



**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Financial Statements and Supplemental Schedules  
and Required Supplementary Information

June 30, 2008 and 2007

(With Independent Auditors' Report Thereon)

# MASSACHUSETTS WATER RESOURCES AUTHORITY

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## **Independent Auditors' Report**

The Board of Directors  
Massachusetts Water Resources Authority:

We have audited the accompanying balance sheets of the Massachusetts Water Resources Authority (the Authority) as of June 30, 2008 and 2007, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the unfunded actuarial accrued liability reported in footnote 11(e). That information was audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included in the unfunded actuarial accrued liability in footnote 11(e), is based on the report of other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority at June 30, 2008 and 2007, and the changes in net assets and cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

As described in note 12, the Authority, in fiscal 2008, implemented Governmental Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 22, 2008, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.



The Management's Discussion and Analysis on pages 3 through 11 and the schedules of funding progress on page 49 are not required parts of the financial statements but are supplementary information required by U.S. generally accepted accounting principles. We and the other auditors have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The supplemental schedules listed in the accompanying table of contents are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied by us in the audits of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

KPMG LLP

October 22, 2008

## MASSACHUSETTS WATER RESOURCES AUTHORITY

### Required Supplementary Information Management's Discussion and Analysis

June 30, 2008 and 2007

(Unaudited)

This section of the Authority's annual financial report presents our discussion and analysis of the Authority's financial performance during the fiscal years ended June 30, 2008 and 2007. Please read it in conjunction with the Authority's financial statements, which immediately follow this section.

#### **Financial Highlights – Fiscal 2008**

The fiscal 2008 customer service revenues were approximately \$534.8 million. Of this amount, rate revenues represent approximately 97%, or \$517.8 million, and were \$22 million higher than fiscal 2007. This was due to an increase in assessments.

Total operating expenses, excluding depreciation, were approximately \$251 million in fiscal 2008. The 10.6% increase in total operating expenses over fiscal 2007 is the result of increased personnel costs, including the recognition of additional post-employment benefits expense of \$13.4 million relating to the implementation of GASB Statement No. 45.

Net nonoperating expenses increased \$23.3 million, or 11.6%, primarily due to a \$20 million increase in interest expense due to the variable rate market conditions (see discussion below).

Total assets at June 30, 2008 were approximately \$8.1 billion, a \$124.2 million, or 1.6%, increase over total assets at June 30, 2007. This increase was primarily reflected as an increase in other assets and deferred charges.

During fiscal 2008, the Authority issued 2008 Series A through F bonds in the aggregate amount of \$1.2 billion to defease \$1.2 billion of bonds outstanding.

Total capital assets (net of depreciation) were approximately \$6.4 billion at June 30, 2008, a \$7.2 million, or 0.1%, increase over June 30, 2007. The increase was due to other asset additions, primarily in the combined sewer overflow (CSO) program.

#### **Variable Rate Market Conditions**

At the beginning of fiscal 2008 the Authority's subordinated general revenue bonds were comprised of a combination of variable rate demand bonds (VRDBs) and auction rate securities (ARS). All of the Authority's VRDBs were issued with a credit enhancement of both bond insurance and a liquidity facility or solely enhanced with a letter of credit. The Authority's ARS bonds were issued with only bond insurance.

The credit ratings downgrades of municipal bond insurers (mainly FGIC and Ambac) created a significant disruption in the municipal bond market. The decreased ratings caused money market funds and other investors to not purchase bonds insured by FGIC or Ambac, resulting in higher interest rate costs on the bonds they insure. As a result, the Authority saw its insured variable rate bonds trading at much higher interest rate costs than those backed solely by a letter of credit agreement.

In May, the Authority took steps to alleviate the increasing interest rate costs of its variable rate debt by refunding all of its VRDBs and ARS bonds, insured by FGIC and Ambac, totaling \$1.2 billion.

## MASSACHUSETTS WATER RESOURCES AUTHORITY

### Required Supplementary Information Management's Discussion and Analysis

June 30, 2008 and 2007

(Unaudited)

#### **Other Post-Employment Benefits (OPEB)**

In fiscal 2008 the Authority budgeted \$7.1 million to prefund its other post-employment benefits (OPEB) in accordance with GASB 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This amount represented the Authority's annual required contribution (ARC) on a prefunding basis as determined by an actuarial valuation performed as of January 1, 2006. This initial ARC of \$8.8 million was reduced by the Authority's current pay-as-you-go costs (\$1.7 million) to arrive at the budgeted amount.

A working group was formed to determine whether it would be advisable to establish a GASB 45-compliant trust to hold and invest annual contributions toward the goal of a fully funded OPEB obligation. This working group concluded that, although the financial and accounting benefits of a GASB 45-compliant trust could not be disputed, it did not feel comfortable with establishing a truly irrevocable trust due to the complexities of disbanding such a trust if, in the future, it is deemed unnecessary and any related tax consequences.

The Authority created a separate reserve fund into which the fiscal 2008 OPEB funding, \$7.1 million, was deposited. This approach strikes a balance between recognition of the need to take an initial step toward funding its long-term OPEB liability, while retaining flexibility until additional guidance is available to make an informed decision as to the best investment structure and accounting treatment of these funds. The Authority's fiscal 2008 financial statements fully comply with GASB 45 requirements by disclosing the nonprefunding actuarially determined ARC of \$15.1 million as an expense and the net OPEB obligation of \$13.4 million as a liability.

In July 2008, the Authority decided to redirect the OPEB reserve funds and funds budgeted in future years for OPEB to the pension fund. This will allow the Authority to take advantage of the higher yields that the pension fund earns and will shorten the time to a fully funded pension plan by 12 years. When the pension plan is fully funded the Authority will have the ability to aggressively pay down the OPEB liability in the future when a long-term OPEB strategy will be developed.

#### **Financial Highlights – Fiscal 2007**

The fiscal 2007 customer service revenues were approximately \$506 million. Of this amount, rate revenues represent approximately 98%, or \$495 million, and were \$23 million higher than fiscal 2006. This was due to an increase in assessments.

Total operating expenses, excluding depreciation, were approximately \$227 million in fiscal 2007. The 1.3% increase in total operating expenses over fiscal 2006 is the result of increased maintenance expenses and increased personnel costs.

Net nonoperating expenses decreased \$8.5 million, or 4%, primarily due to an increase in interest income and debt service grants.

Total assets at June 30, 2007 were approximately \$7.9 billion, a \$48 million, or 0.6%, increase over total assets at June 30, 2006. This increase was primarily reflected as an increase in other assets and deferred charges.

## MASSACHUSETTS WATER RESOURCES AUTHORITY

### Required Supplementary Information Management's Discussion and Analysis

June 30, 2008 and 2007

(Unaudited)

During fiscal 2007, the Authority issued 2007 Series A and B bonds in the aggregate amount of \$848 million to defease \$675 million of bonds and refinance \$179 million of commercial paper notes outstanding.

Total capital assets (net of depreciation) were approximately \$6.4 billion at June 30, 2007, a \$38 million, or 0.6%, decrease over June 30, 2006. The decrease was due to the rate of depreciation exceeding capital asset additions.

#### **Overview of the Financial Statements**

The financial section of this annual report consists of three parts: management's discussion and analysis (this section), the financial statements and related notes to the financial statements, required supplementary information, and other supplementary information.

The financial statements provide both long-term and short-term information about the Authority's overall financial status. The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of other supplementary information that further explains and supports the information in the financial statements.

#### **Financial Analysis of the Authority**

##### *Net Assets*

The Authority's total net assets at June 30, 2008 were approximately \$2.1 billion, a \$44 million decrease from June 30, 2007. Total assets increased \$124.2 million, or 1.6%, to \$8.1 billion, and total liabilities increased 2.9% to \$6 billion.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Required Supplementary Information  
Management's Discussion and Analysis

June 30, 2008 and 2007

(Unaudited)

The Authority's total net assets at June 30, 2007 were approximately \$2.1 billion, a \$44 million decrease from June 30, 2006. Total assets increased \$48 million, or 0.6%, to \$7.9 billion, and total liabilities increased 2.9% to \$5.8 billion.

**Net Assets**

(Dollars in thousands)

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>Percentage change 2008-2007</u>	<u>Percentage change 2007-2006</u>
Current assets	\$ 114,348	107,291	93,866	6.6%	14.3%
Restricted assets	690,382	669,278	681,400	3.2	(1.8)
Capital assets	6,413,403	6,406,195	6,444,534	0.1	(0.6)
Other assets	854,070	765,231	679,748	11.6	12.6
<b>Total assets</b>	<b>8,072,203</b>	<b>7,947,995</b>	<b>7,899,548</b>	<b>1.6</b>	<b>0.6</b>
Current liabilities	323,667	146,318	303,148	121.2	(51.7)
Payable from restricted assets	219,067	203,323	90,235	7.7	125.3
Long-term debt	5,317,572	5,370,663	5,144,294	(1.0)	4.4
Long-term lease	34,733	35,210	35,651	(1.4)	(1.2)
Other liabilities	111,208	82,364	171,795	35.0	(52.1)
<b>Total liabilities</b>	<b>6,006,247</b>	<b>5,837,878</b>	<b>5,745,123</b>	<b>2.9</b>	<b>1.6</b>
Net assets:					
Invested in capital assets – net of related debt	1,289,563	1,441,950	1,554,532	(10.6)	(7.2)
Restricted	240,804	189,396	180,695	27.1	4.8
Unrestricted	535,589	478,771	419,198	11.9	14.2
<b>Total net assets</b>	<b>\$ 2,065,956</b>	<b>2,110,117</b>	<b>2,154,425</b>	<b>(2.1)%</b>	<b>(2.1)%</b>

**Changes in Net Assets**

The decrease in net assets at June 30, 2008 was \$44 million, or 2.1%, as compared with June 30, 2007. The Authority's total operating revenues increased by 5.9% to \$540 million and total operating expenses increased 10.6% to \$251 million.



## MASSACHUSETTS WATER RESOURCES AUTHORITY

### Required Supplementary Information Management's Discussion and Analysis

June 30, 2008 and 2007

(Unaudited)

The decrease in net assets at June 30, 2007 was \$44 million, or 2.1%, as compared with June 30, 2006. The Authority's total operating revenues increased by 4% to \$510 million and total operating expenses increased 1.3% to \$227 million.

#### Changes in Net Assets

(Dollars in thousands)

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>Percentage change 2008-2007</u>	<u>Percentage change 2007-2006</u>
Operating revenues:					
Customer service revenues	\$ 534,809	506,354	484,529	5.6%	4.5%
Other revenues	5,600	4,122	6,455	35.9	(36.1)
Total operating revenues	<u>540,409</u>	<u>510,476</u>	<u>490,984</u>	<u>5.9</u>	<u>4.0</u>
Operating expenses:					
Operations	93,733	87,590	93,517	7.0	(6.3)
Maintenance	26,409	25,915	19,485	1.9	33.0
Payments in lieu of taxes	6,226	5,969	5,920	4.3	0.8
Engineering, general, and administrative	124,687	107,493	105,034	16.0	2.3
Total operating expenses	<u>251,055</u>	<u>226,967</u>	<u>223,956</u>	<u>10.6</u>	<u>1.3</u>
Depreciation and amortization	<u>180,173</u>	<u>180,179</u>	<u>180,217</u>	—	—
Operating income	109,181	103,330	86,811	5.7	19.0
Nonoperating items:					
Regulatory accounting provisions	64,912	47,699	72,254	36.1	(34.0)
Net nonoperating expenses	(225,106)	(201,792)	(210,301)	11.6	(4.0)
Capital grants and contributions	6,852	6,455	5,886	6.2	9.7
Total nonoperating items	<u>(153,342)</u>	<u>(147,638)</u>	<u>(132,161)</u>	<u>3.9</u>	<u>11.7</u>
Change in net assets	(44,161)	(44,308)	(45,350)	(0.3)	(2.3)
Total net assets – beginning of year	<u>2,110,117</u>	<u>2,154,425</u>	<u>2,199,775</u>	<u>(2.1)</u>	<u>(2.1)</u>
Total net assets – end of year	<u>\$ 2,065,956</u>	<u>2,110,117</u>	<u>2,154,425</u>	<u>(2.1)%</u>	<u>(2.1)%</u>

During fiscal 2008, the increases in customer service revenues were primarily due to the 4.5% increase in the rate revenue requirement (\$22 million).

During fiscal 2007, the increases in customer service revenues were primarily due to the 4.9% increase in the rate revenue requirement (\$23 million).

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Required Supplementary Information  
Management's Discussion and Analysis

June 30, 2008 and 2007

(Unaudited)

Total operating costs, before depreciation and amortization, in fiscal 2008 were \$251 million; a \$24 million or 10.6% increase over fiscal 2007. This increase is primarily due to increases in OPEB expenses (\$13.4 million) and total personnel costs (\$3.6 million). OPEB expenses increased with the implementation of GASB 45 which requires the eventual recognition of the unfunded actuarially required contribution. Total personnel costs increased due to union contract increases for salaries and wages and increased health and dental insurance costs.

Total operating costs, before depreciation and amortization, in fiscal 2007 were \$227 million; a \$3 million or 1.3% increase over fiscal 2006. This increase is primarily due to increases in maintenance expenses (\$6.4 million) and total personnel costs (\$1.4 million). Maintenance expenses increased primarily at Deer Island where, as the facility ages, increased maintenance is required to run the plant optimally. Total personnel costs increased due to union contract increases for salaries and wages and increased health insurance costs. These increases were offset by a decrease in utility expenses of \$4.4 million, primarily due to decreased usage and prices of electricity and diesel fuel.

In fiscal 2008, net nonoperating expenses increased \$23.3 million, or 11.6%, primarily due to an increase in interest expense due to the variable rate market conditions during fiscal 2008.

In fiscal 2007, net nonoperating expenses decreased \$8.5 million, or 4%, primarily due to an increase in interest income and debt service grants.

**Operating Costs by Functionality**

(Dollars in thousands)

	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>Percentage change 2008-2007</b>	<b>Percentage change 2007-2006</b>
Wastewater treatment and transport	\$ 97,310	94,921	91,188	2.5%	4.1%
Water treatment and transport	29,153	27,607	24,950	5.6	10.6
Water and wastewater quality	8,584	8,361	8,917	2.7	(6.2)
Metering and monitoring	4,612	4,372	4,405	5.5	(0.7)
Facilities planning, design, and construction	10,495	10,027	9,733	4.7	3.0
Management Information Systems	8,941	8,727	7,970	2.5	9.5
Administration and support	43,324	39,897	42,504	8.6	(6.1)
<b>Total direct operating costs</b>	<b>202,419</b>	<b>193,912</b>	<b>189,667</b>	<b>4.4</b>	<b>2.2</b>
Indirect operating costs	48,636	33,055	34,289	47.1	(3.6)
<b>Total operating costs</b>	<b>\$ 251,055</b>	<b>226,967</b>	<b>223,956</b>	<b>10.6%</b>	<b>1.3%</b>

Across all functionalities the greatest increase in expense was due to increased wages and salaries due to union-negotiated contractual increases. Additional increases in administration and support are due to increases in fringe benefits as the result of increased health and dental insurance costs. Water treatment and transport experienced increases in chemical costs, particularly at the John J. Carroll Water Treatment Plant.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Required Supplementary Information  
Management's Discussion and Analysis

June 30, 2008 and 2007

(Unaudited)

**Capital Assets and Debt Administration**

***Capital Assets***

As of June 30, 2008 and 2007, the Authority had \$6.4 billion of capital assets (net of depreciation). This includes land, construction in progress, plant and equipment for the water and sewer systems, furniture and fixtures, leasehold improvements, and motor vehicles and equipment. The Authority's net capital assets increased approximately \$7.2 million, or 0.1%, during fiscal 2008, primarily due to other asset additions, primarily combined sewer overflow (CSO) projects.

**Capital Assets**

(Net of depreciation, dollars in thousands)

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<b>Percentage change 2008-2007</b>	<b>Percentage change 2007-2006</b>
Land	\$ 6,692	6,692	11,036	—%	(39.4)%
Construction in progress	285,941	273,516	245,542	4.5	11.4
Plant and equipment, water, and sewer systems	6,119,821	6,122,818	6,182,573	—	(1.0)
Furniture and fixtures	21	2,210	4,395	(99.0)	(49.7)
Leasehold improvements	394	406	418	(3.0)	(2.9)
Motor vehicles and equipment	534	553	570	(3.4)	(3.0)
	<u>\$ 6,413,403</u>	<u>6,406,195</u>	<u>6,444,534</u>	<u>0.1%</u>	<u>(0.6)%</u>

Increases in construction in progress are primarily due to increased spending for the North Dorchester Bay tunnel project, Blue Hills covered storage, Morrissey Boulevard drain, rehab of other pump stations and Braintree-Weymouth relief facilities.

***Debt Administration***

The Authority's bond sales must be approved by its board of directors (the Board) and must comply with rules and regulations of the United States Treasury Department. Neither the Commonwealth of Massachusetts (the Commonwealth) nor any political subdivision thereof shall be obligated to pay the principal of, or premium or interest on, any debt outstanding and neither the faith and credit nor the taxing power of the Commonwealth or any political subdivision thereof is pledged to such payment.

***Bond Resolutions***

Pursuant to its general bond resolution, the Authority must comply with a rate covenant that requires it to set rates to maintain revenues sufficient to pay: current expenses; debt service on indebtedness; required deposits to reserves; costs of maintenance, replacement, and/or improvements to the wastewater and water systems that are considered current expenses and any additional amounts the Authority may be required to pay by any law or contract.

## MASSACHUSETTS WATER RESOURCES AUTHORITY

### Required Supplementary Information Management's Discussion and Analysis

June 30, 2008 and 2007

(Unaudited)

In addition to the rate covenant, the Authority is required to meet two covenants with respect to debt service coverage. The primary debt service coverage requires that the Authority fix and adjust rates and charges to provide revenues available for bond debt service in an amount equal to 1.2 times that is required for debt service on all outstanding bonds, not including subordinated bonds. The subordinated debt service coverage requires that the Authority fix and adjust rates and charges to provide revenues available for bond debt service in an amount equal to 1.1 times that is required for debt service on all outstanding bonds, including subordinated bonds.

#### ***Credit Rating***

Of the \$5.5 billion of revenue bonds the Authority currently has outstanding, \$3.1 billion is credit enhanced by a combination of bond insurance, liquidity, or letters of credit. The Authority's enhanced revenue bonds are rated "AAA" by FITCHRATINGS, "Aaa" by Moody's Investors Service, and "AAA" by Standard and Poor's. The Authority's unenhanced \$1.4 billion long-term, senior debt is rated "AA" by FITCHRATINGS, "Aa2" by Moody's Investors Service, and "AA" by Standard and Poor's. The subordinated debt of \$1 billion is not rated as the Authority's debt.

#### ***Economic Factors and Next Year's Budget***

In June 2008, the Board approved the fiscal 2009 Current Expense Budget (CEB), which totals \$590.5 million in expenses before debt service offsets of \$11.3 million, for a net expense total of \$579.3 million. The \$11.3 million in debt service offsets is for debt service assistance.

The \$590.5 million expense total (before debt service offsets) is comprised of \$328.8 million (56%) in capital financing costs and \$261.7 million (44%) in operating expenses, of which \$215.9 million (82%) is for direct expenses and \$45.8 million (18%) is for indirect expenses. The total represents an increase of \$26.4 million from fiscal 2008 spending, which is comprised of \$16.4 million in higher operating costs and \$10 million in higher debt service costs.

The fiscal 2009 rate revenue requirement approved by the Board is \$540.8 million; an increase of 4.5% compared with the fiscal 2008 budget.

Fiscal 2009 budgeted nonrate revenue totals \$38.5 million, a decrease of \$17.6 million from actual fiscal 2008 nonrate revenue. The nonrate revenue budget is comprised of \$20.4 million in investment income, \$17.6 million in other user charges and other revenue and \$0.5 million in entrance fees.

## MASSACHUSETTS WATER RESOURCES AUTHORITY

Required Supplementary Information  
Management's Discussion and Analysis

June 30, 2008 and 2007

(Unaudited)

### ***CIP 10 Year Plan***

The Authority's planned spending for capital improvements in future years reflects the continuation and completion of projects now underway. These include:

- Completion of covered storage facilities, including Blue Hills Covered Storage, to provide safe, reliable storage for water treated at JCWTP and transported through the MetroWest Tunnel and Hultman Aqueduct.
- Rehabilitation of the Wachusett and Hultman Aqueducts as well as rehabilitation of top shaft structures on the Quabbin Tunnel, Dorchester Tunnel, City Tunnel, Southborough Tunnel, and City Tunnel Extension.
- Completion of the long-term CSO control plan, resulting in closing of 34 of 84 CSO outfalls and the reduction of CSO discharges to Boston Harbor and the Mystic, Charles, and Neponset River systems by 85% from 1987, when MWRA accepted responsibility for CSO control, with 94% of remaining discharges receiving treatment.
- Construction of new interceptor facilities to serve Braintree, Hingham, Holbrook, Randolph, Weymouth, and sections of Quincy, and to reduce sewage overflows into the Weymouth Fore River.
- Installation of new sewers to reduce overflows to adjacent residential areas and water bodies in West Roxbury and Newton.
- Continued rehabilitation of the water distribution system at a rate of six to seven miles per year (2% to 2.5% of the total 275 miles of Authority pipeline).
- Improvement and replacement of equipment on Deer Island to ensure that the plant continues to operate efficiently and effectively.
- Security improvements to protect the Authority's facilities.

### **Contacting the Authority's Financial Management**

This report is designed to provide our bondholders, member communities and other interested parties with a general overview of the Authority's finances and to demonstrate the Authority's accountability for the revenue it receives. If you have questions about this report or need additional information, contact the Massachusetts Water Resources Authority, Finance Division, 100 First Avenue, Boston, MA 02129.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Balance Sheets

June 30, 2008 and 2007

(Dollars in thousands)

Assets	2008	2007
Unrestricted current assets:		
Cash and cash equivalents (note 4)	\$ 43,408	40,828
Investments (note 4)	47,790	42,444
Intergovernmental loans (note 7)	22,660	22,097
Accounts receivable	490	1,922
Total unrestricted current assets	114,348	107,291
Restricted assets:		
Investments (note 4)	687,161	664,196
Interest receivable	3,221	5,082
Total restricted assets	690,382	669,278
Capital assets – not being depreciated (note 8)	292,633	280,208
Capital assets – being depreciated – net (note 8)	6,120,770	6,125,987
Deferred charges (notes 3 and 9)	554,589	475,057
Other assets, net (notes 7 and 9 )	299,481	290,174
Total	\$ 8,072,203	7,947,995
<b>Liabilities and Net Assets</b>		
Current liabilities:		
Accounts payable and accrued expenses (note 14)	\$ 55,443	56,466
Commercial paper notes (note 6)	191,000	39,000
Current portion of long-term debt (note 6)	77,224	50,852
Total current liabilities	323,667	146,318
Payable from restricted assets:		
Accounts payable for construction	36,637	21,813
Accrued interest on bonds payable	77,789	77,341
Reserves (note 5)	104,641	104,169
Total payable from restricted assets	219,067	203,323
Retainage on construction in progress	13,122	11,852
Long-term debt – less current portion (note 6)	5,317,572	5,370,663
Long-term capital lease (note 10)	34,733	35,210
Other long-term liabilities (note 12)	13,426	—
Deferred credits (note 3)	84,660	70,512
Total liabilities	6,006,247	5,837,878
Net assets:		
Invested in capital assets, net of related debt	1,289,563	1,441,950
Restricted	240,804	189,396
Unrestricted	535,589	478,771
Total net assets	2,065,956	2,110,117
Commitments and contingencies (notes 10, 11, 12, 13, and 14)		
Total	\$ 8,072,203	7,947,995

See accompanying notes to financial statements.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Statements of Revenues, Expenses, and Changes in Net Assets

Years ended June 30, 2008 and 2007

(Dollars in thousands)

	<u>2008</u>	<u>2007</u>
Operating revenues (note 2):		
Customer services	\$ 534,809	506,354
Other	5,600	4,122
Total operating revenues	<u>540,409</u>	<u>510,476</u>
Operating expenses:		
Operations	93,733	87,590
Maintenance	26,409	25,915
Payments in lieu of taxes	6,226	5,969
Engineering, general, and administrative	124,687	107,493
Total operating expenses	<u>251,055</u>	<u>226,967</u>
Income from operations before depreciation	289,354	283,509
Depreciation and amortization	<u>180,173</u>	<u>180,179</u>
Operating income	<u>109,181</u>	<u>103,330</u>
Regulatory accounting provisions:		
Change in reserves (note 5)	(472)	(3,119)
Change in deferrals, net (note 3)	65,384	50,818
Total regulatory accounting provisions	<u>64,912</u>	<u>47,699</u>
Nonoperating revenues (expenses):		
Debt service grants	16,980	18,937
Investment income	41,199	42,966
Interest expense	(283,285)	(263,695)
Total nonoperating expenses	<u>(225,106)</u>	<u>(201,792)</u>
Net loss before capital contributions	(51,013)	(50,763)
Capital grants and contributions	<u>6,852</u>	<u>6,455</u>
Decrease in net assets	(44,161)	(44,308)
Total net assets, beginning of year	<u>2,110,117</u>	<u>2,154,425</u>
Total net assets, end of year	<u>\$ 2,065,956</u>	<u>2,110,117</u>

See accompanying notes to financial statements.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Statements of Cash Flows

Years ended June 30, 2008 and 2007

(Dollars in thousands)

	<u>2008</u>	<u>2007</u>
Cash flows from operating activities:		
Cash received from customers	\$ 534,766	508,450
Cash paid to suppliers for goods and services	(109,114)	(111,377)
Cash paid to employees for services	(124,477)	(107,458)
Cash paid in lieu of taxes	(6,226)	(5,975)
Other operating receipts	5,600	4,122
Net cash provided by operating activities	<u>300,549</u>	<u>287,762</u>
Cash flows from capital and related financing activities:		
Proceeds from sale of revenue bonds, loans, and notes	272,355	341,909
Capital grants for construction	6,852	7,808
Debt service grant	16,980	18,937
Capital lease principal payments	(477)	(441)
Capital lease interest payments	(2,740)	(2,776)
Repayment of debt	(172,630)	(295,177)
Interest paid on debt	(252,272)	(237,364)
Plant expenditures	(180,785)	(165,139)
Net cash used for capital and related financing activities	<u>(312,717)</u>	<u>(332,243)</u>
Cash flows from investing activities:		
Purchases of short-term investments	(86,801)	(3,000)
Sales and maturities of short-term investments	141,003	48,976
Increase in restricted cash and investments – net	(75,874)	(33,381)
Interest received	36,420	40,940
Net cash provided by investing activities	<u>14,748</u>	<u>53,535</u>
Net increase in cash and cash equivalents	2,580	9,054
Cash and cash equivalents, beginning of year	<u>40,828</u>	<u>31,774</u>
Cash and cash equivalents, end of year	\$ <u><u>43,408</u></u>	\$ <u><u>40,828</u></u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 109,181	103,330
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	180,173	180,179
Decrease in other accounts	88	1,042
Increase in accounts payable	11,107	3,211
Net cash provided by operating activities	\$ <u><u>300,549</u></u>	\$ <u><u>287,762</u></u>

Noncash capital and related financing activities:

In May 2008, general revenue refunding bonds in the aggregate principal amount of \$1,162,090 were issued to defease \$1,197,745 of bonds outstanding.

In February 2007, general revenue refunding bonds in the aggregate principal amount of \$647,950 were issued to defease \$674,570 of bonds outstanding.

See accompanying notes to financial statements.



# MASSACHUSETTS WATER RESOURCES AUTHORITY

## Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

### (1) Organization

The Massachusetts Water Resources Authority (the Authority) was established in January 1985 pursuant to Chapter 372 (the Enabling Act) of the Act of 1984 of the Commonwealth of Massachusetts (the Commonwealth). The Authority, a successor agency to certain functions of the Metropolitan District Commission (the MDC) (which became part of the Department of Conservation and Recreation (the DCR) in July 2003), is a public instrumentality and, effective July 1, 1985, provides water supply services and sewage collection, treatment, and disposal services to areas of the Commonwealth.

The Authority is governed by an 11-member board of directors (the Board) chaired by the Secretary of Environmental Affairs for the Commonwealth. The Secretary and four other members are appointed by the Governor, one upon recommendation of the Mayor of Quincy and one upon recommendation of the Selectmen of Winthrop. Three members of the Board are appointed by the Mayor of Boston and three are appointed by the Authority's Advisory Board.

### (2) Summary of Significant Accounting Policies

The accounting policies of the Authority conform to U.S. generally accepted accounting principles as applicable to government enterprises. The following is a summary of the Authority's significant accounting policies:

#### (a) Basis of Presentation

The Authority is required by the Enabling Act to establish user rates for its water and sewer services which provide sufficient funds to recover the costs of operations (excluding depreciation), debt service, maintenance, replacements, improvements to its facilities, and appropriate reserves. The Authority's financial statements are reported on the accrual basis of accounting and the economic measurement focus as specified by the Governmental Accounting Standards Board's (GASB) requirements for an enterprise fund.

The Authority distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing water and sewer services to its member communities. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. All operating revenues are pledged for repayment of outstanding debt service.

Under GASB Statement No. 20, *Accounting and Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the Authority has adopted the option to apply all Financial Accounting Standards Board (FASB) Statements and Interpretations issued before November 30, 1989, except for those that conflict with or contradict GASB pronouncements.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

In addition, the Authority has adopted the provisions of FASB Statement No. 71, *Accounting for the Effects of Certain Types of Regulation*, to provide a better matching of revenues and expenses. The effect of this policy has been to defer certain costs, which will be recovered through future revenues in accordance with the Authority's rate model, and to record deferred credits for revenue collected through current rates for costs expected to be incurred in the future. The effects of the Authority's accounting policies under Statement No. 71 are discussed further in notes 3 and 9.

**(b) Capital Assets**

On July 1, 1985, ownership of the MDC's sewer and waterworks personal property was transferred to the Authority. Pursuant to the Enabling Act, ownership of the real property of the MDC sewer and waterworks systems was not transferred from the Commonwealth to the Authority; however, the Authority has the right to use, improve, maintain, and manage that property. In addition, ownership of the real and personal property of the watershed system remains with the Commonwealth; however, the Authority has the right to utilize the water therefrom for water supply purposes.

The personal property, together with the rights to the real property and watershed system, was recorded at its estimated fair value of \$2,331,465 (including certain construction projects which were in progress as of July 1, 1985), based upon an appraisal performed by valuation specialists. Property, plant, and equipment acquired or constructed since July 1, 1985, is stated at historical cost, and includes the expenditure of capital grants in aid of construction.

Betterments and major renewals are capitalized and included in capital asset accounts, while expenditures for maintenance and repairs are charged to expense when incurred. The cost of depreciable assets and related accumulated depreciation is eliminated from the accounts when such items are disposed of or otherwise retired.

**(c) Interest Cost and Principal Payments on Construction**

During fiscal 2008 and 2007, none of the Authority's interest expense was capitalized to construction in progress in accordance with its current policy of recovering such costs through rates as incurred. Rates collected for principal payments on debt related to assets under construction are deferred until the related asset is completed and depreciation commences.

**(d) Depreciation**

The Authority provides for depreciation by use of the straight-line method. Depreciation is intended to distribute the cost of depreciable properties, including those financed by capital grants in aid of construction, over the following estimated average useful lives:

	<u>Years</u>
Plant and equipment, water and sewerage systems	5 – 100
Motor vehicles and equipment	5
Furniture and fixtures	7
Leasehold improvements	3 – 5

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

**(e) Revenue Recognition**

The Authority recognizes revenue as amounts become collectible from its customers for water and sewer services provided. The majority of the Authority's billings to cities and towns are subject to, in the event of nonpayment, the local aid intercept allowed by the Enabling Act.

**(f) Cash and Cash Equivalents**

The Authority's policy is to treat unrestricted investments with a maturity date of three months or less when purchased as cash equivalents for purposes of the statements of cash flows. Restricted cash and cash equivalents are combined with investments on the balance sheets, and shown separately on the statements of cash flows as an investing activity.

**(g) Payments in Lieu of Taxes**

The Enabling Act authorizes and directs the Authority to pay to the DCR (formerly the MDC) Division of Watershed Management, who in turn remits payment to each city or town in which land of the Quabbin watershed and Ware River watershed is located. Each such payment is equal to the amount which the respective city or town would receive in property taxes, based upon the fair value of such land if such land were not tax exempt.

**(h) Investments**

Most investments are recorded at fair value. Fair value is determined based on quoted market price. Guaranteed investment contracts are recorded at cost. The Authority recorded unrealized gains of \$6,839 and \$382 in fiscal 2008 and fiscal 2007, respectively, as part of investment income.

**(i) Use of Estimates**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

**(j) Compensated Absences**

Employees of the Authority may accumulate unused sick time of which 30% will be paid in cash upon retirement from the Authority. The liability for vacation leave is based on the amount earned but not used; for sick leave, it is based on a percentage of the amount accumulated at the statement of net assets dates. The liability for both amounts is calculated based on the pay or salary rates in effect at the statements of net assets dates.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

**(3) Deferred Charges and Credits**

In accordance with FASB No. 71, deferred charges and credits result primarily from differences between depreciation on property, plant, and equipment not financed by grants or capital contributions, which is recovered through rates as principal payments on debt service, and from amounts determined by the Board to be utilized in a subsequent year to reduce customer billings (rate stabilization).

A summary of the activity of FASB No. 71 charges (credits) for fiscal 2008 and 2007 is as follows:

	<u>Sewer</u>	<u>Water</u>	<u>Total</u>
Balance – June 30, 2006 – net	\$ 288,856	64,871	353,727
Difference between depreciation of capital assets not financed by grants or capital contributions, and debt service in excess of interest expense	50,321	9,605	59,926
Rate stabilization – current year recovery	6,203	(8,395)	(2,192)
Other – net	<u>(5,633)</u>	<u>(1,283)</u>	<u>(6,916)</u>
Balance – June 30, 2007 – net	339,747	64,798	404,545
Difference between depreciation of capital assets not financed by grants or capital contributions, and debt service in excess of interest expense	71,581	10,507	82,088
Bond redemption, net	2,556	—	2,556
Other – net	<u>(8,638)</u>	<u>(10,622)</u>	<u>(19,260)</u>
Balance – June 30, 2008 – net	\$ <u>405,246</u>	<u>64,683</u>	<u>469,929</u>

The net balance at June 30, 2008 and 2007, is presented on the balance sheets as follows:

	<u>2008</u>	<u>2007</u>	<u>Current year change</u>
Deferred charges	\$ 554,589	475,057	79,532
Deferred credits	<u>(84,660)</u>	<u>(70,512)</u>	<u>(14,148)</u>
Net change in deferrals	\$ <u>469,929</u>	<u>404,545</u>	<u>65,384</u>

The balance in the rate stabilization reserve, which is included in deferred credits, was \$43,737 at June 30, 2008 and 2007.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

**(4) Deposits and Investments**

The following represents essential risk information about the Authority's deposits and investments.

**(a) Custodial Credit Risk – Deposits**

The custodial credit risk for deposits and certificates of deposit is the risk that, in the event of a bank failure, the Authority's deposits may not be recovered. The deposits in the bank in excess of the insured amount are uninsured and uncollateralized.

The bank deposits at June 30, 2008 and 2007 were \$46,854 and \$43,041, respectively. Of these amounts, \$46,754 and \$42,941 were exposed to custodial credit risks as uninsured and uncollateralized.

**(b) Investments**

The Authority is authorized by its general bond resolution to invest in obligations of the U.S. Treasury, its agencies and instrumentalities, bonds, or notes of public agencies or municipalities, bank time deposits, guaranteed interest contracts, money market accounts, interest rate swap agreements, and repurchase agreements. All investments are held by a third-party in the Authority's name. These investments are recorded at fair value.

The following guaranteed investment contracts were in force as of June 30, 2008 and 2007, respectively, all of which are fully collateralized and recorded at cost:

<u>Investment agreement provider</u>	<u>Rate</u>	<u>Maturity</u>	<u>2008</u>	<u>2007</u>
AIG financial products	6.05	August 1, 2014	\$ 18,342	18,342
Wachovia Bank	5.17	August 1, 2016	14,456	14,456
Total			\$ 32,798	32,798

In September 2008, AIG was downgraded to an A – rating by Standard & Poor's (S&P). This downgrade resulted from AIG's lack of liquidity and its ability to raise sufficient capital to back its financial obligations. Under its contract with the Authority, AIG is required to maintain an S&P rating of at least AA – or else it will be in default. In the event of a default, the contract provides for the principal and unpaid interest to become due and payable immediately. On September 29, 2008 the Authority received from AIG the \$18,342,000 in principal and \$185,000 in accrued interest which was subsequently invested in the Massachusetts Municipal Depository Trust (MMDT).

**(c) Credit Ratings**

All debt securities purchased, such as FNMA, FHLMC, and FHLB issues have an implied credit rating of AAA or they have been collateralized to AAA. The guaranteed investment contracts themselves are not rated. Further, the certificates of deposits and money market funds are not rated.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

The general bond resolution limits the Authority to investing in securities that are rated in the three highest rating categories as defined by S&P and Moody's.

**(d) Concentration Risk**

The Authority has no investments, at fair value, which exceeds 5% of the Authority's total investments as of June 30, 2008 and 2007.

**(e) Interest Rate Risk**

The following is a listing of the Authority's fixed income investments and related maturity schedule as of June 30, 2008 and 2007:

<b>June 30, 2008</b>					
<b>Investment maturities (in years)</b>					
<b>Investment type</b>	<b>Fair value</b>	<b>&lt;1</b>	<b>1-3</b>	<b>4-8</b>	<b>&gt;9</b>
Certificate of deposit	\$ 3,000	3,000	—	—	—
Money market mutual funds	498,402	498,402	—	—	—
U.S. Treasury notes and bonds	4,130	—	—	4,130	—
U.S. agency obligations	196,621	—	7,304	123,031	66,286
Guaranteed investment contracts	32,798	18,342	—	—	14,456
Total	<u>\$ 734,951</u>	<u>519,744</u>	<u>7,304</u>	<u>127,161</u>	<u>80,742</u>

<b>June 30, 2007</b>					
<b>Investment maturities (in years)</b>					
<b>Investment type</b>	<b>Fair value</b>	<b>&lt;1</b>	<b>1-3</b>	<b>4-8</b>	<b>&gt;9</b>
Certificate of deposit	\$ 3,100	100	3,000	—	—
Money market mutual funds	422,528	422,528	—	—	—
U.S. Treasury notes and bonds	21,540	17,753	—	3,787	—
U.S. agency obligations	226,674	—	7,024	124,617	95,033
Guaranteed investment contracts	32,798	—	—	18,342	14,456
Total	<u>\$ 706,640</u>	<u>440,381</u>	<u>10,024</u>	<u>146,746</u>	<u>109,489</u>

The Authority's bond resolution limits maturities to less than 15 years. The majority of the Authority's investments are long-term investments held in the debt service reserve funds where the intent is to hold until maturity. This reduces the exposure to fair value losses arising from increasing interest rates.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

**(f) Restricted Investments by Fund**

The following summarizes restricted investments as of June 30, 2008 and 2007 by various funds and accounts established by the Authority for debt covenants and other purposes:

	<u>2008</u>	<u>2007</u>
Restricted investments:		
Construction	\$ 105,237	83,892
Debt service reserves	220,868	253,083
Debt service	177,987	148,296
Revenue redemption	30,852	35,191
Revenue	67,452	66,328
Renewal and replacement reserve	33,947	31,429
Insurance	18,997	18,997
OPEB Reserve	7,183	—
Community obligation and revenue enhancement	20,508	20,105
Insurance related escrow deposits	4,130	6,875
Total restricted investments	<u>\$ 687,161</u>	<u>664,196</u>

**(5) Bond Resolution Reserves**

The components of the reserves required by the general and supplemental bond resolutions at June 30, 2008 and 2007 are as follows:

<u>Reserves</u>	<u>Sewer</u>	<u>Water</u>	<u>Total 2008</u>	<u>Total 2007</u>
Renewal and replacement	\$ 17,300	11,701	29,001	29,001
Insurance	9,500	9,500	19,000	19,000
Operating	26,998	9,526	36,524	36,052
Community obligation and revenue enhancement	18,399	1,717	20,116	20,116
Total	<u>\$ 72,197</u>	<u>32,444</u>	<u>104,641</u>	<u>104,169</u>

A renewal and replacement reserve of \$6,000 was established through grant receipts transferred from the Commonwealth in 1985 and is included in restricted net assets at June 30, 2008 and 2007.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

**(6) Notes Payable and Long-Term Debt**

Long-term debt at June 30, 2008 and 2007 consisted of the following:

	<u>2008</u>	<u>2007</u>
General Revenue Bonds:		
1993 Series C, 5 1/4% to 6%, issued December 2, 1993, due 2008 to 2015	\$ 51,285	51,285
1998 Series A, 4 3/4%, issued January 27, 1998, due 2021 to 2032	100,355	100,355
2002 Series B, 5% to 5 1/8%, issued March 15, 2002, due 2021 to 2027	74,415	74,415
2002 Series J, 5% to 5 1/2%, issued December 18, 2002, due 2008 to 2042	553,080	553,080
2003 Series D, 4 5/8% to 5%, issued January 7, 2004, due 2022 to 2028	113,340	113,340
2004 Series A, 4 3/4% to 5 1/8%, issued June 10, 2004, due 2021 to 2029	104,870	104,870
2006 Series A, 4% to 5%, issued March 16, 2006, due 2023 to 2046	200,000	200,000
2007 Series A, 4 3/8% to 5%, issued February 1, 2007 due 2022 to 2046	200,000	200,000
	<u>1,397,345</u>	<u>1,397,345</u>
General Revenue Refunding Bonds:		
1997 Series D, 5% to 6%, issued December 15, 1997, due 2008 to 2020	123,245	128,815
1998 Series B, 4 1/2% to 5 1/2%, issued January 27, 1998, due 2008 to 2022	103,165	103,550
2004 Series B, 5%, issued September 29, 2004, due 2016 to 2020	49,390	49,390
2005 Series A, 3% to 5 1/4%, issued April 14, 2005, due 2008 to 2034	410,675	410,675
2005 Series B, 5%, issued April 14, 2005, due 2031 to 2035	80,290	80,290
2006 Series B, 4% to 5%, issued March 16, 2006, due 2015 to 2040	264,945	264,945
2007 Series B, 5 1/4%, issued February 1, 2007 due 2023 to 2038	647,950	647,950
	<u>1,679,660</u>	<u>1,685,615</u>



**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

	<u>2008</u>	<u>2007</u>
Subordinated debt:		
General Revenue Bonds with the Massachusetts		
Water Pollution Abatement Trust:		
1993 Series A, 5 3/10% to 5 1/2%, issued		
March 18, 1993, due 2008 to 2013	\$ 3,305	4,285
1993 Series D, 5 1/10% to 5 1/4%, issued		
January 6, 1994, due 2008 to 2014	3,235	3,925
1995 Series A, 5% to 5 1/2%, issued		
November 21, 1995, due 2008 to 2015	4,090	4,885
1998 Series C, 4 1/2% to 5 3/8%, issued		
July 9, 1998, due 2008 to 2018	9,135	10,385
1999 Series E Sewer, 4 1/2% to 5 3/8%, issued		
October 6, 1999, due 2008 to 2029	8,758	9,023
1999 Series E Water, 4 1/2% to 5 3/8%, issued		
October 6, 1999, due 2008 to 2019	8,072	8,615
1999 Series F, 5% to 6%, issued		
November 3, 1999, due 2008 to 2029	330,155	340,710
2000 Series E Sewer, 4 6/8% to 5 5/8%, issued		
November 1, 2000, due 2008 to 2030	64,035	65,715
2000 Series E Water, 4 3/4% to 5 5/8%, issued		
November 1, 2000, due 2008 to 2020	9,111	9,665
2001 Series C Water, 5% to 5 1/4%, issued		
July 26, 2001, due 2009 to 2021	3,926	4,162
2001 Series D Sewer, 5% to 5 3/4%, issued		
July 26, 2001, due 2008 to 2029	5,905	6,279
2001 Series D Water, 4 8/10% to 5 3/4%, issued		
July 26, 2001, due 2008 to 2019	1,141	1,218
2002 Series H Sewer, 3 1/2% to 5 1/4%, issued		
October 31, 2002, due 2008 to 2032	81,790	83,875
2002 Series H Water, 3 1/2% to 5 1/4%, issued		
October 31, 2002, due 2008 to 2022	26,650	28,020
2002 Series I Sewer, 4 1/4% to 5 5/8%, issued		
October 31, 2002, due 2008 to 2030	2,334	2,400
2002 Series I Water, 4 1/4% to 5 5/8%, issued		
October 31, 2002, due 2008 to 2020	24	26
2003 Series A Water, 3 2/5% to 5 1/4%, issued		
October 31, 2002, due 2008 to 2022	1,229	1,293
2003 Series B Water, 5% to 5 1/4%, issued		
July 24, 2003, due 2009 to 2021	3,544	3,757
2003 Series C Sewer, 2 3/10% to 5 1/2%, issued		
November 6, 2003, due 2008 to 2033	29,324	30,049
2003 Series C Water, 2 3/10% to 5 1/2%, issued		
November 6, 2003, due 2008 to 2023	18,055	18,969

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

	<u>2008</u>	<u>2007</u>
2004 Series C Sewer, 2 3/10% to 5 1/2%, issued October 26, 2004, due 2008 to 2033	\$ 9,956	10,203
2004 Series C water, 3 2/5% to 5 1/4%, issued October 26, 2004, due 2008 to 2022	1,441	1,528
2004 Series D Sewer, 3% to 5 1/4%, issued November 29, 2004, due 2008 to 2034	59,007	61,027
2004 Series D Water, 3% to 5 1/4%, issued November 29, 2004, due 2008 to 2024	11,897	12,400
2005 Series C Sewer, 2 3/10% to 5 1/2%, issued November 3, 2005, due 2008 to 2034	6,934	7,211
2005 Series C Water, 2 3/10% to 5 1/2%, issued November 3, 2005, due 2008 to 2024	943	990
2005 Series D Sewer, 2% to 2 3/10%, issued November 16, 2005, due 2008 to 2035	63,403	65,214
2005 Series D Water, 0% to 2%, issued November 16, 2005, due 2008 to 2025	13,516	14,231
2005 Series E Sewer, 2%, issued November 16, 2005, due 2008 to 2025	366	387
2005 Series E Water, 2%, issued November 16, 2005, due 2008 to 2025	81	86
2006 Series C Sewer, 3% to 5 1/4%, issued October 26, 2006, due 2008 to 2034	8,410	8,646
2006 Series D Sewer, 2% to 2 3/10%, issued December 14, 2006, due 2008 to 2036	64,799	58,715
2006 Series D Water, 0% to 2%, issued November 16, 2006, due 2008 to 2026	28,509	26,922
2006 Series E Sewer, 2%, issued December 14, 2006, due 2008 to 2026	359	374
2006 Series E Water, 2%, issued December 14, 2006, due 2008 to 2026	161	168
2007 Series C Sewer, 2% to 2 3/10%, issued November 9, 2007, due 2008 to 2035	4,798	—

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

	<u>2008</u>	<u>2007</u>
2007 Series C Water, 2%, issued November 9, 2007, due 2008 to 2025	\$ 2,727	—
2007 Series D Sewer, 2 3/10%, issued November 9, 2007, due 2008 to 2036	22,978	—
2007 Series E Sewer, 2% to 2 2/5%, issued December 18, 2007, due 2008 to 2037	58,853	—
2007 Series E Water, 2% , issued December 18, 2007, due 2008 to 2027	19,373	—
	<u>992,329</u>	<u>905,358</u>
<b>General Revenue Bonds (variable rates):</b>		
1997 Series A, 2.75% to 6.0%, issued June 18, 1997	—	76,600
1997 Series B, 2.94% to 9.0%, issued June 18, 1997	—	76,600
1999 Series A, 2.90% to 7.0%, issued January 14, 1999	—	87,600
1999 Series B, 1.11% to 3.92%, issued January 29, 1999, due 2008 to 2028	86,100	87,600
1999 Series C, 2.12% to 4.68%, issued June 8, 1999	—	67,900
1999 Series D, 3.68% to 5.0%, issued June 8, 1999	—	67,900
2001 Series A, 3.0% to 10.0%, issued September 26, 2001	—	84,900
2001 Series B, 1.52% to 11.0%, issued September 26, 2001	—	85,000
	<u>86,100</u>	<u>634,100</u>
<b>General Revenue Refunding Bonds (variable rates):</b>		
1998 Series D, 3.0% to 9.0%, issued December 22, 1998	—	198,895
2000 Series B, 3.0% to 9.0%, issued March 22, 2000	—	133,300
2000 Series C, 3.0% to 9.0%, issued March 22, 2000	—	133,300
2002 Series C, 0.89% to 4.05%, issued August 15, 2002, due 2020	70,575	76,300

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(Dollars in thousands)

	<u>2008</u>	<u>2007</u>
2002 Series D, 0.85% to 4.05%, issued August 15, 2002, due 2008 to 2017	\$ 76,450	76,450
2002 Series E, 3.25% to 4.68%, issued August 15, 2002	—	83,400
2002 Series F, 3.0% to 4.7%, issued August 15, 2002	—	90,900
2002 Series G, 2.7% to 4.95%, issued August 15, 2002	—	99,250
2008 Series A, 1.42% to 1.7%, issued May 29, 2008, due 2009 to 2037	338,005	—
2008 Series B, 1.25% to 1.7%, issued May 29, 2008, due 2009 to 2031	124,595	—
2008 Series C, 1.46% to 1.75%, issued May 29, 2008, due 2009 to 2027	199,400	—
2008 Series D, 1.46% to 1.75%, issued May 29, 2008, due 2010 to 2011	83,615	—
2008 Series E, 1.55% to 1.7%, issued May 29, 2008, due 2012 to 2037	224,770	—
2008 Series F, 1.4% to 1.6%, issued May 29, 2008, due 2009 to 2029	191,705	—
	<u>1,309,115</u>	<u>891,795</u>
	<u>5,464,549</u>	<u>5,514,213</u>
Less:		
Unamortized bond premiums and discounts	142,819	144,053
Unamortized excess of reacquisition price over net carrying amount of defeased bonds	(212,572)	(236,751)
Current portion of long-term debt	(77,224)	(50,852)
	<u>(146,977)</u>	<u>(143,550)</u>
Long-term debt, net	\$ <u>5,317,572</u>	<u>5,370,663</u>

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Long-term debt at June 30, 2008 and 2007 consisted of the following:

		<b>2007 beginning balance</b>	<b>Additions</b>	<b>Reductions</b>	<b>2008 ending balance</b>	<b>Due within one year</b>
General Revenue Bonds	\$	2,031,445	—	548,000	1,483,445	21,935
General Revenue Refunding Bonds		2,577,410	1,162,090	750,725	2,988,775	18,480
General Revenue Bonds with the Massachusetts Water Pollution Abatement Trust		905,358	119,799	32,828	992,329	36,809
	\$	<u>5,514,213</u>	<u>1,281,889</u>	<u>1,331,553</u>	<u>5,464,549</u>	<u>77,224</u>

  

		<b>2006 beginning balance</b>	<b>Additions</b>	<b>Reductions</b>	<b>2007 ending balance</b>	<b>Due within one year</b>
General Revenue Bonds	\$	2,550,445	200,000	719,000	2,031,445	12,299
General Revenue Refunding Bonds		1,973,215	647,950	43,755	2,577,410	5,725
General Revenue Bonds with the Massachusetts Water Pollution Abatement Trust		842,275	111,596	48,513	905,358	32,828
	\$	<u>5,365,935</u>	<u>959,546</u>	<u>811,268</u>	<u>5,514,213</u>	<u>50,852</u>

The Authority is required to establish water and sewer rates and charges at a level sufficient to provide, among other things, primary and subordinated debt service coverage ratios of 120% and 110%, respectively. For the year ended June 30, 2008, the Authority had primary and subordinated debt service coverage ratios of 232% and 117%, respectively.

The Act of 1984 imposes a limitation of \$600,000 on the total amount of bonds and notes which may be outstanding at any one time. The Authority has requested increases in its debt limit as necessary to allow for issuances of bonds in amounts required to finance the capital program. The state legislature increased the debt limit to \$6,100,000.

On May 29, 2008, the Authority issued General Revenue Refunding Bonds, 2008 Series A, 2008 Series B, 2008 Series C, 2008 Series D, 2008 Series E and 2008 Series F in the principal amounts of \$338,005, \$124,595, \$199,400, \$83,615, \$224,770 and \$191,705, respectively.

The proceeds from the new bonds were used to defease \$1.2 billion of variable rate bonds outstanding. These new bonds are variable rate demand obligations which are reset weekly. The interest rates on the new bonds from issuance until the fiscal year end ranged from 1.25% to 1.75%.

On February 1, 2007, the Authority issued General Revenue Bonds, 2007 Series A and General Revenue Refunding Bonds, 2007 Series B in the principal amounts of \$200,000 and \$647,950, respectively. The proceeds from the Series A bonds were used to retire \$179,000 of Commercial Paper Notes. The interest rate on these bonds is 4-3/8% to 5%.

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The proceeds from the Series B bonds were used to defease \$674,570 of the 1992 Series A, 1993 Series C, 1995 Series B, 1998 Series A, 2000 Series A, 2002 Series B, 2003 Series D, 2004 Series A, 2004 Series B, and 2006 Series B bonds outstanding. The interest rate on these bonds is 5.25%. The cash flow required to make principal and interest payments on the refunding bonds is approximately \$451,925 more than the debt service requirements for the defeased bonds. The economic gain (the difference between the present values of the debt service payments on the old and new debt) obtained from this refunding was \$4,940.

In connection with several of its bond issues, the Authority has entered into various interest rate swap agreements to reduce the impact of changes in interest rates on its variable rate debt. Under these agreements, the Authority pays a fixed interest rate (ranging from 3.9% to 6.9%) and receives interest from the swap counterparties at a variable rate (either Bond Market Association (BMA) rate or 67% LIBOR). The BMA rate is based on the seven-day high-grade market index of tax-exempt variable rate demand obligations.

### Summary of Swap Transactions

#### *Synthetic Fixed Rate Swap Transactions*

Date of execution	Notional amount	Termination date	Associated bonds	Fixed payable swap rate	Variable receivable swap rate	Lump-Sum payment from counterparty	Counterparty credit rating at June 30, 2008	Fair value at June 30, 2008
March 22, 2000	\$ 266,600	August 1, 2030	2008 Series A & E	4.470%	BMA	N/A	Aaa*	\$ (52,879)
August 1, 2030	70,400	August 1, 2037	2008 Series A & E	6.935	BMA	N/A	Aaa*	(2,596)
December 22, 1998	119,335	November 1, 2026	2008 Series C	3.994	BMA	N/A	Aaa	(4,702)
December 22, 1998	79,560	November 1, 2026	2008 Series C	4.032	BMA	N/A	Aaa	(3,382)
August 15, 2002	350,000	August 1, 2015	2002 Series D, 2008 Series A, D & E	4.127	67% LIBOR	N/A	Aa3	(19,357)

\* As a result of the continuing fallout from the sub-prime mortgage crisis, Lehman Brothers Holdings Inc., the counterparty to these swaps, filed for bankruptcy on September 15, 2008.

Under these interest rate swap agreements, the Authority incurred net interest expense of \$11,238 and \$4,975 in fiscal 2008 and fiscal 2007, respectively.

For the swap execution on March 22, 2000, with a current notional amount of \$266,600, the fixed rate paid by the Authority is as follows: 5.130% from execution through August 2005, 4.470% from August 2005 through August 2013, 5.494% from August 2013 through August 2019, and 6.935% from August 2019 through August 2030.

Lehman Brothers Holdings, Inc., the parent company of the counterparties to two of these swaps, filed for bankruptcy on September 15, 2008. The first swap is with Lehman Brothers Financial Products Inc. for an initial notional amount of \$270,600 and covers the period from March 22, 2000 until August 1, 2030. Lehman Brothers Financial Products Inc. was not self-liquidating and designed to be remote from the bankruptcy of Lehman Brothers Holdings Inc. and therefore had a decreased risk of termination of that swap. Under the existing structure, the swap would be managed by contingent manager which was scheduled to be West LB. Subsequent to the parent company bankruptcy filing, Lehman Brothers Financial Products, Inc. filed for bankruptcy on October 5, 2008. As provided for under the existing ISDA

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Agreement, the Authority issued a Request for Quotations to find a replacement counterparty. Under the terms of the ISDA Agreement, after excluding the highest and lowest values, the median of the bid amounts will be the termination payment. On October 28, 2008, the Authority secured two replacement counterparties and received payments from the replacement counterparties in excess of the amount of the termination payment of \$47,994. The termination payment, net of adjustments, was made on November 3, 2008.

The second swap, which has a notional amount of \$70,400 and covers the period of August 1, 2030 until the bonds mature in 2037, was with Lehman Brothers Derivative Products, Inc. (LBDP). LBDP was a self-liquidating subsidiary which means that there was a higher risk of termination of that swap if a termination trigger event occurs, such as bankruptcy or credit downgrade. The Authority negotiated to have this swap assigned to Lehman Brothers Special Financing, Inc. to preserve the swap for an interim period. Lehman Brothers Special Financing, Inc. filed for bankruptcy on October 5, 2008. The Authority has issued a Request for Quotations to find a replacement counterparty and determine the termination value of the swap. The market value if the swap were to be terminated is currently estimated at \$4,100 as of October 10, 2008.

#### ***Risk Disclosure***

*Credit Risk* – Because all of the Authority’s swaps rely upon the performance of the third parties who serve as swap counterparties, the Authority is exposed to credit risk, or the risk that a swap counterparty fails to perform according to its contractual obligations. The appropriate measurement of this risk at the reporting date is the fair value of the swaps, as shown in the columns labeled fair value in the tables above. All fair values have been calculated using the mark to market or par value method. To mitigate credit risk, the Authority maintains strict credit standards for swap counterparties. All swap counterparties for longer term swaps are rated in the A+ category or higher by at least two of the three rating agencies (FITCHRATINGS, Moody’s Investors Service, and Standard and Poor’s).

*Basis Risk* – The Authority is exposed to basis risk if the relationship between the floating index the Authority receives on the swaps (BMA or 67% of LIBOR) falls short of the variable rate on the associated bonds. Should this occur, the expected savings may not be realized.

#### ***Swap Payments and Associated Bonds Outstanding***

Bonds outstanding include certain variable rate bonds where the Authority pays a fixed interest rate and receives interest at a variable rate from a counterparty. The table below presents the debt service requirements and related net swap payments for these bonds. As rates vary, variable rate interest payments will vary.

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Using rates as of June 30, 2008, debt service requirements of the variable rate bonds and net swap payments, assuming current interest rates remains constant, were as follows:

<b>Fiscal year ending June 30</b>	<b>Variable-rate</b>		<b>Interest rate swaps, net</b>	<b>Total</b>
	<b>Principal</b>	<b>Interest</b>		
2009	\$ 10,000	37,465	17,407	64,872
2010	14,500	36,794	12,113	63,407
2011	46,600	35,079	8,057	89,736
2012	44,215	32,943	5,490	82,648
2013	50,510	30,671	4,395	85,576
2014-2018	236,070	117,261	21,570	374,901
2019-2023	239,870	68,608	23,229	331,707
2024-2028	104,870	28,186	13,049	146,105
2029-2033	5,650	17,159	8,908	31,717
2034-2038	65,090	7,242	4,657	76,989
<b>Total</b>	<b>\$ 817,375</b>	<b>411,408</b>	<b>118,875</b>	<b>1,347,658</b>



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At June 30, 2008, the following bonds outstanding are considered defeased in-substance:

<b>Description</b>	<b>Redemption date</b>	<b>Redemption price</b>	<b>Outstanding principal amount</b>
1990 Series A	2009 – 2020	102	\$ 602,975
1991 Series A	2011 – 2021	100 to 102	224,630
1992 Series A	2008 – 2022	100 to 102	646,325
1992 Series B	2008 – 2020	100	345,095
1993 Series A	2008 – 2013	100 to 102	44,285
1993 Series B	2009 – 2022	100 to 102	363,915
1993 Series C	2008 – 2023	100 to 102	265,285
1993 Series D	2008 – 2014	100 to 102	35,640
1994 Series A	2008 – 2024	102	113,145
1995 Series A	2008 – 2015	100 to 102	40,195
1995 Series B	2008 – 2024	100	204,060
1996 Series A	2008 – 2026	100 to 102	121,095
1997 Series A	2009 – 2028	100	74,200
1997 Series B	2009 – 2028	100	74,200
1997 Series D	2009 – 2012	100 to 101	5,570
1998 Series A	2009 – 2020	100	75,385
1998 Series B	2009	100	385
1998 Series C	2008 – 2018	100 to 102	75,980
1998 Series D	2008 – 2026	100	198,895
1999 Series A	2009 – 2028	100	86,100
1999 Series C	2009 – 2029	100	66,800
1999 Series D	2009 – 2029	100	66,800
2000 Series A	2008 – 2039	100	271,295
2000 Series B	2020 – 2037	100	133,300
2000 Series C	2020 – 2037	100	133,300
2000 Series D	2009 – 2011	100	150,000
2001 Series A	2008 – 2023	100	82,600
2001 Series B	2023 – 2031	100	85,000
2002 Series B	2008 – 2024	100	95,940
2002 Series E	2010 – 2011	100	83,400
2002 Series F	2012 – 2013	100	90,900
2002 Series G	2014 – 2015	100	99,250
2002 Series J	2012	100	38,315
2003 Series D	2008 – 2021	100	44,475
2004 Series A	2008 – 2020	100	21,650
2004 Series B	2016	100	15,865
2005 Series A	2010	100	2,690
2006 Series B	2015 – 2020	100	21,375

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The proceeds and available funds were deposited in irrevocable trusts with escrow agents in an amount which will provide for payment of interest due to the redemption date and redemption of the defeased bonds outstanding on such date. The defeased portion of such debt, accrued interest thereon, and related unamortized issuance and discount costs were removed from the balance sheet in an in substance defeasance transaction.

In June 2008, the Authority used funds on hand to defease \$5,570 of the 1997 Series D and \$385 of the 1998 Series B General Revenue bonds outstanding.

In May 2007, the Authority deposited \$42,781 on into an escrow account with the trustee to defease \$38,315 of the 2002 Series J and \$2,690 of the 2005 Series A General Revenue bonds outstanding.

At June 30, 2008, outstanding bonds that are redeemable before their scheduled due dates are as follows:

<b>Description</b>	<b>Redemption date</b>	<b>Redemption price</b>	<b>Outstanding principal amount</b>
1997 Series D	August 2008	100 – 101	\$ 113,375
1998 Series A	August 2008	100	100,355
1998 Series B	August 2008	100	72,945
2002 Series B	August 2011	100 – 101	74,415
2002 Series J	August 2012	100	200,000
2003 Series D	August 2013	100	113,340
2004 Series A	August 2014	100	104,870
2004 Series B	August 2014	100	49,390
2005 Series A	August 2017	100	285,000
2005 Series B	August 2017	100	80,290
2006 Series A	August 2018	100	200,000
2006 Series B	August 2018	100	261,775
2007 Series A	February 2017	100	200,000

The variable rate General Revenue Bonds are subject to redemption prior to maturity at the option of the Authority in whole or in part, on any interest payment date.

During fiscal 2008, the Authority executed loan agreements with Massachusetts Water Pollution Abatement Trust (MWPAT) providing for 2007 Series C, 2007 Series D and 2007 Series E Sewer and Water loans in the principal amounts of \$7,525, \$22,978, and \$81,765, respectively. All proceeds for these loans were received by June 30, 2008, except \$3,539, principal for 2007 Series E Sewer and Water. The remaining funds are expected to be drawn down in fiscal 2009.

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During fiscal 2007, the Authority executed loan agreements with Massachusetts Water Pollution Abatement Trust (MWPAT) providing for 2006 Series C, 2006 Series D and 2006 Series E Sewer and Water loans in the principal amounts of \$8,646, \$96,708, and \$542, respectively. All proceeds for these loans were received by June 30, 2007, except \$11,071, principal for 2006 Series D Sewer and Water. The remaining funds are expected to be drawn down in fiscal 2008.

Federal and Commonwealth subsidies for purposes of offsetting principal payments aggregating \$110,867 will be recognized as capital grants in aid of construction over the term of the loans.

Interest is payable semiannually on all debt, except on the commercial paper and capital appreciation bonds, on which interest is payable upon maturity and the General Revenue Bonds with variable interest rates on which interest is payable monthly. The Senior General Revenue Bonds and the General Revenue Refunding Bonds are collateralized equally and ratably by a lien and pledge on substantially all of the Authority's cash and revenues, except the operating fund. The subordinated debt series, including the commercial paper are collateralized equally and ratably by a subordinated pledge on substantially all of the Authority's revenues and cash and investments, except the operating, debt service, and debt service reserve funds. Premiums, discounts, issuance costs, and the excess of reacquisition price over the carrying amount of the defeased debt are being amortized over the lives of the respective issues.

The amounts of long-term debt, principal, and interest payable in future fiscal years are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Year ending June 30:			
2009	\$ 77,224	235,117	312,341
2010	74,937	232,430	307,367
2011	103,451	229,027	332,478
2012	121,457	224,448	345,905
2013	110,332	220,743	331,075
2014 – 2018	825,766	1,016,567	1,842,333
2019 – 2023	1,306,250	800,659	2,106,909
2024 – 2028	1,238,418	505,439	1,743,857
2029 – 2033	806,702	265,377	1,072,079
2034 – 2038	465,052	126,230	591,282
2039 – 2043	228,940	46,604	275,544
2044 – 2048	106,020	9,275	115,295
Total	\$ <u>5,464,549</u>	<u>3,911,916</u>	<u>9,376,465</u>

The Authority issued commercial paper notes of \$191,000 to finance capital expenditures, which are secured by \$100,000 and \$250,000 irrevocable direct-pay letters of credit which expire on September 8, 2009, and May 20, 2010, respectively. These letters of credit carry a fee of 0.27% and 0.30% per annum, respectively, on the amount available. The maximum aggregate principal amount of commercial paper which may be outstanding at any one time is \$350,000.

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Commercial paper at June 30, 2008 and 2007 consisted of the following:

	<b>2008 Beginning balance</b>	<b>Additions</b>	<b>Reductions</b>	<b>2008 Ending balance</b>
3.62% commercial paper	\$ 39,000		39,000	—
3.70% commercial paper	—	52,000	—	52,000
3.75% commercial paper	—	139,000	—	139,000
	<u>\$ 39,000</u>	<u>191,000</u>	<u>39,000</u>	<u>191,000</u>
	<b>2007 Beginning balance</b>	<b>Additions</b>	<b>Reductions</b>	<b>2007 Ending balance</b>
3.00% commercial paper	\$ 164,000	—	164,000	—
3.62% commercial paper	—	39,000	—	39,000
	<u>\$ 164,000</u>	<u>39,000</u>	<u>164,000</u>	<u>39,000</u>

**(7) Accounts Receivable/Intergovernmental Loans**

The Authority has entered into various interest-free loan agreements with certain member communities. Under these agreements, the Authority loaned these communities \$17,086 and \$35,232 in fiscal 2008 and 2007, respectively, to be received in five or ten equal annual installments.

The long-term portion of these loans at June 30, 2008 and 2007, is \$96,144 and \$101,715, respectively, and is included in other assets. The loans due within one year total \$22,660 and \$22,097 at June 30, 2008 and 2007, respectively. This program is designed to assist member communities with sewer and water systems rehabilitation.

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**(8) Capital Assets**

Capital assets at June 30, 2008 and 2007, consisted of the following:

	<u>2007</u>	<u>Additions</u>	<u>Disposals/ transfers</u>	<u>2008</u>
Capital assets – not being depreciated:				
Land	\$ 6,692	—	—	6,692
Construction in progress	<u>273,516</u>	<u>175,658</u>	<u>(163,233)</u>	<u>285,941</u>
Total capital assets – not being depreciated	<u>280,208</u>	<u>175,658</u>	<u>(163,233)</u>	<u>292,633</u>
Capital assets – being depreciated:				
Plant and equipment – water and sewage system	8,267,612	163,233	—	8,430,845
Furniture and fixtures	33,061	—	—	33,061
Leasehold improvements	5,081	—	—	5,081
Motor vehicles and equipment	<u>1,595</u>	<u>—</u>	<u>—</u>	<u>1,595</u>
Total capital assets – being depreciated	<u>8,307,349</u>	<u>163,233</u>	<u>—</u>	<u>8,470,582</u>
Less accumulated depreciation for:				
Plant and equipment – water and sewage system	2,144,794	166,230	—	2,311,024
Furniture and fixtures	30,851	2,189	—	33,040
Leasehold improvements	4,675	12	—	4,687
Motor vehicles and equipment	<u>1,042</u>	<u>19</u>	<u>—</u>	<u>1,061</u>
Total accumulated depreciation	<u>2,181,362</u>	<u>168,450</u>	<u>—</u>	<u>2,349,812</u>
Total capital assets – being depreciated – net	<u>6,125,987</u>	<u>(5,217)</u>	<u>—</u>	<u>6,120,770</u>
Capital assets – net	<u>\$ 6,406,195</u>	<u>170,441</u>	<u>(163,233)</u>	<u>6,413,403</u>

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Capital assets at June 30, 2007 and 2006, consisted of the following:

	<u>2006</u>	<u>Additions</u>	<u>Disposals/ transfers</u>	<u>2007</u>
Capital assets – not being depreciated:				
Land	\$ 11,036	—	(4,344)	6,692
Construction in progress	245,542	132,992	(105,018)	273,516
Total capital assets – not being depreciated	<u>256,578</u>	<u>132,992</u>	<u>(109,362)</u>	<u>280,208</u>
Capital assets – being depreciated:				
Plant and equipment – water and sewage system	8,162,594	105,018	—	8,267,612
Furniture and fixtures	33,061	—	—	33,061
Leasehold improvements	5,081	—	—	5,081
Motor vehicles and equipment	1,595	—	—	1,595
Total capital assets – being depreciated	<u>8,202,331</u>	<u>105,018</u>	<u>—</u>	<u>8,307,349</u>
Less accumulated depreciation for:				
Plant and equipment – water and sewage system	1,980,021	164,773	—	2,144,794
Furniture and fixtures	28,666	2,185	—	30,851
Leasehold improvements	4,663	12	—	4,675
Motor vehicles and equipment	1,025	17	—	1,042
Total accumulated depreciation	<u>2,014,375</u>	<u>166,987</u>	<u>—</u>	<u>2,181,362</u>
Total capital assets – being depreciated – net	<u>6,187,956</u>	<u>(61,969)</u>	<u>—</u>	<u>6,125,987</u>
Capital assets – net	\$ <u>6,444,534</u>	<u>71,023</u>	<u>(109,362)</u>	<u>6,406,195</u>

Depreciation and amortization for fiscal 2008 and 2007, was \$180,173 and \$180,179, respectively.

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**(9) Other Assets**

On December 17, 1997, the Authority sold to Massachusetts Heavy Industries, Inc. (MHI) certain land, buildings, machinery, equipment, and other items located within a former shipbuilding facility, known as the Fore River Shipyard, for a total purchase price of \$10,000. The Authority received \$3,000 in December 1997. The remaining balance of \$7,000 was due to be received beginning in December 1999. In accordance with FASB No. 71, the original loss of \$28,303 was accounted for as a deferred charge and is expected to be recovered through future rates. During fiscal 2000, the \$7,000 receivable was determined to be uncollectible increasing the deferred loss on the original sale to \$35,303.

**(10) Leases**

*(a) Operating*

The Authority leases electrical power assets, office space in Boston, and other property under long-term operating leases. Future minimum rental payments required under operating leases having initial or remaining noncancelable lease terms in excess of one year at June 30, 2008, are as follows:

Year ending June 30:	
2009	\$ 5,818
2010	5,239
2011	5,091
2012	5,682
2013	4,783
2014 – 2016	9,785
Total	<u>\$ 36,398</u>

Rental expense was \$6,977 and \$7,362 in fiscal years 2008 and 2007, respectively.

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**(b) Capital**

In fiscal 2003, the Authority entered into a 30-year capital lease agreement for the new maintenance facility. The interest rate for the capital lease is 7.83%. Future minimum lease payments for the capital lease at June 30, 2008, are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Year ending June 30:			
2009	\$ 516	2,701	3,217
2010	558	2,659	3,217
2011	603	2,614	3,217
2012	652	2,565	3,217
2013	705	2,512	3,217
2014 – 2018	4,481	11,604	16,085
2019 – 2023	6,618	9,467	16,085
2024 – 2028	9,779	6,306	16,085
2029 – 2032	10,821	1,780	12,601
Total	\$ <u>34,733</u>	<u>42,208</u>	<u>76,941</u>

Under this lease, the Authority is also responsible for “Additional Rent,” as defined in the lease. The Additional Rent includes real estate taxes, assessments, and other government charges.

The associated capital asset is reported in plant and equipment – water and sewage system at a cost of \$37,134 with \$7,428 of depreciation accumulated as of June 30, 2008.

**(11) Retirement Benefits**

**(a) Plan Description**

The Enabling Act provided for the establishment of the Massachusetts Water Resources Authority Employees’ Retirement System (the Plan), a contributory single-employer retirement system that is separate from the State Employees Retirement System. The Plan is a defined benefit pension plan covering those employees not employed by the MDC prior to July 1, 1985. Total payroll and covered payroll for all Authority employees in the Plan were \$78,946 and \$75,029, respectively, for the year ended June 30, 2008.

Under the provisions of the Plan, pension benefits vest after 10 years of full-time employment. An employee may retire after 20 years of service or at age 55 and completion of 10 years of service. At age 65, annual pension benefits equal 2.5% of the employee’s average regular compensation earned during the last three years of employment or any three consecutive years when compensation was higher, multiplied by each year of creditable service. The benefit is reduced if retirement occurs before age 65 or if survivor’s benefits are elected. The Plan also provides death and disability benefits. Ordinary disability benefits are available only to employees under age 55 with at least



**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

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(Dollars in thousands)

10 years of service. Complete financial statements for the Plan can be obtained from the Authority's administrative offices at Charlestown Navy Yard, 100 First Avenue, Boston, MA 02129.

**(b) Funding Policy**

Contributions made by employees are based upon a percentage of employee base pay (5% for employees hired before December 31, 1974, 7% for employees hired between January 1, 1975 and December 31, 1983, 8% for employees hired between December 31, 1983, and June 30, 1996, and 9% for employees hired after July 1, 1996). Additionally, certain employees earning in excess of \$30 contribute an extra 2% of their salary effective January 1, 1979. Employees receive full payment of contributions upon withdrawal from the Plan and 50% of interest earned for employees with five to nine years of service or 100% of interest earned for employees with 10 or more years of service.

The Authority's 2008 and 2007 contributions to the plan were based on an amount approved by the Retirement Board and the Authority's board of directors, which is based on an actuarially determined amount. The Authority's Enabling Act requires funding to be made in accordance with the Retirement Board's recommendation.

**(c) Annual Pension Cost and Net Pension Obligation**

The annual required contribution for the current year, determined by the January 1, 2007 actuarial valuation, was as follows:

Annual required contribution	\$	4,233
Contributions made		<u>(4,233)</u>
Increase (decrease) in net pension obligation		—
Net pension obligation, beginning of year		<u>—</u>
Net pension obligation, end of year	\$	<u><u>—</u></u>

**(d) Three-Year Trend Information**

	<u>Annual pension cost (APC)</u>	<u>Percentage of APC contributed</u>	<u>Net pension asset/ (obligation)</u>
Fiscal year ending:			
2008	\$ 4,259	100%	\$ —
2007	4,094	100	—
2006	3,577	100	—

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

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**(e) Funded Status and Funding Progress**

As of January 1, 2007, the most recent actuarial valuation date, the funded status of the Plan was as follows:

Actuarial accrued liability	\$	255,962
Actuarial value of assets		<u>211,716</u>
Unfunded actuarial accrued liability (UAAL)	\$	<u>44,246</u>
Funded ratio		<u>82.7%</u>
Covered payroll	\$	<u>75,444</u>
UAAL as percentage of covered payroll		<u>58.6%</u>

The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits. Effective for the January 1, 2007 actuarial valuation, the Authority changed to the entry age normal actuarial cost method. Prior actuarial valuations were completed using the aggregate cost method.

**(f) Actuarial Methods and Assumptions**

The annual required contribution for the current year was determined as part of the January 1, 2007, actuarial valuation using the entry age normal actuarial cost method. Under this method an unfunded actuarial accrued liability of \$44.2 million was calculated. The actuarial assumptions included (a) 8% investment rate of return and (b) projected salary increase of 4.8% per year. Liabilities for cost of living increases have been assumed at an annual increase of 3%, on the first \$12 of benefit payments. The actuarial value of assets is determined by projecting the market value of assets as of the beginning of the prior plan year with the assumed rate of return during that year (8.0%) and accounting for deposits and disbursements with interest at the assumed rate of return. An adjustment is then applied to recognize the difference between the actual investment return and expected return over a five year period. As of January 1, 2007 the unfunded actuarially accrued liability is being amortized over 17 years using an open group method which assumes a 4.5% per year increase in payroll.

# MASSACHUSETTS WATER RESOURCES AUTHORITY

## Notes to Financial Statements

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**(g) Other Benefits**

All MDC personnel who became employees of the Authority on July 1, 1985, and were members of the State Employees Retirement System, retained their membership in that system. The Authority is not liable for retirement allowances paid to or on account of these employees. Funding of the pension liability of the State Employees Retirement System is the obligation of the Commonwealth. Employees covered by this plan become 100% vested after 10 years of service. The Authority's covered payroll for members of this plan for the year ended June 30, 2008, was \$8,341.

**(12) Other Postemployment Benefits**

During the year, the Authority implemented GASB Statement No 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. Statement No. 45 requires governments to account for other postemployment benefits (OPEB), primarily healthcare, on an accrual basis rather than on a pay-as-you-go basis. The effect is the recognition of an actuarially required contribution as an expense on the statement of revenues, expenses, and changes in net assets when a future retiree earns their postemployment benefits, rather than when they use their postemployment benefit. To the extent that an entity does not fund their actuarially required contribution, a postemployment benefit liability is recognized on the balance sheet over time.

**(a) Plan Description**

In addition to providing the pension benefits described, the Authority provides postemployment health care and life insurance benefits for retired employees through the Group Insurance Commission (GIC). The GIC is a quasi-independent state agency that administers an agent multi-employer defined benefit OPEB plan. The benefits, benefit levels, employee contributions and employer contributions are governed by the Authority and can be amended by the Authority. As of January 1, 2006, the actuarial valuation date, approximately 257 retirees and 1,108 active employees meet the eligibility requirements. The plan does not issue a separate financial report.

**(b) Benefits Provided**

The Authority provides medical, prescription drug, mental health/substance abuse and life insurance to retirees and their covered dependents. All active employees who retire from the Authority and meet the eligibility criteria will receive these benefits.

**(c) Funding Policy**

Retirees who retired on or before July 1, 1994 contribute 10% of the cost of the health plans, as determined by the GIC. Those who retired after July 1, 1994 contribute 15% of the cost of the health plan, as determined by the GIC. The Authority contributes the remainder of the health plan costs on a pay-as-you-go basis.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

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June 30, 2008 and 2007

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**(d) Annual OPEB Costs and Net OPEB Obligation**

The Authority's fiscal 2008 annual OPEB expense is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost per year and amortize the unfunded actuarial liability over a period of thirty years. The following table shows the components of the Authority's annual OPEB cost for the year ending June 30, 2008, the amount actually contributed to the plan, and the change in the Authority's net OPEB obligation based on an actuarial valuation as of January 1, 2006:

Annual Required Contribution (ARC)	\$	15,120
Interest on net OPEB obligation		—
Adjustment to ARC		—
		<hr/>
Annual OPEB cost		15,120
Contributions made		<hr/> (1,694)
		<hr/>
Increase in net OPEB obligation		13,426
Net OPEB obligation – beginning of year		<hr/> —
Net OPEB obligation – end of year	\$	<hr/> <hr/> 13,426

The Authority's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation were as follows:

<u>Fiscal year ended</u>		<u>Annual OPEB cost</u>		<u>Percentage of OPEB cost contributed</u>		<u>Net OPEB obligation</u>
2008	\$	15,120		11%	\$	13,426

The Authority's net OPEB obligation as of June 30, 2008 is recorded as a component of the "other long-term liabilities" line item.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

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(Dollars in thousands)

**(e) Funded Status and Funding Progress**

The funded status of the plan as of January 1, 2006, the date of the most recent actuarial valuation, was as follows:

Actuarial accrued liability (AAL)	\$ 154,449
Actuarial value of plan assets	<u>—</u>
Unfunded actuarial accrued liability (UAAL)	<u>154,449</u>
Funded ratio (actuarial value of plan assets/AAL)	<u>—%</u>
Covered payroll (active plan members)	\$ <u>72,476</u>
UAAL as a percentage of covered payroll	<u>213%</u>

Actuarial valuations of an ongoing plan involve estimates of the value of reported amount and assumptions about the probability of occurrence of events far into the future. Examples included assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

**(f) Actuarial Methods and Assumptions**

Projections of benefits for financial reporting purposes are based on the plan as understood by the Authority and the plan members and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the Authority and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the January 1, 2006 actuarial valuation the projected unit credit cost method was used. The actuarial value of assets was not determined as the Authority has not advance funded its obligation. The actuarial assumptions included a 4.5% investment rate of return and an initial annual healthcare cost trend rate of 10.5% which decreases to a 5% long-term trend rate for all healthcare benefits after ten years. The amortization costs for the initial UAAL is a level percentage of payroll for a period of 30 years, on a closed basis. This has been calculated assuming the amortization payment increases at a rate of 4.5%.

# MASSACHUSETTS WATER RESOURCES AUTHORITY

## Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

### (13) Commitments and Contingencies

#### (a) *General*

The Authority's capital improvement program continues to proceed. As part of this program, the Authority has entered into a number of contracts for the design and construction of infrastructure and improvements to its facilities. Commitments under these contracts aggregated approximately \$263,901 at June 30, 2008.

The Authority's operating and construction plans are designed to comply with the Federal District Court's schedule of actions. The Authority has incurred capital expenditures of approximately \$7,251,000 from fiscal 1986 through fiscal 2008, including those projects required to comply with the Federal District Court's schedule. The Authority anticipates spending an additional \$1,755,000 on these projects through fiscal 2018. These capital expenditures have been forecasted based upon certain preliminary assumptions and estimates, which may change significantly as design and construction of the necessary facilities proceed. Funding is expected to come from various federal and state grants, as available and approved, and from the Authority's debt proceeds. To date, federal appropriations for the Boston Harbor Project have aggregated \$810,000.

#### (b) *Boston Harbor Case*

The Authority continues to be a defendant, along with Boston Water and Sewer Commission (BWSC) and the Commonwealth, in the federal Boston Harbor Case. The federal action was originally brought in 1985 by the United States on behalf of the United States Environmental Protection Agency (EPA) and by certain citizens groups for Clean Water Act violations. As part of the Boston Harbor Case, the Authority was required to undertake certain corrective actions to meet wastewater treatment, discharge and combined sewer overflow (CSO) requirements. The only corrective action remaining is CSO related which is currently scheduled for completion in 2015.

In March 2006, the Authority reached agreement with the United States and the Massachusetts Department of Environmental Protection (DEP) on the scope and schedule for the remaining CSO projects which was filed with the Court as part of a joint motion to amend the Court Schedule. In April 2006, the Court allowed the joint motion and issued an Order with a schedule. Under the Order, the Authority has until 2020 to complete the remaining CSO work and subsequent monitoring which will be used to verify that the long term CSO control goals are achieved.

As part of the agreement, DEP agreed to reissue and EPA agreed to approve five (5) consecutive variances of no more than three years duration each, through the year 2020, for the Charles River and Alewife Brook/Upper Mystic River that are consistent with and limited to the requirements in the Authority's revised Long Term CSO Control Plan. Variances have most recently been issued by DEP in August 2007. The variances will remain in place for the Charles River until October 1, 2010 and for the Alewife/Upper Mystic until September 1, 2010. In addition, the United States and the Authority agreed to withdraw the February 27, 1987 *Stipulation of the United States and the Massachusetts Water Resources Authority on Responsibility and Legal Liability for Combined Sewer Overflows* and replace it with a Second Stipulation that requires the Authority to implement the CSO requirements set forth in the Court Schedule and to meet the levels of control described in the

# MASSACHUSETTS WATER RESOURCES AUTHORITY

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(Dollars in thousands)

Authority's long term CSO control plan. Upon completion of the long term CSO control plan and with results that demonstrate performance parameters are as predicted, the stipulation makes the Authority responsible for only those CSO outfalls which it owns and operates. As a result of the agreement, the Authority now has 35 CSO projects, 22 of which are complete, and six of which are under construction. The estimated cost to complete the Authority's long term CSO control plan is now \$964 million, including contingency and escalation of unawarded contracts.

The Authority and the City of Cambridge (City) plan to resume design efforts in October 2008 as to several CSO projects which comprise the Alewife Brook CSO control plan while continuing to monitor a citizens' group Chapter 30A appeal pending in Suffolk Superior Court (SUCV2007-05011-F). The appeal was taken from an October 2007 Final Decision of DEP which upheld a Superseding Order of Conditions (Order) issued by DEP in March 2005 with respect to the City's CambridgePark Drive Area Drainage Project. While the pending appeal does not pose a direct challenge to the CSO control plan, progress on final design and construction of projects by the Authority and the City can still be affected by the final outcome of the appeal, especially if the terms of the Order and the Final Decision concerning wetlands and storm water control issues are modified. To date, portions of the Alewife Brook projects have been delayed for 27 months beyond scheduled Court milestones primarily because of continuing uncertainties arising out of this litigation.

There has been no imposition of penalties by the Court against the Authority on the merits of the claims originally asserted in the Boston Harbor Case to date. EPA and the Authority in the past year settled a separate civil enforcement proceeding in which the Authority will pay a small civil penalty and perform three supplemental environmental projects to resolve allegations contained in a supplemental complaint filed with the Court in the Boston Harbor case on July 1, 2008. The Court is expected to enter the parties' settlement agreement as an Order in the case in early fall of 2008.

In addition, the Court always retains the right to order further remedial action and assess penalties.

(c) ***Deer Island Submarine Power Cable***

In 2004, the United States Army Corps of Engineers (Corps) notified Boston Edison Co. (BECo, now N-Star), its subsidiary Harbor Energy Electric Company (HEEC) and the Authority that they were in violation of a permit (MA BOSS 198900530, dated August 31, 1989) which authorized the installation of a submarine electric power cable running under Boston Harbor from South Boston to Deer Island. The Corps alleges that the power cable, in places, had been installed at depths less than those required by permit. The Corps has demanded that the permittees develop plans and an implementation schedule for bringing the cable into compliance with the permit. The demand has been made in connection with proposed dredging operations intended to deepen the harbor channel as to make it navigable by deep-draft vessels. The Authority has responded stating that it had become a co-permittee only to facilitate issuance of the permit, that it did not install and has never owned the cable, and therefore, it had neither any right nor responsibility, nor the ability, to move or alter the position of the cable. In 2005, the Corps referred the matter to the United States Department of Justice. In May 2005, the Department of Justice advised the permittees that the matter had been referred to it by the Corps for the purpose of either commencing a lawsuit to compel the relocation of

# MASSACHUSETTS WATER RESOURCES AUTHORITY

## Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

the cable or negotiating an amicable resolution that would bring the permittees into compliance with the permit's conditions. The Authority has informed the Court in the Boston Harbor Case of its position in its Compliance and Progress report filed on June 15, 2005. The Department of Justice (DOJ) and the permittees have continued to meet at various times since October 2005 to discuss this matter, the most recent meeting having occurred in January 2008. At the meeting, representatives of the Authority, NStar, HEEC, the Corps and DOJ further discussed the options for relocation or protection of the cable during the intended channel-deepening dredging operations. Representatives of the Corps and NStar/HEEC had previously met several times to discuss a so-called "mechanical option" which involves protecting the cable by covering it with concrete mats. The Corps and DOJ seemed more amenable to that option than in the past but have required a further triangulation study to be done by NStar/HEEC to more precisely locate the position/depth of the cable before agreeing to it. While this study has been undertaken by NStar/HEEC in August 2008, there is no firm date when the study's findings will be released to the Corps, DOJ or the Authority. Whatever option may ultimately be agreed upon, NStar and HEEC have asserted that they intend to pass the costs associated with the relocation and/or protection of the cable along to the Authority. The Authority has advised NStar and HEEC that it believes it has no financial responsibility whatsoever for these costs.

**(d) *Miscellaneous***

The Authority is also a defendant in several legal actions and administrative proceedings arising out of its operation, maintenance, and improvement of the water and sewer systems under its care. It is the opinion of management that any judgments or settlements that may result from these actions will not have a materially adverse effect upon the Authority.

**(14) Risk Management**

The Authority is exposed to various risks of loss. The risk management program involves insurance and self insurance related to property, general liability (including automobile, marine and employers' liability), excess liability, public officials' liability, workers' compensation, unemployment liability, and employee health care and life insurance.

Buildings, plants, and equipment are fully insured on an all risk replacement basis to the extent that losses exceed \$2,500 per occurrence. The Authority maintains insurance coverage for general liability, automobile liability, marine liability, and employers' liability to the extent that losses exceed \$2,500 per occurrence, up to a limit of \$35,000. In addition to the primary liability insurance, the Authority maintains an excess liability policy with an additional limit of \$65,000. The Authority also maintains public officials' errors and omissions insurance with a limit of \$5,000 per occurrence with a \$1,000 deductible. All insurance policies are renewed on an annual basis.

The Authority reimburses the Commonwealth on a paid-claims basis for unemployment claims. Claims expensed during fiscal 2008 and 2007 were \$81 and \$52, respectively. The Authority is a licensed self-insurer for workers' compensation. Excess loss insurance is carried on workers' compensation as required by law in excess of \$500 per occurrence retention, with a limit of \$25,000 per occurrence.



**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Notes to Financial Statements

June 30, 2008 and 2007

(Dollars in thousands)

The Authority participates in and pays premiums to the Commonwealth's Group Insurance Commission for employee health benefits. The Authority pays 85% of these health premiums, with employees paying the balance.

Insurance claims have not exceeded insurance coverage in any of the last three fiscal years.

GASB Statement No. 10 requires that liabilities for self-insured claims be reported if it is probable that a loss has been incurred and the amount can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. The Authority records such liabilities in accrued expenses.

Changes in the claims liability insurance reserves in fiscal 2008 and 2007 were as follows:

	<b>General liability and property</b>	<b>Workers' compensation</b>
Liability balance – June 30, 2006	\$ 2,239	2,111
Provision to record estimated losses	531	1,236
Payments	(894)	(1,620)
Liability balance – June 30, 2007	1,876	1,727
Provision to record estimated losses	623	1,160
Payments	(670)	(1,614)
Liability balance – June 30, 2008	\$ 1,829	1,273

**REQUIRED SUPPLEMENTARY INFORMATION**

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Schedules of Funding Progress

Required Supplementary Information

June 30, 2008

(Unaudited)

(Dollars in thousands)

**Employees' retirement system**

<b>Actuarial valuation</b>	<b>Assets (a)</b>	<b>Actuarial Accrued Liability (AAL) – (b)</b>	<b>Unfunded AAL (UAAL) (b-a)</b>	<b>Funded ratio (a/b)</b>	<b>Covered payroll (c)</b>	<b>UAAL as a percentage of covered payroll ((b-a)/(c))</b>
January 1, 2007	\$ 211,716	255,962	44,246	82.7%	\$ 75,444	58.6%
January 1, 2005	172,512	172,512	—	100.0	75,790	—
January 1, 2003	146,188	146,188	—	100.0	66,711	—
January 1, 2002	141,069	141,069	—	100.0	66,322	—
January 1, 2001	128,385	128,385	—	100.0	65,955	—
January 1, 1999	96,318	96,318	—	100.0	66,782	—

Effective for the January 1, 2007 actuarial valuation, the Authority changed actuarial cost methods. See footnote 11 (e).

**Other postemployment benefits**

<b>Actuarial valuation</b>	<b>Assets (a)</b>	<b>Actuarial Accrued Liability (AAL) – (b)</b>	<b>Unfunded AAL (UAAL) (b-a)</b>	<b>Funded ratio (a/b)</b>	<b>Covered payroll (c)</b>	<b>UAAL as a percentage of covered payroll ((b-a)/(c))</b>
January 1, 2006	\$ —	154,449	154,449	—%	\$ 72,476	213.1%

See accompanying independent auditors' report.

## **SUPPLEMENTAL SCHEDULES**

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Accounts Established by the General Revenue Bond Resolution

Year ended June 30, 2008  
(comparative totals for June 30, 2007)

(Dollars in thousands)

	<u>Construction</u>	<u>Revenue</u>	<u>Debt service</u>	<u>Reserves</u>	<u>Total</u>
Balance – June 30, 2007	\$ 83,892	66,328	456,675	50,426	657,321
Proceeds from:					
Revenue bonds and loans	195,355	—	77,000	—	272,355
Cash received from customers	—	540,366	—	—	540,366
Debt service grant	—	—	16,980	—	16,980
Interest income	4,672	8,595	24,551	2,614	40,432
Grant receipts	—	—	6,852	—	6,852
Construction payments	(182,548)	1,763	—	—	(180,785)
Capital lease payments	(480)	—	(2,737)	—	(3,217)
Debt service payment	(945)	(1,710)	(422,247)	—	(424,902)
Other commonwealth payments	—	(20,923)	—	—	(20,923)
Interfund transfers	1,825	(292,134)	290,406	(97)	—
Transfers from (to) operating account	3,466	(234,832)	2,735	—	(228,631)
Balance – June 30, 2008	\$ <u>105,237</u>	<u>67,453</u>	<u>450,215</u>	<u>52,943</u>	<u>675,848</u>

	<u>Sewer</u>	<u>Water</u>	<u>2008 total</u>	<u>2007 total</u>
Restricted cash and investments:				
Construction	\$ 59,863	45,374	105,237	83,892
Debt service reserves	141,540	79,328	220,868	253,083
Debt service	120,804	57,183	177,987	148,296
Revenue redemption	3,820	27,032	30,852	35,191
Revenue	28,338	39,114	67,452	66,328
Renewal and replacement reserve	21,800	12,147	33,947	31,429
Insurance	9,499	9,498	18,997	18,997
Community obligation and revenue enhancement	17,564	2,944	20,508	20,105
Total restricted cash and investments	\$ <u>403,228</u>	<u>272,620</u>	<u>675,848</u>	<u>657,321</u>

See accompanying independent auditors' report.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Combining Balance Sheet

June 30, 2008

(Dollars in thousands)

<b>Assets</b>	<b>Sewer</b>	<b>Water</b>	<b>Combined total</b>
Unrestricted current assets:			
Cash and cash equivalents	\$ 29,614	13,794	43,408
Investments	35,426	12,364	47,790
Intergovernmental loans	8,607	14,053	22,660
Accounts receivable	147	343	490
Total unrestricted current assets	<u>73,794</u>	<u>40,554</u>	<u>114,348</u>
Restricted assets:			
Cash and investments	411,140	276,021	687,161
Interest receivable	1,896	1,325	3,221
Total restricted assets	<u>413,036</u>	<u>277,346</u>	<u>690,382</u>
Capital assets – not being depreciated	194,089	98,544	292,633
Capital assets – being depreciated – net	3,711,374	2,409,396	6,120,770
Deferred charges	432,944	121,645	554,589
Other assets – net	219,042	80,439	299,481
Total	<u>\$ 5,044,279</u>	<u>3,027,924</u>	<u>8,072,203</u>
<b>Liabilities and Net Assets</b>			
Current liabilities:			
Accounts payable and accrued expenses	\$ 38,796	16,647	55,443
Commercial paper notes	86,449	104,551	191,000
Current portion of long-term debt	68,127	9,097	77,224
Total current liabilities	<u>193,372</u>	<u>130,295</u>	<u>323,667</u>
Payable from restricted assets:			
Accounts payable for construction	30,770	5,867	36,637
Accrued interest on bonds payable	50,397	27,392	77,789
Reserves	72,197	32,444	104,641
Total payable from restricted assets	<u>153,364</u>	<u>65,703</u>	<u>219,067</u>
Retainage on construction in progress	9,907	3,215	13,122
Long-term debt – less current portion	3,545,649	1,771,923	5,317,572
Long-term capital leases	23,650	11,083	34,733
Other long-term liabilities	9,676	3,750	13,426
Deferred credits	27,698	56,962	84,660
Total liabilities	<u>3,963,316</u>	<u>2,042,931</u>	<u>6,006,247</u>
Net assets:			
Invested in capital assets – net of related debt	513,606	775,957	1,289,563
Restricted	148,817	91,987	240,804
Unrestricted	418,540	117,049	535,589
Total net assets	<u>1,080,963</u>	<u>984,993</u>	<u>2,065,956</u>
Commitments and contingencies			
Total	<u>\$ 5,044,279</u>	<u>3,027,924</u>	<u>8,072,203</u>

See accompanying independent auditors' report.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Combining Balance Sheet

June 30, 2007

(Dollars in thousands)

<b>Assets</b>	<b>Sewer</b>	<b>Water</b>	<b>Combined total</b>
Unrestricted current assets:			
Cash and cash equivalents	\$ 26,696	14,132	40,828
Investments	33,458	8,986	42,444
Intergovernmental loans	9,039	13,058	22,097
Accounts receivable	1,448	474	1,922
Total unrestricted current assets	<u>70,641</u>	<u>36,650</u>	<u>107,291</u>
Restricted assets:			
Cash and investments	401,088	263,108	664,196
Interest receivable	3,632	1,450	5,082
Total restricted assets	<u>404,720</u>	<u>264,558</u>	<u>669,278</u>
Capital assets – not being depreciated	172,414	107,794	280,208
Capital assets – being depreciated – net	3,724,096	2,401,891	6,125,987
Deferred charges	363,919	111,138	475,057
Other assets – net	204,803	85,371	290,174
Total	<u>\$ 4,940,593</u>	<u>3,007,402</u>	<u>7,947,995</u>
<b>Liabilities and Net Assets</b>			
Current liabilities:			
Accounts payable and accrued expenses	\$ 39,368	17,098	56,466
Commercial paper notes	15,000	24,000	39,000
Current portion of long-term debt	33,806	17,046	50,852
Total current liabilities	<u>88,174</u>	<u>58,144</u>	<u>146,318</u>
Payable from restricted assets:			
Accounts payable for construction	18,871	2,942	21,813
Accrued interest on bonds payable	49,242	28,099	77,341
Reserves	71,751	32,418	104,169
Total payable from restricted assets	<u>139,864</u>	<u>63,459</u>	<u>203,323</u>
Retainage on construction in progress	9,674	2,178	11,852
Long-term debt – less current portion	3,551,571	1,819,092	5,370,663
Long-term capital leases	23,973	11,237	35,210
Deferred credits	24,172	46,340	70,512
Total liabilities	<u>3,837,428</u>	<u>2,000,450</u>	<u>5,837,878</u>
Net assets:			
Invested in capital assets – net of related debt	628,616	813,334	1,441,950
Restricted	112,167	77,229	189,396
Unrestricted	362,382	116,389	478,771
Total net assets	<u>1,103,165</u>	<u>1,006,952</u>	<u>2,110,117</u>
Commitments and contingencies			
Total	<u>\$ 4,940,593</u>	<u>3,007,402</u>	<u>7,947,995</u>

See accompanying independent auditors' report.

**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Combining Statement of Revenues, Expenses, and Changes in Net Assets

Year ended June 30, 2008

(Dollars in thousands)

	<u>Sewer</u>	<u>Water</u>	<u>Combined total</u>
Operating revenues:			
Customer services	\$ 352,041	182,768	534,809
Other	5,094	506	5,600
Total operating revenues	<u>357,135</u>	<u>183,274</u>	<u>540,409</u>
Operating expenses:			
Operations	60,133	33,600	93,733
Maintenance	21,280	5,129	26,409
Payments in lieu of taxes	—	6,226	6,226
Engineering, general, and administrative	87,562	37,125	124,687
Total operating expenses	<u>168,975</u>	<u>82,080</u>	<u>251,055</u>
Income from operations before depreciation	188,160	101,194	289,354
Depreciation	<u>127,094</u>	<u>53,079</u>	<u>180,173</u>
Operating income	<u>61,066</u>	<u>48,115</u>	<u>109,181</u>
Regulatory accounting provisions:			
Change in reserves	(446)	(26)	(472)
Change in deferred credits – net	65,498	(114)	65,384
Total regulatory accounting provisions	<u>65,052</u>	<u>(140)</u>	<u>64,912</u>
Nonoperating income (expense):			
Debt service grants	15,112	1,868	16,980
Investment income	25,110	16,089	41,199
Interest expense	(194,423)	(88,862)	(283,285)
Total nonoperating expense	<u>(154,201)</u>	<u>(70,905)</u>	<u>(225,106)</u>
Net loss before capital grants	(28,083)	(22,930)	(51,013)
Capital grants	<u>5,881</u>	<u>971</u>	<u>6,852</u>
Decrease in net assets	(22,202)	(21,959)	(44,161)
Total net assets – beginning of year	<u>1,103,165</u>	<u>1,006,952</u>	<u>2,110,117</u>
Total net assets – end of year	\$ <u>1,080,963</u>	<u>984,993</u>	<u>2,065,956</u>

See accompanying independent auditors' report.



**MASSACHUSETTS WATER RESOURCES AUTHORITY**

Combining Statement of Revenues, Expenses, and Changes in Net Assets

Year ended June 30, 2007

(Dollars in thousands)

	<u>Sewer</u>	<u>Water</u>	<u>Combined total</u>
Operating revenues:			
Customer services	\$ 334,636	171,718	506,354
Other	3,720	402	4,122
Total operating revenues	<u>338,356</u>	<u>172,120</u>	<u>510,476</u>
Operating expenses:			
Operations	57,753	29,837	87,590
Maintenance	20,718	5,197	25,915
Payments in lieu of taxes	—	5,969	5,969
Engineering, general, and administrative	73,847	33,646	107,493
Total operating expenses	<u>152,318</u>	<u>74,649</u>	<u>226,967</u>
Income from operations before depreciation	186,038	97,471	283,509
Depreciation	<u>127,286</u>	<u>52,893</u>	<u>180,179</u>
Operating income	<u>58,752</u>	<u>44,578</u>	<u>103,330</u>
Regulatory accounting provisions:			
Change in reserves	(2,331)	(788)	(3,119)
Change in deferred credits – net	50,891	(73)	50,818
Total regulatory accounting provisions	<u>48,560</u>	<u>(861)</u>	<u>47,699</u>
Nonoperating income (expense):			
Debt service grants	15,907	3,030	18,937
Investment income	26,701	16,265	42,966
Interest expense	(177,746)	(85,949)	(263,695)
Total nonoperating expense	<u>(135,138)</u>	<u>(66,654)</u>	<u>(201,792)</u>
Net loss before capital grants	(27,826)	(22,937)	(50,763)
Capital grants	<u>5,563</u>	892	6,455
Decrease in net assets	(22,263)	(22,045)	(44,308)
Total net assets – beginning of year	<u>1,125,428</u>	<u>1,028,997</u>	<u>2,154,425</u>
Total net assets – end of year	\$ <u>1,103,165</u>	<u>1,006,952</u>	<u>2,110,117</u>

See accompanying independent auditors' report.