after a review of projected needs.

In July of 2002, the Board of Directors approved a change from the existing level of treatment, a blend of 50 percent advanced primary and 50 percent secondary treated wastewater, to secondary treatment standards. The reasoning behind the decision to move to secondary standards included (1) the possibility that bacteria from the ocean outfall may at times reach the shoreline, (2) upgraded treatment will aid additional water reclamation with the Orange County Water District, and (3) the public clearly favored upgrading wastewater treatment at this time.

In November 2007, the Board approved the District's Five-Year Strategic Plan that reaffirmed the 2002 capital construction estimate of $649 million to meet secondary treatment standards by 2013, and to proceed with the $2.6 billion, 20-year capital improvement program.

In February 2008, following a Proposition 218 notice process, the Board approved sewer rate increases for each year over the next five years averaging approximately 10 percent a year. These increases are necessary to provide needed capital improvements, to meet additional treatment and disinfection requirements, and to minimize future rate increases.

The impact of this five-year sewer fee schedule increased the annual single family residence user fee from $182 to $201 in FY 2008-09, to $221 in FY 2009-10, to $244 in FY 2010-11, to $267 in FY 2011-12, and to $294 in FY 2012-13.



Even with these increases, District rates will remain well below the current State-wide average annual sewer rate of $406 reported in the 2008 California

Wastewater Charge Survey of 920 agencies conducted by the State Water Resources Control Board.

In FY 1997-98, the District's Rate Advisory Committee, made up of elected city officials, community, business and industry leaders, and District staff analyzed the District's rate structure to determine whether user fees were equitable among residences and industry. In May of 1998, the Board approved the proposed revisions to the Sewer Service User Fee rate structure that more equitably charged consumers based on actual usage while remaining revenue neutral. Significant changes in the rate structure included:

- Non-residential user charge will be based upon typical quantity and strength of discharge per 1,000 square feet.
- Fees for users who discharge high quantities or high-strength waste, including former Class III permittees such as restaurants and Laundromats, will be based on the assumed flow and strength per 1,000 square feet.
- Discontinuation of the Class III permit process because of the implementation of the expanded and more accurate rate structure. This resulted in simplification of the billing and collection process for these two hundred users.
- The revised rate structure resulted in a greater number of decreases in charges (22,000) for non-residential users than increases (13,000).

Overall, the total fees collected remained essentially the same as those generated by the old structure.

Property Taxes

The District's share of the one percent ad valorem property tax is dedicated for the payment of COP debt service. The apportionment of the ad valorem tax is pursuant to the Revenue Program adopted in April 1979 to comply with regulations of the Environmental Protection Agency and the State Water Resources Control Board and in accordance with COP documents and Board policy.

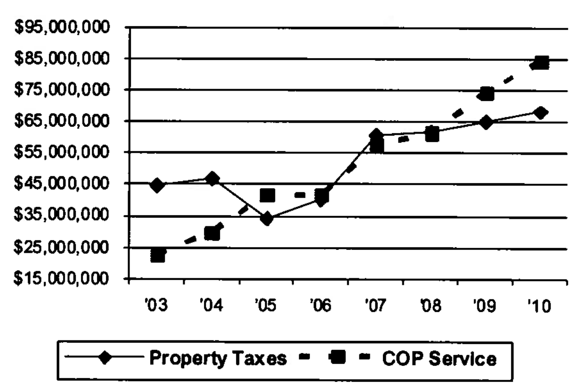
Recent results indicate that property tax revenues had steadily increased to a level where they could once again support the District's debt service obligations. However, future anticipated capital improvements of $2.0 billion over the next 10 years will require new COP debt issuances totaling $550 million. This increase in debt has increased debt service payments beyond the capability of being funded solely from property tax revenues.

This problem had been exacerbated by the State's recent two-year raid on property tax revenues. Because of the State's fiscal crisis, the State legislature approved a $1.3 billion property tax shift in FY 2004-05 and FY 2005-06 from non-education local governments. Of this $1.3 billion shift for each of these two years, $350 million a year was projected to be contributed from special districts, an amount equal to 40 percent of current property taxes.

The overall reduction on total property tax revenue received by the District was 23.7 percent, to $35.8 million in FY 2004-05 and 18.6 percent, to $39.9 million in FY 2005-06, due to the steady increase attributed to the home sales market and the corresponding increase in home values, and receiving the full benefit of these increases on all non-secured property tax distributions. Full property tax allotments were received in FY 2006-07 totaling $60.6 million, and are expected to reach $61.8 million for FY 2007-08. Property taxes are being budgeted in FY 2008-09 and FY 2009-10 at $64.9 million and $68.2 million, respectively, increases of approximately 5.0 percent a year over the FY 2007-08 projected amount.

Any property tax revenue shortfalls in meeting debt service obligations will have to come from user fees, as making debt service payments is a priority.

COP Funding Requirements vs.
Property Tax Funding Source



Budget Highlights

This section briefly outlines the proposed major changes in all departments and Revenue Areas over the next two years. All Joint Works Operations, or plant operating costs and collection system costs are consolidated into the individual department budgets for better accountability and control. However, separate accounting is maintained between Joint Works Operation activities (treatment and disposal operational costs) and collection operational activities since each Revenue Area is directly responsible for their own collection operating costs. The Joint Works Operation activities are allocated to the Revenue Areas based on their individual contributions to the annual sewage flow. Likewise, the Joint Works Capital Improvements are allocated to the Revenue Areas on a three-year average of sewage flows called the "joint works equity percentage", and each Revenue Area is responsible for their own collection system capital improvements.

Details for each department can be found in "Section 6 – Operations" of this document. Complete staffing schedules are located in the Appendix.

General Management

- An amount equaling 0.5 percent of the Operating materials and services budget is included within the General Manager's Re-appropriation line item for each of the next two fiscal years. Since the current year's budget lapses each year, re-appropriation of funds are needed to pay for goods or services ordered at the end of one budget year but not provided until the following year. The General Manager reviews and approves all departmental re-appropriation requests to ensure that prior year funding was available and has not been spent.

- An amount equal to 0.5 percent of the Operating materials and services budget is included within the General Manager's contingency account for each of the next two fiscal years.

- A decrease of 0.5 FTE beginning in FY 2008-09.

Administrative Services

- A decrease in property/general liability insurance in-lieu premiums of $1.1 million in FY 2008-09 due to favorable market conditions on insurance renewals and minimal claim losses.

- Decrease in postage of $228,000 in FY 2008-09 as the last Proposition 218 Notices sent cover the next five years.

- An amount equal to 2.0 percent of regular salaries is being proposed for agency-wide training for each of the next two fiscal years. This training budget is centralized within the Human Resources Division for better control and accountability, and to maximize the benefits of training costs that are related to training efforts required throughout the agency.

- Projected increases in Information Technology service maintenance agreements of $122,000 and $70,000 in FY 2008-09 and FY 2009-10.

- A decrease of 1.0 FTE for FY 2008-09.

- An increase of 7.0 FTE's for FY 2009-10. These increases are all located within the Human Resources Division due to overall planned District-wide increases. These positions will remain in this division until specific positions and divisional assignments are determined.

Technical Services

- Legal service costs increased $210,000 in FY 2008-09 over prior year actual due to court ordered CEQA compliance for Kern County litigation.

- Regulatory Operating Fees increased $215,000 in FY 2008-09 and FY 2009-10 over the FY 2007-08 Budget.

- Research and monitoring are being proposed at an increase of $330,000 in FY 2008-09 over the projected amount for FY 2007-08.

- A net decrease of 2.0 FTE in FY 2008-09.

Engineering

- FY 2008-09 budgeted CIP outlays are proposed to increase $70.9 million, or 23.4 percent, to $373.7 million over the prior year budgeted CIP cash outlays. However, FY 2009-10 budgeted CIP outlays are proposed to decrease $144.8 million, or 38.7 percent, to $228.9 million over FY 2008-09 proposed budgeted CIP cash outlays.

- A $2.2 million decrease in capital grants to member agencies in FY 2008-09, followed by an increase of $1.8 million in FY 2009-10.

- A net increase of 4.0 FTE's beginning with FY 2008-09.

Operations & Maintenance

FY 2008-09 increases over FY 2007-08 Projection:

- An increase in disinfection of $ 2.2 million.
- An increase in solids removal of $5.6 million.
- An increase in other waste disposal of $2.7 mil.
- An increase in odor control of $1.0 million.
- An increase of electricity costs of $836,000.
- An increase in natural gas of $393,000.
- An increase in Repairs & Maint. of $448,000.

FY 2009-10 Budgeted increases of FY 2008-09:

- A decrease in disinfection of $ 87,000.
- An increase in solids removal of $2.0 million.
- A decrease in other waste disposal of $1.5 mil.
- An increase in odor control of $511,000.
- An increase of electricity costs of $305,000.
- Natural Gas budget remains the same.
- A decrease in Repairs & Maint. of $1.2 million.

FY 2008-09 and FY 2009-10 Staffing changes:

- Net increase of 6.5 FTE's beginning with FY 2008-09.

Individual Collection System

Operating- reflects costs of operating and maintaining each Revenue Area's collection system, utilities, and Directors' fees. Industrial/commercial monitoring costs reflecting the expense of enforcing the Uniform Use Ordinance and EPA's pre-treatment standards are also included. The largest operating cost is the Revenue Area's flow-based share of the Joint Works Operating expenses.

Capital Facilities- accounts for each Revenue Area's share of the Joint Works Capital Improvement projects and for individual Revenue Area trunk sewer or pump station projects. The entire collection system has a sewer construction program Master Plan in progress as a result of the 1999 Strategic Plan. Other line items in these funds are accumulated reserves for future capital improvements in accordance with Master Plans and federal and state requirements and annual purchase or sale of equity in the jointly-owned treatment works as provided for in the Joint Ownership, Operation, and Construction Agreement.

Debt Service/COP- accounts for the proceeds from and service of the Capital Improvement Program Certificates of Participation (COPs). The District's share of the one percent basic levy ad valorem property tax is dedicated to provide for COP principal and interest payments.

See Section 9 for additional information on the District's debt financing program.

Reserves

In 1998, the District conducted an in-depth review of the agency's reserve policies. This review included a survey of the reserve policies of 23 other public agencies as a tool to assist in the evaluation of the underlying economic reasons supporting the District's reserve policies. Based on this review, the Directors approved the following reserve policies:

- Cash Flow Reserve has been established at a level to fund operation, maintenance and certificates of participation debt service expenses for the first half of the fiscal year. The first installment of property tax revenues and sewer service user fees that is collected by the County through the property tax bill is not available until late December each year.

- Operating Contingency Reserve has been established to provide for non-recurring expenditures that were not anticipated when the annual budget and sewer service fees were considered and adopted. The level of this reserve will be established at an amount equal to ten percent of the annual operating budget.

- Capital Improvement Reserve has been maintained to fund annual increments of the capital improvement program. The long-term goal is to fund one half of the capital improvement program from borrowing and the other half from current revenues and reserves. With this program in mind, the target level of this reserve has been established at one half of the average annual cash outlay of the capital improvement program through the year 2020. Levels higher and lower than the target can be expected while the long-term financing and capital improvement programs are being finalized. Proceeds from any debt issuance targeted for construction are also included in this reserve until spent.

- Catastrophic Loss, or Self-Insurance Reserves has been maintained for property damage including fire, flood and earthquake, for general liability and for workers' compensation. These reserves are intended to work with purchased insurance policies, FEMA and State disaster reimbursements. Based on the current plant infrastructure replacement value of $3.12 billion, the level of this reserve has been set to fund the District's non-reimbursed costs, estimated to be $57 million.

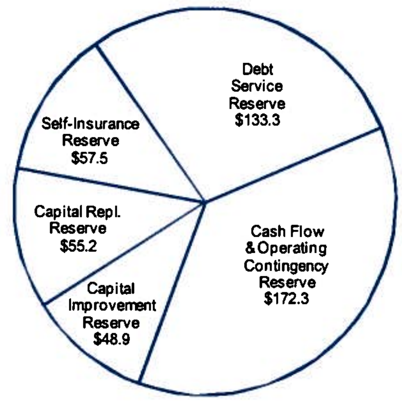
- Capital Replacement/Renewal Reserve will be established to provide thirty percent of the funding to replace or refurbish the current collection, treatment and disposal facilities at the end of their useful economic lives. The current replacement value of these facilities is estimated to be $5.38 billion. The initial reserve level had been established at $50 million, and is augmented by interest earnings and a small portion of the annual sewer user fee, in order to meet projected needs through the year 2030.

- Debt Service Reserve is required to be under the control of a Trustee by the provisions of the certificate of participation (COP) issues. These reserve funds are not available for the general needs of the District and must be maintained at specified levels.

- Rate Stabilization Reserve will be used to accumulate all available funds exceeding the targets for all other reserves. These funds will be applied to future years' needs in order to maintain rates or to moderate annual fluctuations. There is no established target for this reserve. Because the reserves of all other funds have not been exceeded, this reserve level is set for zero at June 30, 2007.

Collectively, these individual reserve requirements total over $450 million for each year of the current ten-year cash flow forecast. As part of the budget development of the previous two-year budget, the District's Finance Management staff and the Board of Directors concluded that there was an overlapping benefit in having individual reserves, and that it was unlikely that situations would arise that called for the drawdown of more than one reserve category at any given point in time. Therefore, the reserve policy was adjusted to reflect individual reserve computations with a 10 percent reduction to the accumulated total, or roughly $40 million.

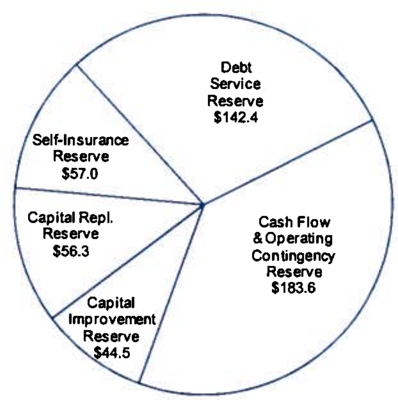
Proposed Reserves
at 6/30/09
(In Millions)



Total Reserves - $467.2

The actual reserve requirement for FY 2008-09 is $460.9 million, which is $6.3 million less than the $467.2 million budgeted for actual year-end reserves.

Proposed Reserves
at 6/30/10
(In Millions)

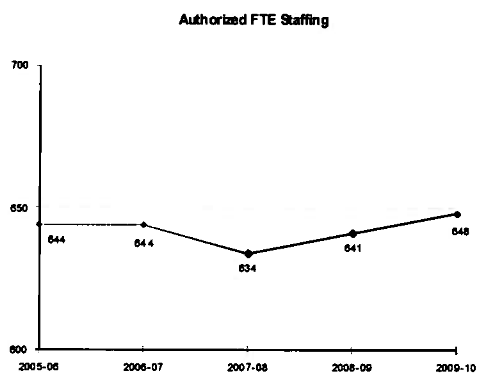


Total Reserves - $483.8

Due to back-to-back 10.5 and 10.0 percent rate increases in FY 2008-09 and FY 2009-10 coupled with a $200 million and $120 million proposed COP debt issuance in FY 2008-09 and FY 2009-10, respectively, actual proposed reserve levels at June 30, 2010 will exceed reserve level requirements by $4.8 million.

Staffing Levels

Authorized staffing levels are being proposed with increases of 7.0 full time equivalents (FTE) each for FY 2008-09 and FY 2009-10 above the staffing level of 634 FTE positions authorized for FY 2007-08. The total FTE count of 648 FTE's in FY 2009-10 would still be 30 FTE below the agency's all time high of 678 positions approved in FY 1995-96.



The District budgets staffing levels by FTE in order to provide a realistic estimate of actual staffing levels since not all employees are full-time employees. The part-time positions are funded at 1,040 hours per year. Part-time employees receive a prorated share of personnel benefits.

The staffing reductions from 1995-96 are a result of this agency's effort in striving to provide wastewater treatment as efficiently and effectively as possible while lowering operational and maintenance costs to more closely match those agencies that are "best in class" for wastewater treatment facilities. However, as the result of new initiatives in the areas of water reclamation and conservation, and the expansion of the Capital Improvement Program (CIP), the existing staffing plan was no longer sufficient to meet the District's needs.

In considering the staffing impacts on the CIP program alone, the most recently completed validation study of the CIP calls for capital expenditures to increase to $373.7 million in FY 2008-09 and $228.9 million in FY 2009-10, a total of $1.4 billion over the next 10 years.

The Appendices within Section 10 provide a Staffing History Summary (by Department and Division) and Detail (by position title within each Department and Division).

Purchasing Authorization

In 1998-99, the Board amended the purchasing authority of the agency's General Manager for purchases up to $100,000. In Section 5 of this document, staff has provided a detailed listing of specific goods or services to be acquired in FY 2008-09, each costing in excess of $100,000. Staff is recommending that the Board approve the acquisition of these items by staff during the next fiscal year without having to bring these items back to the Board for re-approval.

Business Plan

The District began development of a comprehensive annual Business Plan that was first included within the FY 2005-06 Budget document, and was updated in the following two-year budget beginning in FY 2006-07. This Business Plan has now been updated once again following the Board acceptance of the Five-Year Strategic Plan in November 2007. This Business Plan now includes the funding resources required as a result of the Board approval of the increased levels of service including the development of a sustainable biosolids management program, minimizing the impact of collection and treatment odors, and the reduction of air toxic emissions. Also included in this updated business plan is the business planning process and the current and projected key performance indicators (level of service). The FY 2008-09 Business Plan, that begins within Section 2 – Page 17, has includes the following topics:

- Strategic Initiatives
- Levels of Service
- Two-Year Staffing Plan
- Updated Financial Model
- Risk Assessment
- Updated Asset Management Plan

Development of the business plan in future years will include an expansion of the risk assessment component to include risk avoidance.

OCSD Long-Term Planning

The District's current efforts in regard to long-term planning include the CIP Strategic Plan Update, which focuses on the District's long-term capital improvement facilities and rehabilitation projects that will be needed annually out to the year 2020, and re-organizing the operations of the District in order for this agency to maintain a "best in-class" wastewater treatment facility.

CIP Strategic Planning

In October 1999 the District completed its Strategic Plan, an update of the 1989 30-year "2020 Vision" Master Plan. Many of the assumptions used to develop the original plan, such as inflation, the projected service population, the level of building activity, and the volume of wastewater treated, were quite different from what was assumed nearly ten years earlier. If the assumptions of the Master Plan were not updated, the District could be constructing unnecessary facilities and charging higher fees than would be needed.

In addition to updating the population and flow assumptions, the Strategic Plan provides for an operations and financial plan and includes a review of the collection, treatment and disposal facilities, and ocean outfalls.

In June 2002, a new, or interim, Strategic Plan Update was completed that revised many of the assumptions used to develop our previous planning documents, including population and land-use projections, the level of building activity in our service area and the volume of wastewater to be treated. This information was needed for the Board's consideration of secondary treatment the following month. The Interim Strategic Plan Update also provides an operations and financial plan including a review of our collection, treatment and disposal facilities, and a study of our ocean outfall system.

In conjunction with preparation for the FY 2008-09 and FY 2009-10 Budget, District staff conducted strategic planning workshops with the Board of Directors to layout a capital program to deliver the levels of service desired by the Board of Directors. These levels of service and resulting capital projects are included in the District's 5-year Strategic Plan. This includes approximately $50 million of new CIP projects over the next 10 years.

In addition, District staff has reviewed each CIP project to ensure that the scope of the project was appropriate, and that the cost estimates were accurate. The validated CIP includes 86 large capital projects and 28 special projects with a 15-year expenditure of $1.47 billion. This total represents a $149 million increase from the 2007-08 CIP estimate. This increase includes $50 million from the District's 5-year Strategic Plan, $28 million in newly identified rehabilitation and renewal needs, and $71 million in project budget revisions for on-going projects.

Over the next ten years, the CIP cash flow needs, including rehabilitation and replacement projects, will approximate $2.0 billion, or an annual average of $200.0 million.

Moving Towards Secondary Treatment

The Board of Directors approved a change from the existing 50/50 level of treatment to meeting secondary treatment standards in July of 2002. The reasoning behind the decision to move to secondary standards included (1) the possibility that bacteria from the ocean outfall may at times reach the shoreline, (2) upgraded treatment will aid additional water reclamation with the Orange County Water District, (3) and the public clearly favored upgrading wastewater treatment at this time.

As a result of the completion of the Capital Improvement Program Validation Study and the Secondary Treatment Review in the spring of 2003, a capital improvement program was developed to meet secondary treatment standards as quickly as possible while providing for increased flows and rehabilitation and refurbishment of existing facilities.

The FY 2008-09 CIP includes three projects totaling $631 million to upgrade the District's treatment plants to meet secondary treatment standards. Implementation of secondary treatment standards is scheduled to be completed by December 31, 2012. This schedule was reviewed and determined to be reasonable and achievable by two independent Peer Review Teams.

Planning Advisory Committee II (PAC2)

As part of the process of developing the Interim Strategic Plan Update, the District sought input, comments and suggestions from the residents and businesses that are served by the District. The commitment to actively solicit public comments on the appropriate level of treatment represented a continuation of a relationship with the public that was established in the original Strategic Plan. This relationship proved to be very effective in developing solid information on which the Board of Directors made their determinations and set the course for the District's future in 1999. For this reason, the District developed a public participation process that reflects its commitment to openness and recognition of the need for public involvement in decision-making.

In moving forward with the development of public participation, the District established the concept of a Public Advisory Committee. Because of the relatively short time frame that was available for the Interim Strategic Plan Update work, the District initially turned to the members of the original Planning Advisory Committee (PAC) and Rate Advisory Committee (RAC). In parallel with the Interim Strategic Plan Update, the District also established a Technical Advisory Committee (TAC) to help advise them with the complex issues required with the planning and execution of the Huntington Beach Studies (Phase III), and a number of these TAC members were also on the PAC2. The District recognized that the PAC2 members would bring several key benefits to the project:

- Familiarity with the technical issues;
- Understanding of the public participation process;
- Balanced distribution of technical, environmental, political, and geographic viewpoints; and
- Demonstrated commitment to active and reliable participation.

In addition to this initial group, the District also reached out to organizations and individuals that had consistently expressed interest in participating in the Interim Strategic Plan Update and the ocean discharge permit renewal process. As a result of this effort, 28 members of the new PAC2 were confirmed.

One of the primary objectives of the Interim Strategic Plan Update was to consider different levels of wastewater treatment and their respective advantages and disadvantages. PAC2 members were to provide key support to the project, specifically:

- Review the technical output of the four treatment alternatives under consideration;
- Establish the performance objectives that are to be used to evaluate the alternatives;
- Provide input, comments, and observations regarding the benefits and problems that might be associated with each of the alternatives; and
- Provide a summary report that captures the issues along with their recommendations.

The PAC2 report was completed in June 2002 and provided guidance to the Board of Directors in its decision to change from the existing 50/50 level of treatment to secondary treatment standards in July of 2002.

Five-Year Strategic Plan
Beginning in summer 2007, the General Manager's Office initiated the process of creating this Strategic Plan, soliciting assistance from all levels of the organization. Input included meetings with staff members who helped to retool the Mission Statement, Vision Statement and Core Values during a series of management workshops and Executive Management Team retreats. This was followed by a series of four workshops with the Board of Directors to provide additional input and direction. As a result, a Strategic Plan was developed that addresses several major objectives and critical challenges facing the Orange County Sanitation District now, in the next five years, and further into the future. They include:

- Achieve a comprehensive five-year plan that focuses our present and future efforts to meet the sanitation, health and safety needs of the 2.5 million people we serve.
- Plan, design and build $2.6 billion worth of essential capital improvement projects over a twenty-year period that continue to meet the regulatory, environmental, health and safety needs of a growing population.
- Continue to direct sufficient resources and keep investigating new technologies to effectively deal with odor issues.
- Apply sufficient funds to meet regulatory requirements related to air emissions.
- Continue to support the Groundwater Replenishment System in partnership with the Orange County Water District.
- Continue to aggressively pursue alternatives that make fiscal and environmental sense in the final disposition of biosolids.
- Apply sufficient resources to ensure the maintenance of our assets remains a priority.

- Address risk assessment issues to protect the environment, our employees and the public's health.
- Sustain and enhance a skilled work force capable of managing a highly technical operation in a dynamic and technologically challenging environment.
- Protect our reserves and credit rating while maintaining a responsible rate structure that is at or below other sanitation agencies.

The Strategic Plan charts a focused roadmap of success for the future of the Orange County Sanitation District. It addresses critical operations and construction issues, financial and budgeting challenges, and gives a clear and concise direction to staff, ratepayers, regulatory agencies, and the general public.

Biosolids Management

The District produces approximately 650 tons of digested and dewatered (Class B) biosolids per day. By 2020, the District's biosolids production is projected to increase by 30 percent, to 310,000 tons annually. The District currently manages its biosolids as follows via two contracts using five options:

- 24% is land applied as Class A biosolids in Kern County, California ($43.07/ton);
- 38% is composted to Class A biosolids in Kern County, California ($63.09/ton);
- 12% is composted to Class A in La Paz County, Arizona ($49.74/ton);
- 23% is land applied as Class B biosolids in Yuma County, Arizona ($45.44/ton); and
- 3% is land filled in Yuma, Arizona ($45.44).

Counties throughout California and Arizona have developed, or are in the process of developing, ordinances that severely restrict or ban the land application of Class B biosolids. Kern and Kings Counties banned land application of Class B biosolids. At the time of this writing, the "Florez" bill which gives the Kern County Board of Supervisors the discretion to ban importation of all biosolids sailed through the California Senate 26-9, and was forwarded onto the Assembly. It has become clear that future requirements for managing biosolids will be more restrictive and costs will increase as current options are anticipated to be eliminated due to these developments in two to five years.

The dynamic regulatory issues, land application ordinances and bans, and public perception challenges prompted the District to develop a Long-Range Biosolids Management Plan. This plan was approved by the Board in December 2003. The goal is to develop a sustainable, reliable, and economical program for long-range biosolids management providing environmentally sound practices that meet the stringent federal, state, and local regulatory requirements.

The Long-Range Biosolids Management Plan (Plan) includes four major elements:

1. Identify long-term potential Southern California Class A biosolids products and product markets.

2. Identify the onsite and offsite facility options for manufacturing marketable products while optimizing the use of the District's facilities necessary in treating wastewater.

3. Develop a flexible implementation plan for positioning the District to be able to participate in multiple markets.

4. Continue to beneficially use biosolids and maintain conformance with the National Biosolids Partnership (NBP) Code of Good Practice.

The Plan includes an analysis of potential technologies and markets for biosolids derived products, an analysis of treatment plant processes to reduce overall biosolids handling and treatment costs, and a long range implementation strategy.

The following is currently being implemented based on the Plan's recommendations:

1. Employing new in-plant technologies to reduce the volume of Biosolids handled by the District's two treatment plants, as follows:

    - Replacement of existing belt filter press dewatering equipment with centrifuges.

    - Replacement of existing secondary sludge dissolved air flotation thickening equipment with gravity belts.

    - Installation of primary sludge thickening equipment.

2. Transitioning to the production of Class A biosolids products using established and reliable technologies.

3. Establishing and maintaining failsafe backup options for 100% of the biosolids produced at OCSD.

4. Working with member agencies and local stakeholders to develop in-county production facilities and markets.

5. Moving into the following markets using vendor contracts for providing processing facilities, product distribution, and marketing:

   - Energy and fuel production
   - Heat dried granular products
   - Heat drying with soil reclamation
   - Compost
   - Organo-mineral fertilizers

In order to quickly transition from Class B to Class A biosolids production before the Class B market collapsed, requests for proposals were submitted requesting services and facilities to support the District's Long Range Biosolids Management Plan. After completing an extensive request for proposal process in April 2005, the Board approved a contract with EnerTech Environmental, Inc. to convert the District's biosolids to a renewable fuel at their Regional Biosolids Processing Facility in Rialto, California. The EnerTech's solution is a relatively new, patented heat treatment process. The patented process increases the ability to dewater biosolids in order to maximize the efficiency of the production of fuel. By decreasing the moisture content of biosolids prior to drying, a smaller dryer is needed, thus reducing capital and energy consumption. The fuel product will be totally recycled and reused, under agreements with area cement kilns and other fuel users. Residual ash from the fuel combustion becomes part of the cement product, resulting in no residual waste product liability. EnerTech proposes to finance, design, construct, and operate this 625 ton per day facility. Several local governmental agencies have previously committed approximately 275 tons per day of biosolids to this project and this project has now become economically viable with the commitment of 200 tons of biosolids per day from the District.

In addition to the contract awarded EnerTech, the Board also approved a contract with Synagro to provide for biosolids composting in Kern County at $63.09 per ton. The EnerTech and Synagro long-term contracts will service approximately two-thirds of OCSD's future biosolids production.
Staff is currently investigating biosolids-to-energy technologies and markets for the remaining one-third of the District's biosolids production because of the concern that biosolids composting markets are being saturated which could result in de-valuing of the product, making it non-sustainable. The private sector significantly invested in developing biosolids-to-energy technologies which enables wastewater agencies to participate in proven and sustainable markets. Staff will also be investigating biosolids management via deep-well injection and methane production which is currently being evaluated by the City of Los Angeles. Following are future cost implications under the various alternatives for the disposal of the remaining one-third of District's future biosolids:

- Energy Production: $85/ton – Annual Cost = $7.8M
- Deep Well Injection: $40/ton – Annual Cost = $3.7M
- Landfill Disposal: $60/ton – Annual Cost = $5.5M

Urban Runoff
In June 2002, AB1892 was passed that allows the District's charter to include permissive language authorizing the diversion and management of dry weather urban runoff flows. This bill allows the District to acquire, construct, operate, maintain, and furnish facilities for the diversion of urban runoff from drainage courses within the District, the treatment of the urban runoff, the return of the water to the drainage courses, or the beneficial use of the water.

The passage of this bill allows the District to divert up to 10 million gallons a day and consider more extensive options, such as building artificial wetlands that would naturally filter the runoff, or building a runoff treatment plant, similar to a $9.5 million facility built in Santa Monica that recycles 500,000 gallons of runoff a day.

For some time now, Orange County's beaches have been affected by storm water and urban runoff pollution. As a result, the Santa Ana Regional Quality Control Board has taken direct action to control discharge of pollutants to tributaries and recreational water bodies in Orange County by issuing a Storm Water Permit to the County and cities. In order to comply with the provisions of the permit, the County and cities have increased resources to fund municipal storm water/urban runoff management and treatment services. However, this effort has been difficult to sustain given the complexity of the program and the competing demands on limited resources.

The District, the County and other local agencies, are currently considering whether to explore public support for levying a fee to property owners to fund regional storm water/urban runoff management and treatment services within Orange County.

Groundwater Replenishment System
The District has shared in construction costs for Phase I of the Groundwater Replenishment (GWR) System with the Orange County Water District (OCWD), with each agency splitting the cost of construction of this facility equally. Phase I will reclaim up to 70 million gallons per day (mgd) of water, becoming the largest water reclamation project in the world. The GWR System will defer the need to build a second outfall estimated at a cost of $200 million.

Phase I of the GWR System became operational in January 2008. The District and OCWD have agreed to match the funding for this project. The District had previously budgeted $248.4 million for this project with the final wrap-up construction outlays of $2.8 million to occur in FY 2008-09. The District has shared equally with OCWD in approximately $44 million of Federal and State Grants in offsetting total project costs.

Pioneering work to develop the world's largest water purification plant for groundwater recharge has earned the Orange County Water District and the Orange County Sanitation District, California, USA, the 2008 Stockholm Industry Water Award. The Stockholm Industry Water Award honours and encourages business sector contributions to sustainable development in the water sector and is presented each August at the World Water Week in Stockholm. It was established in 2000 by the Stockholm Water Foundation in collaboration with the Royal Swedish Academy of Engineering Sciences and the World Business Council for Sustainable Development.

Fiscal Policies
Included within Section 3 – Pages 1 through 8 is a listing of the District's Board Adopted Fiscal Policies. These fiscal polices were established for the purpose of:

- sustaining a financially viable Sanitation District;
- having the flexibility to adapt to local and regional economic changes; and
- maintaining and enhancing sound fiscal condition of the District.

Included within the District's fiscal policies are specific polices for Budgeting, Revenues, Expenses, Capital Improvements, Vehicles, Short-term Debt, Long-term Debt, Reserves, Investment, and Accounting, Auditing and Financial Reporting.

GFOA Recommended Practices
Included in the budget within Section 3 – Pages 9 through 15 is a listing of the 124 accounting, auditing, financial reporting, cash management, budgetary and fiscal policy, debt management, retirement and benefit administration, and economic development and compliance planning practices recommended by the Government Finance Officers Association of the United States and Canada. Included within this list of best financial practices for state and local governments is the District's status as to whether we are in compliance or in progress towards compliance, or whether the practice is applicable to this agency. Out of these 124 practices, the District is in compliance with 84, 35 are not considered applicable to the District, and we are in the process of complying with the final five.

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The District's Business plan is intended to be an overarching plan based on sound decision making that provides direction on the work that the District will take on during the next two-year budget cycle and what will be deferred. This Plan is the underlying foundation for the development of the District's Budget.

During the process of developing the Plan, the District's Executive Management Team reviewed the proposed work for the upcoming year, balance it with the staffing and funding resources needed and either approve the plan or make reductions. Reductions in work or resource commitment for the coming year will be considered in light of the Level of Service that the agency is committed to and appropriate levels of risk.

Updates to the Business Plan are performed on an on-going basis, to be developed ahead of the bi-annual budgeting process, and will ultimately have a five-year horizon.

Each year, it is staff's intent to build upon the foundation of the previous Business Plan and to make each succeeding Business Plan more detailed and comprehensive. Included in this first Business Plan was the following elements: (1) Business Planning Process; (2) Current and Projected Key Performance Indicators (Level of Service); and (3) 2005 Asset Management Plan Summary.

The previous version of the Business Plan included (1) the ten most critical strategic initiatives; (2) performance results pertaining to the Current and Projected Key Performance Indicators (Level of Services); (3) Two-Year Staffing Plan; (4) Financial Model Update; (5) Risk Assessment & Mitigation Analysis; and (6) Asset Management Plan II.

Additions to the FY 2008-09 and FY 2009-10 Business Plan includes further development of the District's comprehensive Strategic Plan will include: (1) the steps required to complete each initiative; the timeframe and milestones for the completion of each step; and the resources required for each step; (2) Business Accountability Charters for each department, and each division within the departments; and (3) strategies to minimize risks identified within the District's current risk assessment profile.

Business Plan Process

The framework for the current Business Plan was developed as part of the process of creating the Five-Year Strategic Plan that was issued in November 2007. Beginning in the summer 2007, the General Manager's Office initiated the process of creating the Strategic Plan, soliciting assistance from all levels of the organization. Input included meetings with staff members who helped to retool the Mission Statement, Vision Statement and Core Values during a series of management workshops and Executive Management Team retreats. This was followed by a series of four workshops with the Board of Directors to provide additional input and direction. As a result, the Strategic Plan addresses major objectives and critical challenges facing the District now, in the next five-years, and further into the future. This Strategic Plan also laid down the foundation for the development of the Business Plan as it addressed critical operations and construction issues, financial and budgeting challenges, and gave a clear and concise direction from the Board of Directors to staff, ratepayers, regulatory agencies, and the general public.

The Business Plan development process started with the initiatives and direction identified within the Strategic Plan. Staff from across the agency further defined these initiatives in terms of level of service, business risk exposure, capital and operational costs, staffing, and long term financial impacts. The Business Plan identifies the required resources and prioritizes projects and initiatives, with recommendations for which initiatives should go forward for inclusion in the District budget, and which should be deferred or dropped from consideration.

Strategic Initiatives

Over the next two years, the District will begin and complete many activities central to the goals of the organization. As part of the strategic planning process, Staff has reviewed all of the initiatives and has identified ten that it would consider highly strategic and worthy of particular focus:

1. Succession Planning
2. SARI Sewer Line Relocation
3. Environmental Compliance Management
4. Odor Nuisance Management
5. Facilities Master Plan Update
6. Energy Master Plan
7. Reclaiming SARI Line Sewer Flows
8. Managing a Sustainable Biosolids Program
9. Making North County Yard Operational
10. Enhancing the District's Security Plan

Resources have been reallocated from lower priority activities within the organization to support these strategic initiatives.

Staff will report quarterly to the General Manager on the progress of each initiative. In parallel, the General Manager will begin the development of a comprehensive strategic plan and District goals for the Board review and adoption.

Level of Service

In 2005, the Orange County Sanitation District first developed a summary of the District's present and future Levels of Service requirements as part of its Asset Management Program. These Levels of Services were further developed with the Business Plan along with measurable outcomes, or key performance indicators, that the District is committed to meeting. This Business Plan documents that the Levels of Service provided by the District will increase significantly, requiring $1.4 billion in identifiable capital improvements and millions in increased maintenance and operations costs over the next ten years.

One area where the District's Level of Service will increase significantly is the quality of effluent that is provided to the Orange County Water District for reclamation or for discharge into the ocean. In 2002 and 2003, three commitments were made that increased this Levels of Service:

1. The District's ocean discharge will meet secondary treatment standards by 2013;

2. The District will provide effluent disinfection to reduce the coliform bacteria content at its outfall to less than the maximum concentration allowed at the beach under California Assembly Bill 411; and

3. The District will provide 70 million gallons a day of secondary effluent satisfying the quality and quantity requirements of Groundwater Replenishment System that began operations in January 2008.

The District is also studying further reduction in the offsite odors from its treatment plants and reducing its emissions of air toxics. The District's Levels of Service will also improve in the area of biosolids management. The District is moving from a 60-40% blend of Class "A" and Class "B" biosolids management options to a 100% Class "A" product.

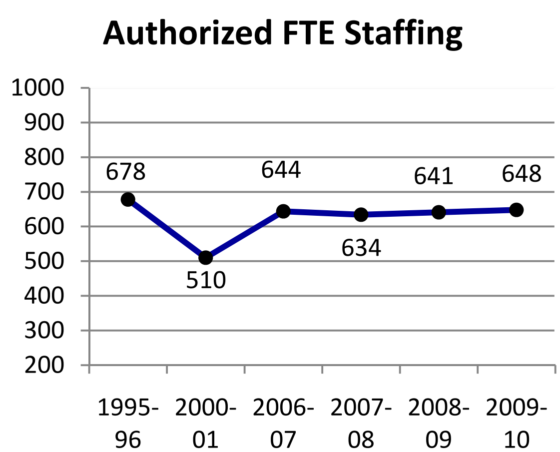
These Levels of Service improvements, along with maintaining the existing performance levels, require a series of annual rate increases and borrowing to ensure that the District maintains the reserves and debt coverage ratios that are included in the Business Principle Key Performance Indicators. The District's present and projected Levels of Service are shown within this section on page 27 through 32.

The District will continue to conduct studies and monitor regulatory trends that may change its level of service beyond 2013. There is a developing area of research concerning contaminants in treated wastewater effluents such as personal care products and pharmaceutically active compounds that are suspected of causing reproductive or other health changes to marine life in receiving waters. These compounds are also subject to research regarding reclaimed water quality. Further changes to the District's source control program and treatment processes could be required to address these concerns as further research defines the problems and potential solutions.

Staffing Plan

A comprehensive review was completed on the District's staffing levels for the next two fiscal years. This undertaking began with a review of the District's vision, mission, goals and objectives as part of the development of the Five-Year Strategic Plan.

This analysis included identification and development of over 110 business units in the District with discreet duties and responsibilities.



Based on the needs of the agency overtime, total FTE requirement have fluctuated greater from a high of 678 authorized FTE's in FY 1995-96 to a low of 510 in FY 2000-01 back up to a newly proposed high of 648 authorized in FY 2009-10 for the operation and maintenance of newly constructed secondary treatment facilities scheduled to come on line as the District strives to meet full secondary treatment standards by December 31, 2012.

Based on the increase of 138 FTEs since FY 2000-01, staff has taken on the challenge of moving towards full-secondary treatment standards while minimizing the increase in total FTE head count over this two-year planning period.

Instead, staff has focused on the reallocation of existing resources in order to balance the needs within the over 110 identified business units of this agency to ensure that core business operations are met, levels of service are maintained, and that strategic initiative elements are accomplished.

In conclusion, the proposed two-year staffing plan contains a significant level of analysis on how existing resources can be utilized in consideration of the increased demands placed on this agency by secondary treatment standards and in support of the $1.4 billion capital improvement program over the next ten years while minimizing the increase in staffing levels. This budget, therefore, proposes staffing increases of 7 FTE's for FY 2008-09 and for FY 2009-10, raising the previously approved FTE count from 634 FTE's in FY 2007-08 to 641 FTE's in FY 2008-09, and to 648 FTE's in FY 2009-10. A detailed breakdown on the proposed reallocation of FTE's can be found within the Appendix section of this budget.

Financial Model Update

The last time a rate study was completed for the District was in July 2006, and previous to that was in 2002 and in 1999. It has been the practice of the Sanitation District to complete a rate study following the completion of a strategic plan update. A strategic plan update is the review of the OCSD collection, treatment and disposal systems to determine a comprehensive strategic approach to manage wastewater flows through the year 2020, and in a way that protects the public health and is technically feasible, enviornmentally responsible, and economical. However, the following four drivers necessitated that a rate study be completed as part of this Business Plan:

1. **The Necessity of a Local Sewer Service Fee -** The District provides regional sewage collection, treatment, and disposal services to approximately 550,000 customers located in central and northwest Orange County and collects fees for these services through a special assessment on the Orange County property tax bill. In addition, the District also maintains, repairs, and replaces the local sewers for approximately 17,000 of the above 550,000 at no additional fee. All customers other than these 17,000 are also paying a local sewer service fee to their local city or special district. A sewer rate study needed to be completed for these 17,000 customers in order to initiate a local sewer service fee to eliminate the subsidization of their local sewer service by all 550,000 regional customers.

2. **Including the Cost Impacts of Strategic initiatives –** The November 5-Year Strategic Plan increased the levels of service for managing air toxins, odor control, and biosolids. The finanical impacts resulting from the outcome of these board approved initiatives needed to be addressed in an updated sewer rate study.

3. **5-Year Proposition 218 Notice-** The District's last California Proposition 218 Notice notifying rate payers of potential sewer rate increases over the past five-years had expired and a new 5-year Proposition 218 Notice approved by the Board and the justification of the new sewer service fee rates over the next five years needed to be supported by an updated sewer rate study.

4. **Development of a Uniform "Net Cost of Service" Rate Methodology -** The sewer rates of high strength dischargers under permit were previously developed gross of property tax revenues. A recent independent sewer rate validation study recommended that a uniform "net cost of service" rate methodolgy be developed and applied to all rate payers that would be fair and equitable to all ratepayers.

In November 2007, the District contracted with an Engineering firm to complete a financial model update for FY 2008-09. The purpose of this engagement was to evaluate the District's wastewater utility revenue needs, and develop sewer service rates and wastewater capital facilities charges to equitably distribute costs among utility customers.

In their Financial Model Update Report for the District issued in April of 2008, Carollo Engineers recommended that the District:

- Based on current operational and capital project assumptions, implement annual increases of 10.5, 10.0, 10.0, 9.8, and 9.8 percent, respectively, over the next five years.

- Increase the unit costs to high strength discharges as follows:

	gallons	B.O.D.	S.S.
Current Unit Cost	0.77	0.35	0.52
Proposed Unit Cost	0.84	0.4	0.42
% Increase	9.1%	14.3%	-19.2%

- Increase the capital facilities capacity charges (CFCC) and the supplemental CFCC by the Engineering News Record Construction Cost Index of 3.4% of the prior year, or as follows:

	Residential CFCC	Commercial/ Industrial CFCC
Current Unit Cost	$4,517	$1,357
Proposed Unit Cost	$4,671	$1,403
% Increase	3.4%	3.4%

	$/ 1,000 gallons	$/ lbs B.O.D.	$/ lbs S.S.
Current Unit Cost	$1.392	$0.781900	$0.095022
Proposed Unit Cost	$1.440	$0.808563	$0.098262
% Increase	3.4%	3.4%	3.4%

- Implement a Five-Year Local Sewer Service Fee for 18,000 parcels located in City of Tustin and in unincorporated areas North of Tustin beginning in FY 2008-09, as follows: $199, $204, $208, $212, and $216, respectively, through FY 2012-13.

All recommendations from the Financial Model pertaining to CFCC fees were approved to ensure that the funding required for the additional capacity projects required for new users would be available at the time of construction.

Risk Assessment Analysis

Many leading organizations are formally applying risk management processes to identify and mange risks across many aspects of their business. The formalization of risk management processes is a logical step towards increased accountability and transparency placed on the Board and District management.

In February 2006, strategic level risk assessment and mitigation workshops were completed by the District's Executive Management Team and District Managers. The aim of the risk assessment and mitigation workshops was to

- identify and assess strategic and organization-wide risks facing the District and to develop a high level risk register;
- identify mitigation measures that the District currently has in place;
- Propose additional mitigation measures that the District considers appropriate to manage; and
- Develop an action plan of responsibilities and timeframes for follow-up.

Business Risk was defined by the workshop participants as a threat that an event, action or inaction will adversely affect an organization's ability to achieve its business objectives and execute its strategies successfully.

The next steps in the development of Risk Management include:

- Completion of the risk register including mitigation strategies (current and proposed) responsibilities, and timeframes;
- Consider independence in the process to ensure a level of integrity in the process without transferring ownership and responsibility;
- Review of risk register to ensure it represents a balanced portfolio of the risks and that the mitigation strategies are appropriate;
- Develop a plan to monitor the effect of mitigation strategies to ensure that controls are in place and effective;
- Develop a formal reporting process to the Board that includes possible revisions to the overall risk profile; and
- Develop protocols to provide assurance to stakeholders that in the annual strategic business plan processes are in place to manage risks organization wide.

The District's Risk Manager has proposed a detailed plan for carrying out the steps mentioned above. That plan is currently under review by

District management for possible implementation in calendar year 2008.

Asset Management

In December 2002 the Orange County Sanitation District (OCSD) Board adopted their "Asset Management Strategic Plan and Framework Analysis" (Strategic Plan). The Strategic Plan defined Asset Management for OCSD as; "to create and acquire, maintain, rehabilitate, replace and augment these valuable wastewater assets in the most cost effective (lowest life cycle cost) sustainable manner at the level of service required *by present and future generations of regulators and customers at an acceptable level of risk.*"
OCSD has taken several steps to sustain this vision since the Strategic Plan was adopted. This has included the development and implementation of many different asset management tools to obtain better information to make better decisions. The most recent effort includes working with the Water Environmental Research Foundation (WERF) and American Water Works Association Research Foundation (AWWARF) on research programs to advance asset management tools and establish standards for bench marking. This will help other utilities and provide improved asset management tools for OCSD's use.

One of the most important asset management tools OCSD created was an Asset Management Plan. This completed in 2005 and was the first one created. OCSD has continued to develop this document to better understand its short-term and long-term business obligations related to the assets that it currently owns and will own. It also reveals how the business decisions related to these assets will affect the ability to sustain the asset performance and consequently sustain the conditions of cost-effective services to customers. OCSD has traditionally performed many of these tasks across the organization; however prior to 2005, the results of this work had never been compiled into a single document to allow the organization to clearly understand the overall business ramifications

<u>Recent improvements</u>

As part of the annual ongoing asset management and business planning processes within OCSD the following efforts continue:

- ► Asset Management Plan has just undergone a two-year revision:
  - o Modeling information was re-run. This allowed for tables, figures and text to be updated and includes useful rate planning information for the Finance department.
  - o Asset Management System Summaries data was updated for both plants. This is at the process level and looks at condition, demand vs. capacity, function, reliability, and business efficiency, which complement the Engineering Department Master Plan updating effort;
- ► New collaboration efforts with WERF to advance asset management will improve the following tools:
  - o Public communication tools that utilities can use to engage decision-makers and ratepayers understand the need for strategic asset management and infrastructure investment.
  - o Best appropriate practices for asset management among utilities, as well as development of case studies that utilities can use to learn how to implement WERF's Strategic Asset Management tool.
  - o Development of tools for decision analysis and implementation of asset management practices. This includes a cost tool and a refined gap tool that helps utilities to compare their asset management practices to those of other utilities. These tools will allow agencies to benchmark against each other.
  - o Develop models for predicting the remaining asset life for both above and below-ground assets. This will complement the risk-based modeling approach used to date for OCSD condition assessment and CCTV programs;
- ► Future participation with AwwaRF to expand on the efforts of the WERF Asset Management advancement efforts. This effort will focus on key asset data for utilities, which will result in the establishment of data standards.
- ► The Risk Plan developed in 2006 continues to be a tool for the Executive Management Team, which provides an ongoing process for managing organizational risk;

► The Condition Assessment Guidelines developed in 2006 continues to be a resource for staff to perform condition assessment of our plants and the collection system;

Levels of Service
For the 2005 Asset Management Plan, OCSD developed a summary of its present and future Levels of Service requirements using the international triple bottom line categories. This documented the measurable outcomes, or key performance indicators that OCSD is committed to meeting under each of the following categories: Environmental, Social, and Economic. In 2006, these performance categories were modified to be consistent with OCSD Core Strategies. This placed additional importance on OCSD environmental responsibilities as demonstrated with the new categories: Environmental Stewardship, Wastewater Management, Business Principles, and Workplace Environment. In 2007 OCSD executive management refined the goals for these categories and gained the support of the Board of Directors by involving them in the process and obtaining their approval. Overall OCSD Levels of Service will increase significantly as a result of its large capital investment program. This will result in millions in increased maintenance and operations annual costs due to these future changes.

Some of the major Levels of Service that will or have changed include:

- Adopting 100% Secondary Treatment Standards
- Adopting 100% Class “A” Biosolids
- Increasing reclamation to 70 mgd
- Reducing odor complaints
- Fire and Safety Code Compliance

Inventory of Assets
Understanding our asset characteristics is critical to our continued success. Our assets can generally be split between two main groups: Collection System – the assets responsible for the collection and transfer of sewage from the cities to the treatment plants, and; Treatment and Disposal – the assets that treat the sewage and dispose of the treated effluent and byproducts.

The following charts present the investment history in both of these systems and the age profile of these assets.

Figure E1 – Collection System (Weighted Average Life)

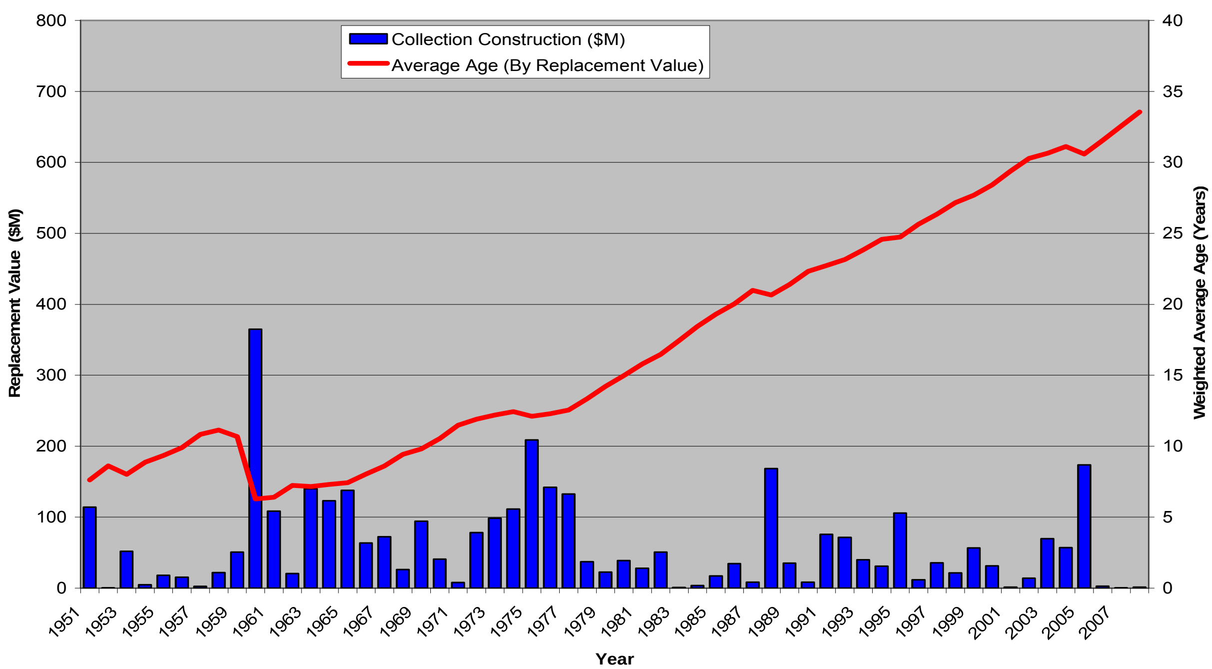
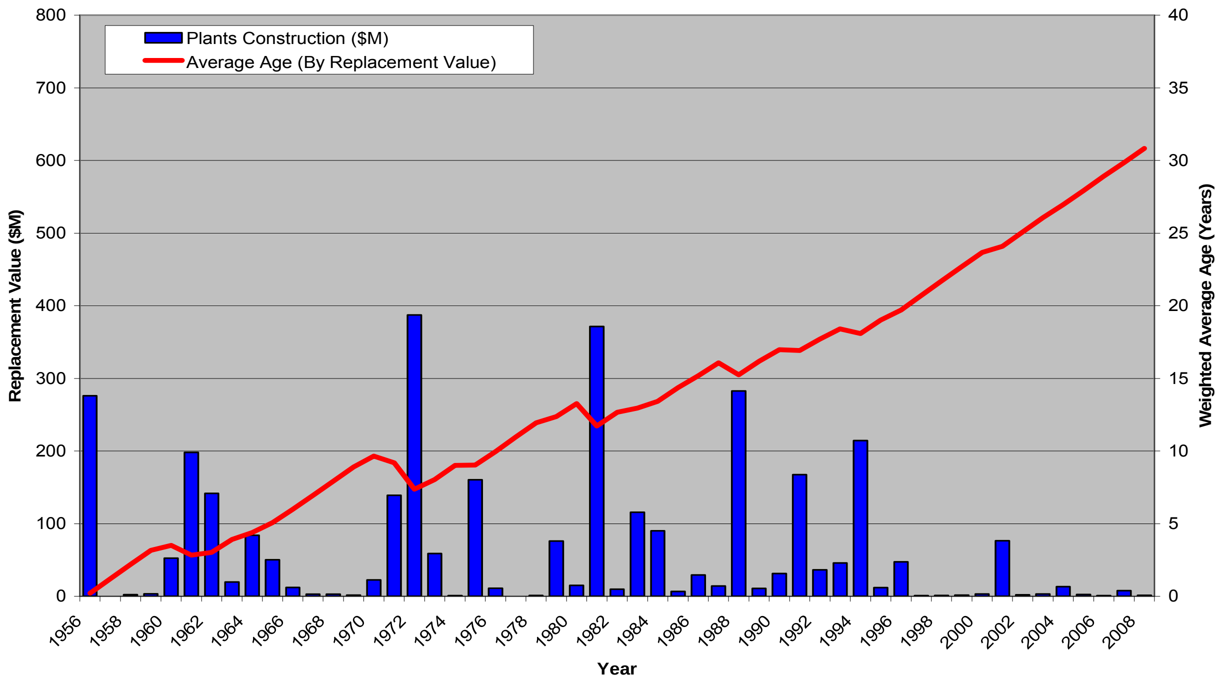


Figure E2 – Treatment Plants (Weighted Average Life)



This average age and value of the assets OCSD own is increasing steadily over time, the latent asset replacement obligation is rising, and as a consequence, OCSD needs to be planning for decreased capital projects for expansion and increased renewal expenditures in the future relative to past expenditure levels. Additional focus will need to be given to ensuring that appropriate operation and maintenance strategies are being applied that consider the different ages of assets being maintained.

Asset Valuation

The replacement valuation for all of OCSD's assets has been updated. The table below presents the current replacement and depreciated values of OCSD's assets. The replacement value represents the cost for December, 2007 dollars to completely rebuild all the assets to a new condition. The depreciated value is the book value of the assets based on their current condition.

The current replacement value is estimated to be $6.26B, which compares to the 1998 prediction of $2.03B, which was based on original purchase cost. This will increase by 2012 to approximately $7.1B after the completion of the existing three billion dollar Capital Improvement Program. The major reasons for this increase are all the new assets added to the asset register and basing the replacement costs on a metropolitan environment rather than a vacant land situation.

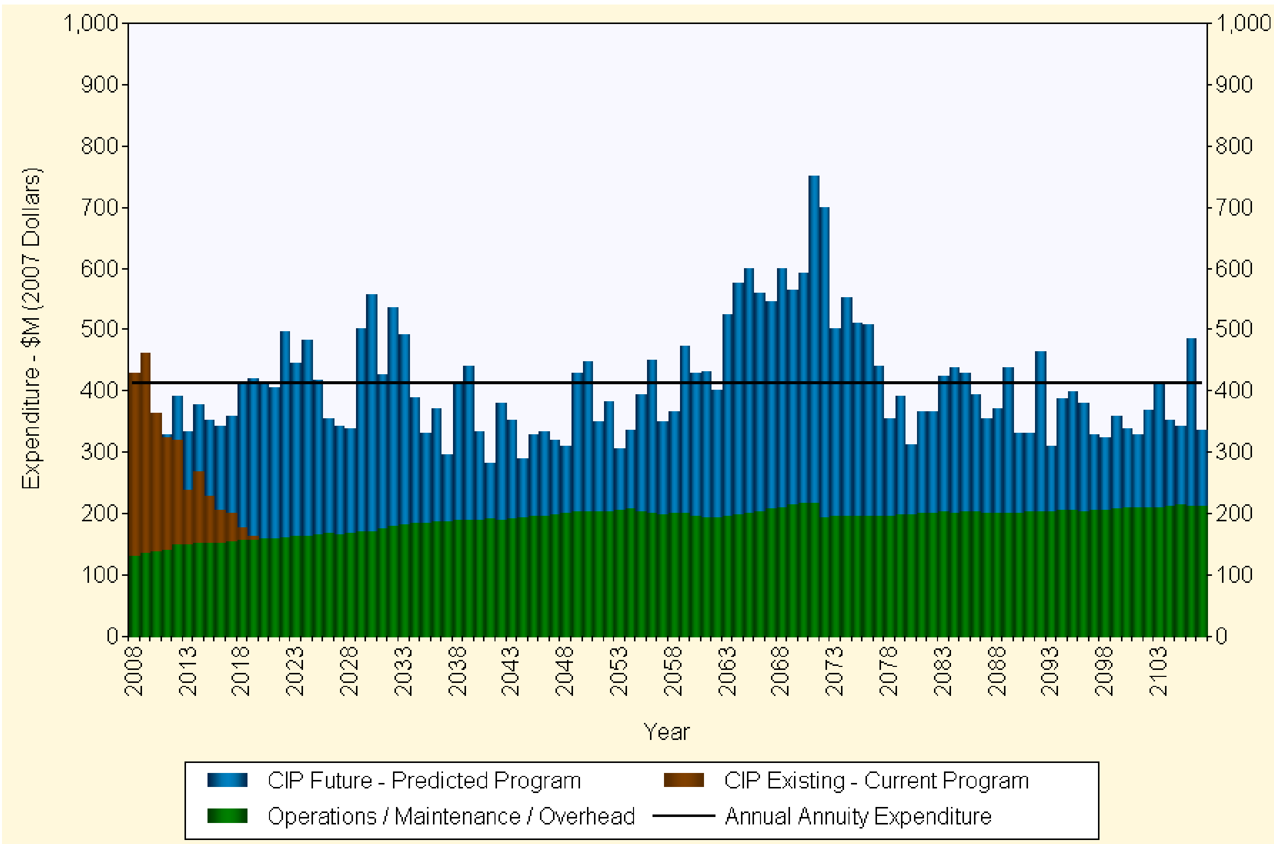
Valuation	Plants	Collection	Total
Replacement Value ($B)	3.12	3.14	6.26
Depreciated Value ($B)	1.67	1.79	3.46

Planned Expenditure

A computer model was developed to produce the future expenditure aspects of this Asset Management Plan. This model was used to perform a series of calculations on information related to the current and future OCSD assets. The following chart is the result of the modeling work undertaken, including current and predicted future Capital Improvement Program projects and operations (including maintenance), improved understanding of asset life and asset condition. The model has been revised to account for business rules for future CIP projects.

The flat black line is the average of all the future cash flows, which represents the average expenditure ($411M current value worth) required by OCSD for each of the next 100 years. The actual annual expenditure will vary depending of the actual work required. At present the expenditure is greater due to the accelerated building program, however, additional income in the future will also be required to pay back the capital that is currently being borrowed.

Figure E3 – OCSD Expenditure – Total Future Predicted Cash Flows



Future Funding Requirements

The predicted overall expenditure in future years will not “drop off” as dramatically as previously predicted after the current Capital Improvement Program spending drops off significantly in approximately five years. This means that pressures on rate increases are likely to grow more than previously thought. Fully funding the replacement and rehabilitation costs of the assets will mean that the likely scenario is greater-than-inflation rate increases over the next 20 years.

Future Efforts

In order to move forward with Asset Management, the District will need to:

- Continue to be selective of the Capital Improvement Program projects based on economic justification and risk presented to OCSD in order to free up available funds and staff resources to concentrate on other areas of greatest risk;

- Continue to validate future maintenance program and workload with a view toward investing in maintenance where it will defer capital. Some observations have indicated that an increase in maintenance expenditures could result in deferred capital investments and a reduction in life-cycle costs (this is especially relevant for civil

- assets). Also, an increased understanding of the future maintenance costs associated with capital projects will help to identify the potential impacts on the maintenance program;

- Continue to improve the existing data standards, processes and data collection programs;

- Continue the effort to implement an information system strategy to ensure that this data collection and data flow is stored and recovered / manipulated to suit the needs for planning and optimizing future asset management decision making;

- Continue the implementation of a works management system and workload allocation / justification / prioritization system for all Engineering, Operations and Maintenance activities;

- Consider ways to influence customer expectations while working to try and to avert or reduce the cost impacts of current and future levels of service;

- Review management strategies and design guidelines with a view to considering revised redundancy requirements.

Next Steps

A number of improvement tasks have also been identified for future years to improve the overall accuracy and coverage of the Asset Management Plan. This includes completing Business Risk Exposures for the asset system summaries, and using more accurate data as it is collected for the models.

Future editions of the Asset Management Plan are critical to the work OCSD is planning for improving its overall asset management performance. Many of the improvements to future Asset Management Plans will derive from other work that is planned to be undertaken across the organization. Sustainability and cultural organizational change are important issues for the Asset Management program, and they need to be well managed to ensure the ongoing improvement in stewardship of the OCSD assets

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Wastewater Management

OCSD beneficially reuses and recycles water and other resources using safe and effective wastewater systems. Goals to support the Wastewater Management Level of Service include:

1. **Sustainable Biosolids Program –** Prepare request for proposal or sole source for selecting a technology for managing the remaining one-twhird of our biosolids capacity. Develop long-term agreement and implement management option. Evaluate the feasibility of deep well injection/methane recovery including commissioning a study of the geological formations below Plants 1 and 2, and availability and acceptability of any existing wells; and processing some of our biosolids at the City of Los Angeles Terminal Island demonstration well. Complete new In-county Compost Take-Back Program Plan strategy.
2. **Implement Energy Master Plan –** The Energy Master Plan is in final stages and will provide recommendations to ensure adequate power resources and energy management.
3. **Odor Control –** Implement Odor Control Projects at Plant 1 (trickling filters) and Plant 2 (solids loading facility) by 2016.

Wastewater Management Levels of Service

OCSD will provide an effluent quality suitable for protecting public health and being a source for water recycling.	**FY 08-09 Target**	**FY 07-08 Results**
Concentration of emerging chemical constituents of concern in Plant No. 1 secondary effluent	NDMA* < 150 ppt 1,4-Dioxane < 2ppb	Not Analyzed
Thirty-day geometric mean of total coliform bacteria in effluent after initial dilution of 180:1	<1,000 mpn	148
Industry permit compliance to discharge into OCSD sewers	100% permit compliance	100%
Meet secondary treatment standards	BOD 100 mg/L TSS 55 mg/L	45 33
OCSD will manage flows reliably.	**FY 08-09 Target**	**FY 07-08 Results**
Frequency of use of emergency one-mile (78-inch diameter) outfall	0 per year during dry weather, less than once per 3 years in peak wet weather	0
Sanitary sewer spills per 100 miles	<2.1	<2.1
Contain sanitary sewer spills within 5 hours	100%	100%
OCSD effluent will be recycled.	**FY 08-09 Target**	**FY 07-08 Results**
Provide up to 104 mgd specification effluent to the Groundwater Replenishment System	104 mgd	35.1 mgd (11/07)
OCSD will implement a sustainable biosolids management program.	**FY 08-09 Target**	**FY 07-08 Results**
National Biosolids Partnership Certification for Biosolids Environmental Management System	Maintain certification	Maintained
Percent of biosolids recycled	>95% recycled <5% landfill	100% recycle 0% landfill

Environmental Stewardship

OCSD participates collaboratively in the protection of regional water resources for the benefit of the people we serve. Goals to support the Environmental Stewardship Level of Service include:

1. **SARI Line Relocation –** Support the County of Orange Resources and Development Management Department effort to relocate the SARI Line by 2011.
2. **Management System for Environmental Compliance –** Implement a management control system for environmental compliance information that incorporates a "dashboard" reporting approach.
3. **Contaminants of Potential Concern (CPC) –** Complete three phase testing and analysis of 550+ CPC, prepare report on findings and recommendations, develop initial source control strategy if there are CPCs identified that require control.
4. **Climate Change/Greenhouse Gases –** Complete development of statewide emission inventory protocol for Publicly-owned Treatment Works and submit mandatory emission inventory to the California Air Resources Board for FY 07–08.
5. **Engine Emission Compliance –** Complete study to evaluate alternatives for complying with lower emission limits in the South Coast Air Quality Management's Rule 1110.2. Initiate planning and design of demonstration testing of the most promising technology(s) identified in the study.
6. **Reclaiming SARI Line flows –** Meet with stakeholders, develop a list of obstacles that need to be overcome to reclaim the SARI Line, and develop an initial strategy for obtaining regulatory approval to allow SARI Line flows to be treated at Reclamation Plant No. 1.

Environmental Stewardship Levels of Service

OCSD will protect public health and the environment.	**FY 08-09 Target**	**FY 07-08 Results**
Provide capacity to collect and treat dry weather urban runoff	Up to 4 mgd	1.59 mgd/month
Maximum off-site odor impact (in D/T*) • Reclamation Plant No. 1 • Treatment Plant No. 2	 42 D/T 48 D/T	 42 D/T 48 D/T
Air emissions health risk to community and employees per one million people	<10	<10
Permit compliance (air, land, and water)	100%	100%
OCSD will be a good neighbor.	**FY 08-09 Target**	**FY 07-08 Results**
Odor complaint response: • Treatment Plants within 1 hour • Collections System within 1 working day	 100% 100%	 100% 100%
Number of odor complaints: • Reclamation Plant No. 1 • Treatment Plant No. 2 • Collection System	 32 4 34	 28 7 14
Restore collection service to customer within 8 hours	100%	100%
Respond to collection system spills within 1 hour	100%	100%

Workplace Environment

OCSD provides an environment of partnership, growth, opportunity, responsibility and accountability. Goals to support the Workplace Environment Level of Service include:

1. **Succession Plan –** Implement the elements of the succession plan including management training and the creation of a Leadership Academy to train future leaders.
2. **Improve the Sanitation District's Security –** Provide long-term security enhancements at both treatment plants and within OCSD's Collections System.
3. **Space Planning Study Recommendations –** Complete relocations of staff housed in Information Technology Trailers, Administration Building, Control Center and Building 6.
4. **North County Yard –** Open the North County Yard and training facility and complete the relocation of selected staff and equipment to the facility. Implement flex space for added agency-wide needs as appropriate.
5. **Safety and Health Strategic Plan –** Develop and implement a Safety and Health Strategic Plan for all Sanitation District activities.

Workplace Environment Levels of Service

OCSD will take care of its people.	FY 08-09 Target	FY 07-08 Results
Training hours per employee	45 per year	34
Employee injury incident rate of 5.2	Industry average	District 5.8 O&M 2.6
Mandatory OSHA training requirements	100%	13%
Annual employee volunteer participation in programs that enhance safety and security culture and awareness	15% per Division	Not implemented

Business Principles

OCSD makes every decision based on short and long-term environmental, societal, and financial impacts (the triple bottom line). Goals to support the Business Principles Level of Service include:

1. **Strategic and Business Plan –** With Board concurrence, annually update and implement the Strategic Plan and Business Plan.
2. **Review Interagency Agreements –** Conduct a comprehensive review of agreements with the Santa Ana Watershed Project Authority and Irvine Ranch Water District and, if appropriate, reopen for discussion.
3. **Enterprise Information Technology Strategic Plan –** Complete a District-wide information technology Strategic Plan.
4. **Complete Facilities Master Plan Update –** Complete a comprehensive update of the Facilities Master Plan and obtain Board approval.
5. **Sewer Rate for "Green Development" –** Submit for board approval an amendment to sewer rate ordinance with incentives for green developments.
6. **Business Accountability Charters –** Create BACs for each department consistent with BACs developed by managers and supervisors.
7. **Local Sewer Services –** Implement the Board's four recommendations based on findings of staff's Revenue Adequacy Report. Continue to seek an asset transfer to another agency. Also transfer other local assets back to cities that are not serving a true regional purpose.
8. **Annex Unincorporated Areas –** With board concurrence, annex unincorporated areas into OCSD's service area.

Business Principles Levels of Service

OCSD will exercise sound financial management.	FY 08-09 Target	FY 07-08 Results
COP service principle and interest	< O&M expenses	< O&M Expenses
Annual user fees	Sufficient to cover all O&M requirements	Sufficient
Annual increase in collection, treatment, and disposal costs per million gallons	<10%	9.92%
Annual variance from adopted reserve policy	<5%	0.18%

OCSD will be responsive to our customers.	FY 08-09 Target	FY 07-08 Results
Respond to public complaints or inquires regarding construction projects within 1 working day	>90%	>90%
New connection permits processed within one working day	>90%	>90%

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Strategic Initiatives for FY 2008-09 & FY 2009-10			
Initiative	**Strategic Importance**	**Desired Outcome**	**Next Steps**
1. Succession Planning	This program provides opportunities for staff to take on broader responsibilities and increases leadership proficiency, thus ensuring organizational viability/success.	Development of management training programs and Leadership Academy, and to provide an opportunity for all employees to participate.	Complete supervisor talent assessments, train mentors, and complete training cycle (12 topics) for the first and second groups (EMT, Mgrs., Supv.).
2. Santa Ana Regional Interceptor (SARI) Line Relocation	Ensure the stability of the SARI Line from floods.	Relocate the SARI from the bottom of the Santa Ana Riverbed to run alongside the riverbed.	Complete design and award construction contract by 12/15/09.
3. Management System for Environmental Compliance	Implement a management control system for environmental compliance information.	Continuous Monitoring and reporting of ongoing Environmental Compliance efforts.	Determine performance indicators for Air Quality, Biosolids, and Waste Discharge Requirements.
4. Odor Nuisance Management	To design and build odor control facilities that will comply with the odor control policy adopted by the Board.	Implement odor control trickling filers at Plant 1 and solids loading facility at Plant 2.	Develop the required 13 project milestones for an overall completion date to occur no later than 2016.
5. Facilities Master Plan Update to Maintain Sustainable Capital Impr. Program	Optimize investments in infrastructure while balancing level of service, risk, and user rates.	Identification of all capital improvement projects to be constructed out to 2030 and the timelines for completion.	Complete the five volume document by the end of calendar year 2008.
6. Implement Energy Master Plan	The Energy Master Plan provides options to ensure power resources & energy management	To ensure that adequate power is available in the future at the lowest possible cost to the District.	Complete project design and award construction to five energy projects totaling $45.6 million by January 2010.
7. Reclaiming Santa Ana River Interceptor (SARI) Line Flows	SARI would add 38 MGD of effluent for recycling.	Identify options that could be implemented with regulatory approval and minimal costs.	Conduct a study to determine issues, options, and potential solution by 06/30/09.
8. Manage and Optimize a Sustainable Biosolids Program	Biosolids Management is a major priority as low–cost options have disappeared.	Monitor the development of technologies for managing the remaining one-third of biosolids capacity.	Obtain proposals, negotiate long-term agreements, notify stakeholders, and obtain Board approval by 9/30/09.
9. North County Yard	This building facility was acquired for the purpose of staffing sewer collection crews closer to the work location.	Customize the existing facility to meet the needs of the selected staff and the housing of the needed equipment.	Award construction contract in FY 2008-09.
10. Enhance the Sanitation District's Security Plan	Long-term security enhancements at both treatment plants and throughout the sewer	To provide a safe and secure work place limiting access throughout the facilities to those	A Central CCTV station monitoring and security response system will be installed by the end of FY 2009-10.

OCSD Long-Term Planning

	Type of Planning Process	Description of Process	Budget Impacts
Development of a Five-Year Strategic Plan	Achieve a 5-year comprehensive strategic plan that addresses the sanitation health and safety needs of the 2.5 million people we serve.	In November 2007, the District's Board approved a 5-Year Strategic Plan that updated the District's Mission, Vision, Levels of Services, and Business Plan. Also included are the strategic objectives listed below.	The Strategic Plan was the foundation for the development of this two-year budget. The level of service identified within this document was the underlying basis for the Board to adopt rate increases of approximately 10 percent a year for the next five years.
Plan for Capital Improvements out to 2023	Plan, design, and build capital improvement projects (CIP) out to 2023 to meet the regulatory, environmental, health, and safety needs of a growing population.	District staff conducted strategic planning workshops with the Board of Directors to layout a capital program to deliver the levels of service desired by the Board of Directors. The approval of the strategic plan by the Board of Directors added $50 million of new capital projects over the next ten years.	The newly validated CIP Budget includes 114 projects with a 15-year cash outlay of $1.47 billion. This $149 million increase from the 2007-08 CIP budget includes $50 million from the Strategic Plan, $28 million in newly identified renewal projects, and $71 million in project budget revisions for on-going projects.
Biosolids Management	Aggressively pursue biosolid disposal alternatives for the remaining 1/3 of non-contractually committed biosolids production that make fiscal and environmental sense.	Staff is studying biosolids energy markets for the remaining 1/3 biosolids because of concerns that composting markets are saturated making this options non-sustainable.	Annual cost of remaining 1/3 biosolids options: Energy Production - $7.8M Deep Well Injection - $3.7M Landfill Disposal - $5.5 M
Odor Control	Direct sufficient resources and investigate new technologies to effectively deal with odor issues.	Design all new processes so that odors remain within 10 dilutions to threshold (D/T), or within treatment plant boundaries.	Two odor control projects have been added to the CIP totaling $18 million. Future O&M budgets will include annual increases of $300,000.
Air Emissions Control	Apply sufficient resources to meet regulatory requirements related to air emissions.	It is anticipated new air toxic emission regulations will require the installation of additional air pollution control equip.	An additional $31 million has been included in the newly validated CIP budget to address the new air toxic emission stds.
Groundwater Replenishment System (GWRS)	Continue partnership with the Orange County Water District in support of GWRS.	Maximize the use of treated effluent for water recycling to defer the need for second ocean outfall	The District will provide: 70 mgd of reclaimed water 50% of capital cost for Phase I 50% of Dioxane removal

Background Information and Description of Services:

The Orange County Sanitation District (the "District") is a public agency that operates the sixth largest wastewater facility in the U.S. Originally formed in 1954 pursuant to a joint powers provision under the County Sanitation District Act of the California Health and Safety Code, the District then consisted of independent special districts responsible for wastewater collection within their own geographical boundaries. These districts were co-participants in a Joint Agreement to provide for the joint construction, ownership, and operation of the District's Joint Facilities for the treatment and disposal of wastewater.

On July 1, 1998, the nine individual existing districts requested to be consolidated into one district by resolution of the Board of Supervisors of the County of Orange and special legislation.

The District is governed by a board of directors made up of mayors or members of city councils, directors of independent special districts, and one member from the County Board of Supervisors. A variety of board committees, made up of members of the Board of Directors, consider topics for action by the Board and make recommendations to the Board.

The District is responsible for collecting, treating, and safely disposing of approximately 250 million gallons of wastewater each day for an area covering 471 square miles in metropolitan (central and northwestern) Orange County. The District's service area includes approximately 2.5 million residents and businesses, or approximately 81 percent of the County's total population.

Professional staff of 641 full-time equivalent employees supports the District's around-the-clock operation. Staff is organized into four departments, including Administration, Engineering, Technical Services, and Operations and Maintenance.

As working environmentalists, the District's staff is regulated by many agencies, including the U.S. Environmental Protection Agency (USEPA), the California Regional Water Quality Control Board (CRWQCB), the California Integrated Waste Management Board, the California Environmental Protection Agency and the South Coast Air Quality Management District (SCAQMD). To maintain the District's operating permit, the District's plants must meet strict conditions set jointly by the USEPA and the CRWQCB.

The District operates under an ocean discharge permit issued by USEPA and the Santa Ana Regional Water Quality Control Board. This permit is renewable every five years and was last issued in December 2004.

The District maintains and operates a large system of trunk sewers and pumping stations in addition to the two modern treatment plants. The plants use chemical, physical and biological processes to produce a high-quality effluent. Chemicals used are either environmentally neutral or biodegradable.

Most of the treated effluent is combined and pumped through a five-mile, 10-foot diameter, ocean outfall pipe. The outfall has a one-mile long diffuser section that discharges treated water through more than 500 portholes four miles off shore. Some secondary effluent is pumped from our Fountain Valley plant to the Orange County Water District (OCWD) where it is further processed and distributed for reuse.

The OCWD and the District recently completed an additional joint project for water reclamation. In January 2008, the Groundwater Replenishment System project began reclaiming up to 70 million gallons of water per day for percolation into the groundwater basin. If successful and economical, the two agencies may expand the project in two additional phases to reclaim up to 130 million gallons each day by the year 2020.

Community Profile of the County of Orange

The County of Orange is bordered on the north by Los Angeles and San Bernardino counties, on the east by Riverside County, on the southeast by San Diego County, and on the west and southwest by the Pacific Ocean. Approximately 42 miles of ocean shoreline provide many beaches, marinas and other recreational areas for use by residents and visitors.

The climate in the County is mild, with an average rainfall of 13 inches. The mean temperature ranges from a minimum of 48 degrees to a maximum of 76 degrees.

The County has become a tourist center in Southern California by offering a broad spectrum of recreational opportunities that is enhanced by the mild climate. Along the shoreline are five state beaches and parks, five municipal beaches and five county beaches. There are two small-craft docking facilities in Newport Harbor, one located in Sunset Beach and another in Dana Point.

Other major recreational and tourist facilities include Disneyland, California Adventure, Knott's Berry Farm and Soak City, Mission San Juan Capistrano, the Anaheim Convention Center, and the Art Colony at Laguna Beach with its annual art festival. Also located within the County is Anaheim Stadium, home of the Los Angeles Angels of Anaheim of Major League Baseball, and the Honda Center, home of the Mighty Ducks of the National Hockey League.

Economic Outlook

Orange County enjoys a diverse economy with no single sector accounting for more than one-third of the county's economic output or labor market. Total payroll employment, the best measure of economic health for the local economy, was 1.56 million as of April 2008 according to the State Employment Development Department (EDD), down from 1.59 million, or 1.9 percent from one year ago.

Orange County is notable for the wealth of its residents, encapsulated by per capita and median family income figures which, as of the last census, stood at 113.7 percent and 121.9 percent of the state figures respectively. The economy currently is showing signs of weakness, with local economists suggesting a recession including some job loss. Unemployment has risen from 3.4 percent in March 2007 to 4.6 percent in March 2008; however, it remains well below the state unemployment rate of 6.4 percent. Assessed value (AV) growth in the district has been strong, particularly in recent years, with peak growth in 2007 of 11.9 percent. Growth in fiscal 2008 slowed to a still healthy 8.14 percent, resulting in $292.7 billion in total district AV. Projections for fiscal 2009 are for a significant deceleration of growth to 4 percent, less than half the prior year rate. While the local economy is currently undergoing stress, the long-term outlook remains strong.

However, the Housing prices in Orange County have taken a tumble. Based on California Association of Realtors' data, after reaching a peak of $747,000 in April 2007, the median price of an existing single-family home fell to $597,000 in February 2008. This is a decline of 22 percent over a period of 22 months or approximately 1 percent per month. The current median house price is about the same as in February 2004.

In their spring of 2008 economic forecast, the Mihaylo College of Business and Economics at California State University, Fullerton (CSUF) predicts that, although half of the anticipated adjustment has taken place in housing prices and related industries, Orange County will experience further downward adjustment in housing prices and related industries for the remainder of the year and possibly into early 2009. Although the pace of job losses so far is below that of the first three-month losses of the 1991-92 and 2001 recessions, further weakness in economic activity and labor market are anticipated through the rest of this year. CSUF expects non-farm payroll in the county to decline by approximately 1 percent for all of 2008 but show slow positive growth next year. Although the continuing economic slowdown is technically not a recession yet, it will definitely feel like one before it is over.

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