

**THE METROPOLITAN SEWER DISTRICT
OF GREATER CINCINNATI**

SINGLE AUDIT REPORTS

for the year ended December 31, 2004



**Auditor of State
Betty Montgomery**

The Honorable Board of County Commissioners
Metropolitan Sewer District of Greater Cincinnati
Cincinnati, Ohio

We have reviewed the *Independent Auditor's Report* of the Metropolitan Sewer District of Greater Cincinnati, Hamilton County, prepared by Foxx & Company, for the audit period January 1, 2004 through December 31, 2004. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The Metropolitan Sewer District of Greater Cincinnati is responsible for compliance with these laws and regulations.

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BETTY MONTGOMERY
Auditor of State

August 15, 2005

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THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI

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Foxx & Company
Certified Public Accountants

**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER
FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

The Honorable Board of County Commissioners
Hamilton County, Ohio

We have audited the financial statements of the Metropolitan Sewer District of Greater Cincinnati (MSD), as of and for the year ended December 31, 2004, and have issued our report thereon dated April 29, 2005. The financial statements present only the financial position of MSD and are not intended to present fairly the financial position of Hamilton County, and the results of its operations and cash flows of its proprietary fund types in conformity with generally accepted accounting principles. We conducted our audit 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.

Compliance

As part of obtaining reasonable assurance about whether MSD's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered MSD's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters

involving the internal control over financial reporting and its operation that we consider to be a material weakness.

This report is intended solely for the information and use of management, the Ohio Auditor of State and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Foxx & Company

Cincinnati, Ohio
April 29, 2005



Foxx & Company
Certified Public Accountants

**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH
MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE IN
ACCORDANCE WITH OMB CIRCULAR A-133**

The Honorable Board of County Commissioners
Hamilton County, Ohio

Compliance

We have audited the compliance of the the Metropolitan Sewer District of Greater Cincinnati (MSD), with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its major federal program for the year ended December 31, 2004. MSD's major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of MSD's management. Our responsibility is to express an opinion on MSD's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about MSD's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on MSD's compliance with those requirements.

In our opinion, MSD complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended December 31, 2004.

Internal Control Over Compliance

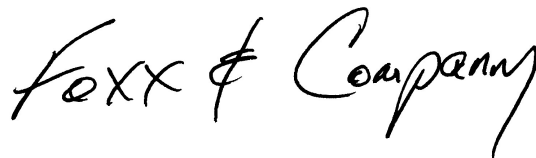
The management of MSD is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered MSD's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be a material weakness.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of MSD, as of and for the year ended December 31, 2004 and have issued our report thereon dated April 29, 2005. Our audit was performed for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit 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.

This report is intended solely for the information and use of management, the Ohio Auditor of State, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Fox & Company". The signature is written in black ink and is positioned to the right of the date and location information.

Cincinnati, Ohio
April 29, 2005

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

for the year ended December 31, 2004

Federal Grantor/Pass-Through Grantor/Program Title	<u>CFDA Number</u>	<u>Grant Number</u>	<u>Federal Disbursements</u>
U.S. Environmental Protection Agency			
<i>Pass-through programs from Ohio Environmental Protection Agency</i>			
Capitalization Grants for State Revolving Funds	66.458	CS391859-02	\$ 5,013,972
Capitalization Grants for State Revolving Funds	66.458	CS391859-03	1,776,821
Capitalization Grants for State Revolving Funds	66.458	CB29E	<u>453,634</u>
Total			<u>7,244,427</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u><u>\$ 7,244,427</u></u>

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

for the year ended December 31, 2004

NOTE A - SIGNIFICANT ACCOUNTING POLICIES

This schedule of expenditures of federal awards includes the federal grant/loan activity of MSD and is presented on an accrual basis of accounting in accordance with generally accepted accounting principles. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

for the year ended December 31, 2004

1. Summary of Auditors' Results

Type of financial statement opinion	Unqualified
Where there any material control weakness conditions reported at the financial statement level (GAGAS)?	No
Were there any reportable control weakness conditions reported at the financial statement level (GAGAS)?	No
Was there any other reported noncompliance at the financial statement level (GAGAS)?	No
Was there any material internal control weakness conditions reported for major federal programs?	No
Where there any other reported internal control weakness conditions reported for major federal programs?	No
Type of Major Programs' compliance opinion	Unqualified
Are there any reportable findings under § .510?	No
Major programs	Capitalization Grants for State Revolving Funds CFDA #66.458
Dollar threshold for Type A/B programs	Type A: Over \$300,000 Type B: All others
Low risk auditee?	Yes

2. Findings Related to the Financial Statements Required to be Reported in Accordance with GAGAS

None

3. Findings and Questioned Costs for Federal Awards

None

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI
SCHEDULE OF PRIOR AUDIT FINDINGS AND QUESTIONED COSTS

for the year ended December 31, 2004

There were no prior audit findings or questioned costs relative to federal awards for the audit of MSD for the year ended December 31, 2003.

**THE METROPOLITAN SEWER DISTRICT
OF GREATER CINCINNATI
CINCINNATI, OHIO**

FINANCIAL STATEMENTS

for the years ended December 31, 2004 and 2003

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI

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Foxx & Company
Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

The Honorable Board of County Commissioners
Hamilton County, Ohio

We have audited the accompanying financial statements of the Metropolitan Sewer District of Greater Cincinnati (MSD), an enterprise fund of the County of Hamilton, Ohio, as of and for the years ended December 31, 2004 and 2003 as listed in the table of contents. These financial statements are the responsibility of MSD's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Metropolitan Sewer District of Greater Cincinnati, at December 31, 2004 and 2003, and the changes in financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1, the financial statements for MSD present only the financial position of MSD, an enterprise fund of the County of Hamilton, Ohio; and are not intended to present fairly the financial position of Hamilton County, Ohio, and the change in financial position and cash flows of its proprietary fund types in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 29, 2005 on our consideration of MSD's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. 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 read in conjunction with this report in considering the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The Management's Discussion and Analysis on pages three to seven, is presented for purposes of additional analysis and is not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

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Cincinnati, Ohio
April 29, 2005

MANAGEMENT'S DISCUSSION AND ANALYSIS

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements are comprised of two components: 1) the financial statements and 2) notes to the financial statements that explain in more detail some of the information in the financial statements.

Required Financial Statements

The financial statements of the District report information about the District using accounting methods similar to those used by the private-sector companies. These statements provide both long-term and short-term information about the District's overall financial status.

The Statement of Net Assets presents information on all of the District's assets and liabilities, with the difference between the two reported as net assets. This statement provides information about the nature and the amounts of investments in resources (assets) and the obligations to District creditors (liabilities). It provides one way to measure the financial health of the District by providing the basis for evaluating the capital structure of the District and assessing the liquidity and financial flexibility of the District. However, there are several outside nonfinancial factors that need to be considered. Factors such as changing economic conditions, population and customer growth, and new or changed rules and regulations.

All of the current year's revenue and expenses are accounted for in the Statement of Revenues, Expenses, and Changes in Net Assets. This statement measures the success of the District's operations over the past year and can be used to determine whether the District has successfully recovered all its cost through its user fees.

The final required statement is the Statement of Cash Flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. This statement provides answers to such questions as where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period.

Financial Analysis of the District

As previously noted, net assets may serve over time as a useful indicator of an entity's financial position. In the case of the District, assets exceeded liabilities by \$452,148,000 at the close of the most recent fiscal year. As can be seen in Table A, on the next page, the largest portion of the District's net assets (67%) reflect its investment in capital assets (e.g., sewers, buildings, machinery and equipment), less any related debt used to acquire those assets that is still outstanding. These capital assets are used primarily in the collection and treatment of

wastewater throughout the District's service area. The related debt will be repaid with resources provided by system users through rates and fees.

Table A
Condensed Summary of Net Assets
(In Thousands)

	<u>2004</u>	Percentage Increase (Decrease) over 2003	<u>2003</u>	Percentage Increase (Decrease) over 2002	<u>2002</u>
Current and other assets	\$ 235,430	(13.6%)	\$ 272,560	33.8%	\$ 203,752
Capital assets	<u>748,727</u>	5.3%	<u>711,245</u>	4.4%	<u>681,288</u>
Total assets	<u>\$ 984,157</u>	0.0%	<u>\$ 983,805</u>	11.2%	<u>\$ 885,040</u>
Long-term debt	\$ 512,744	(2.1%)	\$ 523,916	20.1%	\$ 436,303
Other liabilities	<u>19,265</u>	(8.2%)	<u>20,991</u>	14.4%	<u>18,345</u>
Total liabilities	<u>\$ 532,009</u>	(2.4%)	<u>\$ 544,907</u>	19.9%	<u>\$ 454,648</u>
Invested in capital assets					
Net of related debt	\$ 302,580	19.9%	\$ 252,441	(13.4%)	\$ 291,490
Restricted	4,128	(26.1%)	5,589	22.4%	4,565
Unrestricted	<u>145,440</u>	(19.6%)	<u>180,868</u>	34.6%	<u>134,337</u>
Total net assets	<u>\$ 452,148</u>	3.0%	<u>\$ 438,898</u>	2.0%	<u>\$ 430,392</u>

Net assets increased \$13.250 million in 2004 and \$8.506 million in 2003. The increases are a combination of income before contributions and contributions in the form of connection fees, assessments, and developer contributions.

Table B
Condensed Summary of Revenues,
Expenses, and Changes in Net Assets
(In Thousands)

	<u>2004</u>	Percentage Increase (Decrease) over 2003	<u>2003</u>	Percentage Increase (Decrease) over 2002	<u>2002</u>
Operating revenues	\$ 145,291	13.0%	\$ 128,579	5.9%	\$ 121,447
Nonoperating revenues	<u>4,077</u>	(13.5%)	<u>4,711</u>	(36.8%)	<u>7,449</u>
Total revenues	<u>149,368</u>	12.1%	<u>133,290</u>	3.4%	<u>128,896</u>
Depreciation expense	27,434	(1.5%)	27,864	2.2%	27,271
Other operating expense	87,670	9.6%	79,994	6.0%	75,436
Nonoperating expense	<u>28,443</u>	18.6%	<u>23,986</u>	10.3%	<u>21,745</u>
Total expenses	<u>143,547</u>	8.9%	<u>131,844</u>	5.9%	<u>124,452</u>
Income before capital contributions	5,821	302.6%	1,446	(67.5%)	4,444
Capital contributions	<u>7,429</u>	5.2%	<u>7,060</u>	(15.1%)	<u>8,314</u>
Changes in net assets	13,250	55.7%	8,506	(33.3%)	12,758
Beginning net assets	<u>438,898</u>	2.0%	<u>430,392</u>	3.1%	<u>417,634</u>
Ending net assets	<u>\$ 452,148</u>	30%	<u>\$ 438,898</u>	2.0%	<u>\$ 430,392</u>

While the Summary of Net Assets (Table A) shows the change in financial position of net assets, the Summary of Revenues, Expenses, and Changes In Net Assets provides details as to the nature and source of these changes. Table B shows that during 2004 total revenues increased 12.1 percent or \$16 million and expenses increased 8.9 percent or \$11.7 million. During 2003 total revenues increased 3.4 percent or \$4.4 million and expenses increased 5.9 percent or \$7.4 million. The major factors which contributed to these results, include:

- Operating revenues reflect a 14 percent rate increase implemented January 9, 2004 and a 7 percent rate increase implemented January 9, 2003.
- Nonoperating revenues decreased in 2004 due to lower interest rates and less funds available for investment. Nonoperating revenues decreased in 2003 which reflects a decrease in the fair value of investments.

- Operating expenses increased 9.6 percent or \$7.7 million in 2004. The increase included a \$1.2 million fine paid under the Consent Decree and the Consent Decree mandated the implementation of Water-in-Basement program, \$2.4 million. Increases in fringe benefits costs, utility costs, and repair/upgrade costs were major factors in the remaining increase. Operating expenses increased 6.0 percent or \$4.6 million in 2003. Increases in sewer repairs, regulatory negotiations, process and system work, flow monitoring, and maintenance which were offset by a reduction in personnel were the main reasons for this increase.
- Nonoperating expense for 2004 increased 18.6 percent or \$4.5 million due to an increase in interest expense, \$880 thousand offset by an increase in fair value of investments, \$2.2 million and a loss on retirement of assets of \$5.8 million. The District replaced its belt filter press equipment and process with a centrifuge system. The loss on retirement of assets reflects the remaining net book value of the assets replaced. Nonoperating expenses for 2003 increased 10.3 percent or \$2.2 million due to a decrease in the fair value of investments.
- Capital contributions will fluctuate depending on building activity and assessment projects.

BUDGETARY HIGHLIGHTS

The District has an annual operating budget that is approved by the Hamilton County Board of County Commissioners. Capital budgets are approved on a project basis, however; annually a current year and a five year plan is presented to the Board. The 2004 expenses were 3.8 percent under the approved budget. About half of the savings was in reduced Water-In-Basement activity attributable to mild weather with reduced debt, due to refundings, and fewer equipment purchases making up the difference. The 2003 expenses were 2.5 percent under the approved budget. A third of the savings was in reduced debt service and the remainder was generated in most part by reduced personnel.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

As of December 31, the District's investment in capital assets amounted to \$749 million and \$711 million (net of accumulated depreciation) as shown in Table C for 2004 and 2003, respectively. In 2004, the District spent about \$69 million on capital improvement projects and received about \$7 million in capital contributions. In 2003, the District spent about \$50 million on capital improvement projects and received about \$7 million in capital contributions.

Sewer replacement and improvement projects were in about two-thirds of the program in both 2004 and 2003. The upgrade and replacement of the belt filter presses and process resulted in a reduction in processing systems of \$16.9 million and \$11.1 million in related accumulated depreciation during 2004.

Table C
Capital Assets
(In Thousands)

	<u>2004</u>	<u>Percentage Increase (Decrease) over 2003</u>	<u>2003</u>	<u>Percentage Increase (Decrease) over 2002</u>	<u>2002</u>
Land	\$ 4,977	0.0%	\$ 4,977	0.0%	\$ 4,977
Buildings & structures	715,309	5.8%	676,033	8.7%	621,759
Processing systems	241,429	(6.7%)	258,841	0.6%	257,417
Office & service equipment	31,972	3.3%	30,937	5.9%	29,221
Construction in progress	<u>195,564</u>	17.7%	<u>166,127</u>	(0.6%)	<u>167,080</u>
Subtotal	1,188,981	4.6%	1,136,915	5.2%	1,080,454
Less accumulated depreciation	<u>440,254</u>	3.4%	<u>425,670</u>	6.6%	<u>399,166</u>
Net capital assets	<u>\$ 748,727</u>	5.3%	<u>\$ 711,245</u>	4.4%	<u>\$ 681,288</u>

Debt Administration

The District finances its construction program primarily through the issuance of revenue bonds. In addition, the District will utilize low interest loan programs through the State of Ohio where appropriate.

The District's revenue bond ratings are:

Moody's Investors Services	Aa3
Standard & Poor's Corporation	AA

Additional information on the District's long-term debt can be found in Note 6 to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The service area of the District is best described as mature. The District is not in a growth situation but one in which the system, generally, is being upgraded and replaced to comply with increasing regulatory requirements. The operating budget for 2005 is \$151,469,440 which is \$6.6 million more than the 2004 budget. The increase of the 2005 operating budget reflects the input of the consent decrees. Rate increases of 12 and 14 percent were approved effective March 31, 2005 and January 9, 2004, respectively.

The capital plan was submitted and accepted for the years 2005 through 2009. The plan contemplates issuing an average of about \$91 million in debt each year to finance the capital improvement program. Each project must be individually approved before proceeding.

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI
STATEMENTS OF NET ASSETS
December 31, 2004 and 2003
(all amounts expressed in thousands)

ASSETS

	2004	2003
Current assets:		
Cash, cash equivalents and pooled investments held by the City of Cincinnati	\$ 14,164	\$ 13,187
Accounts receivable (Note 3)	26,099	20,782
Prepaid expenses and other	1,880	2,427
Total current assets	42,143	36,396
Noncurrent assets:		
Restricted assets:		
Cash, cash equivalents, and pooled investments held by the City of Cincinnati:		
Construction account	5,850	10,661
Amount to be transferred to surplus account	17,421	9,223
Held by trustee:		
Cash and cash equivalents (Note 2)	9,986	13,665
Investments - Held to maturity (Note 2)	154,655	196,065
Total restricted assets	187,912	229,614
Other assets:		
Unamortized financing costs	4,228	4,110
Other	1,147	2,440
Total other assets	5,375	6,550
Capital assets: (Note 5)		
Land	4,977	4,977
Building and structures	715,039	676,033
Processing systems	241,429	258,841
Office and service equipment	31,972	30,937
Construction in progress	195,564	166,127
	1,188,981	1,136,915
Less accumulated depreciation	(440,254)	(425,670)
Net capital assets	748,727	711,245
Total noncurrent assets	942,014	947,409
Total assets	\$ 984,157	\$ 983,805

The notes to the financial statements are an integral part of the financial statements.

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI
STATEMENTS OF NET ASSETS
December 31, 2004 and 2003
(all amounts expressed in thousands)

LIABILITIES

	2004	2003
Current liabilities:		
Payable from current assets:		
Current portion of long-term debt (Note 6)	\$ 21,828	\$ 18,600
Accounts payable	4,390	5,464
Accrued payroll expenses	1,501	1,213
Total current liabilities payable from current assets	27,719	25,277
Payable from restricted assets:		
Construction accounts payable	4,766	5,481
Accrued interest payable	2,262	2,942
Total current liabilities payable from restricted assets	7,028	8,423
Total current liabilities	34,747	33,700
Noncurrent liabilities:		
Accrued compensated absences (Note 6)	6,346	5,891
Long-term debt (Note 6)	490,916	505,316
Total noncurrent liabilities	497,262	511,207
Total liabilities	532,009	544,907
Net assets:		
Invested in capital assets, net of related debt	302,580	252,441
Restricted	4,128	5,589
Unrestricted	145,440	180,868
Total net assets	\$ 452,148	\$ 438,898

The notes to the financial statements are an integral part of the financial statements.

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI
STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN NET ASSETS
for the years ended December 31, 2004 and 2003
(all amounts expressed in thousands)

	<u>2004</u>	<u>2003</u>
Operating revenues:		
Sewerage service charges	\$ 125,992	\$ 111,291
Sewer surcharges	16,858	14,544
All other revenues	<u>2,441</u>	<u>2,744</u>
Total operating revenues	<u>145,291</u>	<u>128,579</u>
Operating expenses:		
Personnel services	36,871	33,599
Purchased services	25,174	23,669
Utilities, fuel and supplies	17,393	15,824
Depreciation	27,434	27,864
Other expenses	<u>8,232</u>	<u>6,902</u>
Total operating expenses	<u>115,104</u>	<u>107,858</u>
Operating income	<u>30,187</u>	<u>20,721</u>
Nonoperating revenues (expenses):		
Interest income	4,077	4,649
Change in fair value of investments	135	(2,080)
Interest expense	(22,785)	(21,906)
Retirement of fixed assets	<u>(5,793)</u>	<u>62</u>
Total nonoperating revenues (expenses)	<u>(24,366)</u>	<u>(19,275)</u>
Income from operations	5,821	1,446
Capital contributions	<u>7,429</u>	<u>7,060</u>
Change in net assets	13,250	8,506
Total net assets, beginning	<u>438,898</u>	<u>430,392</u>
Total net assets, ending	<u>\$ 452,148</u>	<u>\$ 438,898</u>

The notes to the financial statements are an integral part of the financial statements.

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI
STATEMENTS OF CASH FLOWS
for the years ended December 31, 2004 and 2003
(all amounts expressed in thousands)

	<u>2004</u>	<u>2003</u>
Cash Flows from Operating Activities		
Cash received from customers	\$ 137,533	\$ 126,110
Cash payments for goods and services	(51,679)	(44,968)
Cash payments for personnel costs	(36,127)	(33,910)
Other operating revenues	2,558	3,024
Net Cash Provided by Operating Activities	<u>52,285</u>	<u>50,256</u>
Cash Flows from Capital and Related Financing Activities		
Principal and interest payments on long-term debt	(86,583)	(175,254)
Acquisition and construction of capital assets	(62,334)	(51,837)
Loan proceeds	7,245	906
Revenue bond proceeds	46,385	238,595
Revenue bond issuance costs	(1,683)	(2,253)
Tap-in fees	4,696	4,623
Gain/loss from sale of property, plant and equipment	(5,793)	62
Net Cash (Used) by Capital and Related Financing Activities	<u>(98,067)</u>	<u>14,842</u>
Cash Flows from Investing Activities		
Purchase of government securities	(178,977)	(280,971)
Maturity or redemption of government securities	219,971	195,427
Net increase in fair value of pooled cash and investments held by City of Cincinnati	572	(356)
Interest earned on investments	4,901	4,612
Net Cash Provided (Used) by Investing Activities	<u>46,467</u>	<u>(81,288)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	685	(16,190)
Cash and Cash Equivalents at January 1	<u>46,736</u>	<u>62,926</u>
Cash and Cash Equivalents at December 31	<u>\$ 47,421</u>	<u>\$ 46,736</u>
Reconciliation of Operating Income to Net Cash Provided by Operating Activities:		
Income from operations	\$ 30,188	\$ 20,721
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	27,434	27,864
Change in assets and liabilities:		
Net change in customer accounts receivable	(5,317)	275
Net change in other assets	311	167
Net change in operating accounts payable	(1,074)	1,540
Net change in accrued payroll and related expenses	743	(311)
Net Cash Provided by Operating Activities	<u>\$ 52,285</u>	<u>\$ 50,256</u>
Non-cash Transactions:		
Structures donated as contributed capital in aid of construction	<u>\$ 1,819</u>	<u>\$ 1,972</u>

The notes to the financial statements are an integral part of the financial statements.

THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI
NOTES TO THE FINANCIAL STATEMENTS
for the years ended December 31, 2004 and 2003

NOTE 1 - ACCOUNTING POLICIES

A summary of the significant accounting policies applied in the accompanying financial statements follows:

Organization

The Metropolitan Sewer District of Greater Cincinnati (MSD), an enterprise fund of the County of Hamilton, Ohio, collects and treats industrial and residential wastewater for municipalities and unincorporated areas of Hamilton County. MSD was formed on April 10, 1968, pursuant to resolutions of the Board of County Commissioners of Hamilton County and Ordinances of the City of Cincinnati, providing for a consolidation of the City Sewer Department and the County Sewer District. Under a contract with the City of Cincinnati, the Board designated the City as its agent for the maintenance and operation of MSD. The annual budget, prepared on the cash basis of accounting, is approved by the Board and administered by the City. Budgetary control is exercised at the divisional level, and between personnel and all other costs. The County issues a separate Comprehensive Annual Financial Report which includes MSD as a separate enterprise fund of the County.

Basis of Accounting

The accompanying financial statements were prepared on the accrual basis of accounting, whereby revenues and expenses are recognized in the period earned or incurred.

Enterprise Fund Activity Accounting and Financial Reporting

In accordance with GASB Statement No. 34, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Government, the District applies all GASB pronouncements and only FASB Statements and Interpretations, Accounting Principles Board of Opinions and Accounting Research Bulletins issued on or before November 30, 1989, unless they conflict with GASB pronouncements.

Use of Estimates

The preparation of financial statements in conformity with 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 expenses during the reporting period. Actual results could differ from those estimates.

Statement of Cash Flows

For purposes of the Statements of Cash Flows, all highly liquid investments with a maturity of three months or less when purchased are considered to be cash equivalents. Pooled cash and investments held by the City of Cincinnati are considered cash equivalents by MSD.

Investments

MSD is required by Ohio law to invest in only United States obligations; federal agency securities; Ohio bonds and other obligations or such obligations of political subdivisions of the state, provided that the subdivisions are located within Hamilton County; time certificates of deposit or deposit accounts in an eligible institution; and no load money market mutual funds consisting only of investments mentioned above. Investments are required to mature within five years from the date of settlement, unless the investment is matched to a specific obligation or debt of MSD.

Investment securities are stated at fair value in accordance with GASB Statement No. 31.

Inventory

Supplies and materials are stated at the lower cost or market on a first-in, first-out (FIFO) basis.

Capital Assets

Capital assets are stated at historical cost for assets acquired after MSD's inception in 1968. Assets which were acquired prior to 1968 and not identifiable with specific historical costs are not included in the capital assets balance. Assets acquired by MSD through contributions, such as contributions from land developers and federal and state grants, are capitalized and recorded in the plant records at the contributors' reported cost. Construction costs include interest capitalized on debt during the period of construction and the cost of in-force labor.

Depreciation expense is computed on the straight-line method over the estimated useful lives of the respective assets. The estimated lives are as follows:

Building and structures	40 years
Processing systems	25 years
Office and service equipment	5-15 years

Any gain or loss arising from the disposal of capital assets has been credited or charged to income.

Unamortized Financing Costs

The unamortized financing costs include insurance, consulting and attorney fees incurred in connection with the revenue bond obligations. These amounts are being amortized on the straight-line method over the lives of the revenue bonds. Bond premiums and discounts are being amortized on the interest method over the lives of the revenue bonds.

Pension Plans

Employees participate in either the City of Cincinnati's Retirement System or the Public Employees Retirement System administered by the State of Ohio. Pension costs reflect a percentage of employees' gross pay, as defined by the terms of pension plans in which employees participate. MSD's policy is to fund pension costs accrued.

Compensated Absences

Compensated absences are accrued in accordance with GASB Statement No. 16. Components of the liability include accrued vacation time, sick leave, compensatory time and other related payments.

Net Assets

Net assets are the difference between assets and liabilities. Net assets invested in capital asset, net of related debt are capital assets less accumulated depreciation and any outstanding long-term debt related to the acquisition, construction or improvement of those assets. Net assets are reported as restricted when there are legal limitations that are imposed on their use by county legislation or external restrictions by other governments, creditors or grantors.

Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the primary activity of the proprietary fund. For the District, these revenues are charges for services for wastewater treatment. Operating expenses are necessary costs incurred to provide the service that is the primary activity of the fund.

NOTE 2 - DEPOSITS AND INVESTMENTS

The following information classifies deposits and investments by category of risk as defined in GASB Statement No. 3, "Deposits with Financial Institutions, Investments and Repurchase Agreements"

Deposits: At December 31, 2004 and 2003, the carrying amount of MSD's deposits held by the City of Cincinnati total \$37,434,000 and \$33,071,000 respectively. Amounts held by the City of Cincinnati are invested on MSD's behalf in accordance with the Cincinnati Municipal Code. Amounts held by the City are collateralized as part of the City's cash and investment balances.

Investments: Funds held by trustees are eligible investments as defined by the Trust Agreement and are in the name of the trustee for the benefit of MSD.

Investments made by MSD are summarized below. Trustee account investments are categorized according to credit risk into the following categories: (1) insured or registered, or securities held by MSD's or its agent (bank trust department) in the MSD's name; or (2) uninsured and unregistered, with securities held by the counterparty's trust department or agent in the MSD's name; or (3) uninsured, unregistered securities held by the counterparty, or its trust department or agent but not in MSD's name. Money market funds are unclassified investments since they are not evidenced by securities that exist in physical or book entry form.

(all amounts in thousands)

<u>December 31, 2004</u>	<u>Category</u>			<u>Carrying Amount</u>	<u>Fair Value</u>
	<u>1</u>	<u>2</u>	<u>3</u>		
U.S. Government Securities	\$ 154,655	\$ -	\$ -	\$ 154,655	\$ 154,655
Money Market Funds		-	-	9,986	9,986
Total	<u>\$ 154,655</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 164,641</u>	<u>\$ 164,641</u>

(all amounts in thousands)

<u>December 31, 2003</u>	<u>Category</u>			<u>Carrying Amount</u>	<u>Fair Value</u>
	<u>1</u>	<u>2</u>	<u>3</u>		
U.S. Government Securities	\$ 196,065	\$ -	\$ -	\$ 196,065	\$ 196,065
Money Market Funds		-	-	13,665	13,665
Total	<u>\$ 196,065</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 209,730</u>	<u>\$ 209,730</u>

The classification of cash and cash equivalents and investments on the financial statements is based on criteria set forth in GASB Statement No. 9. A reconciliation between the classifications of cash and investments on the financial statements and the classification per GASB Statement No. 3 is as follows:

	(all amounts in thousands)	
<u>December 31, 2004</u>	<u>Cash and Cash Equivalents</u>	<u>Investments</u>
GASB Statement No. 9	\$ 47,420	\$ 154,655
Money Market Funds	(9,986)	9,986
GASB Statement No. 3	<u>\$ 37,434</u>	<u>\$ 164,641</u>

	(all amounts in thousands)	
<u>December 31, 2003</u>	<u>Cash and Cash Equivalents</u>	<u>Investments</u>
GASB Statement No. 9	\$ 46,736	\$ 196,065
Money Market Funds	(13,665)	13,665
GASB Statement No. 3	<u>\$ 33,071</u>	<u>\$ 209,730</u>

NOTE 3 - ACCOUNTS RECEIVABLE

Accounts receivable consist of the following:

	(all amounts in thousands)	
	<u>2004</u>	<u>2003</u>
Sewerage charges and surcharges:		
Unbilled amount	\$ 13,279	\$ 11,940
Billed amount	14,802	10,328
Less allowance for doubtful accounts	(2,500)	(2,000)
Other	518	514
Total	<u>\$ 26,099</u>	<u>\$ 20,782</u>

NOTE 4 - RESTRICTED ASSETS

Land acquired for MSD's use is titled to either the City of Cincinnati or Hamilton County. The cost of this land has been recorded on the books of MSD since it has the full benefit of the land as an economical resource.

In August 1985, the Federal District Court entered a consent order in an action with MSD and others. In complying with the consent order, MSD was required to maintain amounts on deposit in an environmental security account. The balance of this account, which is included in other assets, was \$1,177,000 at December 31, 2003. The new Global Consent Decree (See Note 9)

specified that this account be part of the funding for the Water-In-Basement program and was liquidated in 2004.

The Trust Agreement for the Series A Revenue Bonds (see Long-Term Debt Note) requires the establishment of certain trust accounts including a Bond Account, Bond Reserve Account, Replacement and Improvement Account, and a Surplus Account to be held by the Trustee. The Bond Account will be used to accumulate periodic principal and interest payments. The Bond Reserve Account will be funded in an amount equal to the highest annual future debt service requirement. The Replacement and Improvement Account is to be maintained with a balance of \$5,000,000. The Surplus Account is available to be used for any other Sewer System purpose. The Trust Agreement also requires the creation of a Construction Account to be held by the City to pay for project costs. At December 31, 2004 and 2003 the following balances (at fair value) were maintained in the trust accounts:

	(all amounts in thousands)	
	<u>2004</u>	<u>2003</u>
Held by trustee:		
Reserve	\$ 45,795	\$ 42,350
Replacement and improvement	4,894	4,940
Bond retirement	4,129	4,556
Surplus	<u>109,824</u>	<u>157,884</u>
Total	<u>\$ 164,642</u>	<u>\$ 209,730</u>

NOTE 5 - CAPITAL ASSETS

The following summarizes the changes to capital assets during 2004:

	(all amounts in thousands)			
<u>December 31, 2004</u>	<u>Balance at January 1, 2004</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance at December 31, 2004</u>
Capital assets not being depreciated:				
Land	\$ 4,977	\$ -	\$ -	\$ 4,977
Construction in progress	166,127	66,931	(37,494)	195,564
	<u>171,104</u>	<u>66,931</u>	<u>(37,494)</u>	<u>200,541</u>
Capital assets being depreciated:				
Buildings and structures	676,033	39,381	(375)	715,039
Processing systems	258,841	82	(17,494)	241,429
Office and service equipment	30,937	1,656	(621)	31,972
	<u>965,811</u>	<u>41,119</u>	<u>(18,490)</u>	<u>988,440</u>
Total Capital Assets	1,136,915	108,050	(55,984)	1,188,981
Less accumulated depreciation	<u>425,670</u>	<u>26,610</u>	<u>(12,026)</u>	<u>440,254</u>
Net capital assets	<u>\$ 711,245</u>	<u>\$ 81,440</u>	<u>\$ (43,958)</u>	<u>\$ 748,727</u>

The following summarizes the changes to capital assets during 2003:

	(all amounts in thousands)			
<u>December 31, 2003</u>	<u>Balance at January 1, 2003</u>	<u>Increase</u>	<u>Decrease</u>	<u>Balance at December 31, 2003</u>
Capital assets not being depreciated:				
Land	\$ 4,977	\$ -	\$ -	\$ 4,977
Construction in progress	167,080	52,786	(53,739)	166,127
	<u>172,057</u>	<u>52,786</u>	<u>(53,739)</u>	<u>171,104</u>
Capital assets being depreciated:				
Buildings and structures	621,759	54,274	-	676,033
Processing systems	257,417	2,028	(604)	258,841
Office and service equipment	29,221	2,298	(582)	30,937
	<u>908,397</u>	<u>58,600</u>	<u>(1,186)</u>	<u>965,811</u>
Total Capital Assets	1,080,454	111,386	(54,925)	1,136,915
Less accumulated depreciation	<u>399,166</u>	<u>27,084</u>	<u>(580)</u>	<u>425,670</u>
Net capital assets	<u>\$ 681,288</u>	<u>\$ 84,302</u>	<u>\$ (54,345)</u>	<u>\$ 711,245</u>

NOTE 6 - LONG-TERM DEBT

Long-term debt consisted of the following:

(all amounts in thousands except percents)

	<u>Principal Issue</u>	<u>Interest Rate %</u>	<u>Year of Maturity</u>	<u>2004</u>	<u>2003</u>
Revenue Bonds					
2004 (a)	\$ 46,385	2.00-5.00	2017	\$ 46,385	-
2003 (b)	215,575	1.50-5.25	2028	213,205	\$ 215,575
2001 (c)	76,000	2.30-5.25	2026	60,510	65,980
2000 (d)	40,085	4.50-5.75	2025	30,140	37,490
1997 (e)	105,245	3.85-5.13	2017	72,720	83,280
1995 (f)	85,800	3.70-6.05	2017	4,680	43,305
1993 (g)	171,790	2.45-5.60	2016	45,345	45,345
				<u>472,985</u>	<u>490,975</u>
Ohio Water Development Authority Contracts					
	41,830	2.00-7.49	2019	1,062	1,161
Ohio Water and Sewer Rotary Commission					
	-	-	-	50	50
Ohio Public Works Commission					
	-	3.54-4.80	2017	4,398	4,199
Water Pollution Control Loan Fund					
	-	0.00-3.00	2018	18,340	12,325
Total obligations				\$ 496,835	\$ 508,710
Bond discounts				(631)	(1,157)
Bond premiums				24,916	23,057
Deferred loss on defeasance				(8,376)	(6,694)
Current maturities				(21,828)	(18,600)
Long-term portion				<u>\$ 490,916</u>	<u>\$ 505,316</u>

Principal and interest payments on long-term debt for the next five years and thereafter are as follows:

(all amounts in thousands)

Year	Revenue Bonds		OWDA		OPWC		WPCLF*	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2005	20,285	23,275	103	38	267	85	1,173	915
2006	21,250	22,309	106	35	272	80	1,361	1,005
2007	22,175	21,380	110	31	277	75	1,414	952
2008	23,170	20,389	114	27	283	69	1,470	896
2009	24,255	19,303	118	23	288	64	1,528	839
2010-2014	140,700	77,308	511	49	1,514	230	8,417	3,243
2015-2019	120,550	39,846	-	-	1,120	86	6,807	1,695
2020-2024	54,435	19,851	-	-	377	13	5,420	548
2025-2029	46,165	5,490	-	-	-	-	273	5
Total	<u>\$ 472,985</u>	<u>\$ 249,151</u>	<u>\$ 1,062</u>	<u>\$ 203</u>	<u>\$ 4,398</u>	<u>\$ 702</u>	<u>\$ 27,863</u>	<u>\$ 10,098</u>

This amount represents the total amount of the loans, some of which have not been fully drawdown or finalized.

Bond discount, premium, loss on defeasance activity for the year:

<u>December 31, 2004</u>	<u>Beginning Balance</u>	<u>Amortized</u>	<u>Refunded</u>	<u>Issued</u>	<u>Ending Balance</u>
Bond discount	\$ (1,157)	\$ 191	\$ 335	\$ -	\$ (631)
Bond premium	23,057	(1,807)		3,666	24,916
Loss on defeasance	(6,694)	1,333	(3,015)	-	(8,376)
Total	<u>\$ 15,206</u>	<u>\$ (283)</u>	<u>\$ (2,680)</u>	<u>\$ 3,666</u>	<u>\$ 15,909</u>

<u>December 31, 2003</u>	<u>Beginning Balance</u>	<u>Amortized</u>	<u>Refunded</u>	<u>Issued</u>	<u>Ending Balance</u>
Bond discount	\$ (4,220)	\$ 322	\$ 2,741	\$ -	\$ (1,157)
Bond premium	1,685	(824)		22,196	23,057
Loss on defeasance	-	460	(7,154)	-	(6,694)
Total	<u>\$ (2,535)</u>	<u>\$ (42)</u>	<u>\$ (4,413)</u>	<u>\$ 22,196</u>	<u>\$ 15,206</u>

Long-term debt activity for the year:

<u>December 31, 2004</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Revenue Bonds	\$ 490,975	\$ 46,385	\$ 64,375	\$ 472,985
Ohio Water Development Authority	1,161	-	99	1,062
Ohio Water and Sewer Rotary Commission	50	-	-	50
Ohio Public Works Commission	4,199	453	254	4,398
Water Pollution Control Loan Fund	12,325	6,790	775	18,340
Total	<u>\$ 508,710</u>	<u>\$ 53,628</u>	<u>\$ 65,503</u>	<u>\$ 496,835</u>

Long-term debt activity for the year:

<u>December 31, 2003</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Revenue Bonds	\$ 420,885	\$ 215,575	\$ 145,485	\$ 490,975
Ohio Water Development Authority	1,335	-	174	1,161
Ohio Water and Sewer Rotary Commission	50	-	-	50
Ohio Public Works Commission	4,440	-	241	4,199
Water Pollution Control Loan Fund	12,128	906	709	12,325
Total	<u>\$ 438,838</u>	<u>\$ 216,481</u>	<u>\$ 146,609</u>	<u>\$ 508,710</u>

Revenue Bonds

- a) Effective October 5, 2004, MSD issued \$46,385,000 Series A, Sewer System Refunding Revenue Bonds dated September 1, 2004. The proceeds from the 2004 bonds were used to defease portions of the 1995, 1997 and 2000 revenue bonds and pay for the cost of issuance. The 2004 bonds are special obligations of the District, payable solely from the net revenues of the District and were issued on parity with the 1993, 1995, 1997, 2000, 2001, and 2003 Series A and 2003 Series B bonds, secured equally and ratably under the Trust Agreement.

A portion of the proceeds was used to purchase U.S. Government Securities which were deposited in an irrevocable trust with an escrow agent to provide for all future debt service to refund \$34,215,000 of outstanding 1995 Series A Bonds, \$6,280,000 of outstanding 1997 Series A Bonds, and \$6,400,000 of outstanding 2000 Series A Bonds. As a result, these bonds are considered defeased and the liability for those bonds removed from the balance sheet.

- b) Although the advance refunding resulted in the recognition of an accounting loss of \$3,163,000 to be amortized over future periods in accordance with GASB 23, the District in effect reduced its aggregate debt service payments by \$3,850,000 and obtained an economic gain (difference between the present values of the old and new debt service payments) of \$3,001,000.

Effective July 9, 2003 and September 4, 2003, MSD issued \$160,065,000 Series A, dated June 1, 2003 and \$55,510,000 Series B, dated September 1, 2003, respectively, County of Hamilton, Ohio Sewer System Improvement and Refunding Revenue Bonds. The proceeds from the 2003 bonds were used to permanently fund certain previous capital expenditures, defease portions of the 1993 and 1995 Series A bond issues, provide funds for new projects, fund the new bond reserve requirement and pay for the cost of issuance. The 2003 bonds are special obligations of the District, payable solely from the net revenues of the District and were issued on parity with the 1993, 1995, 1997, 2000, and 2001 Series A bonds, secured equally and ratably under the Trust Agreement.

A portion of the proceeds was used to purchase U.S. Government Securities which were deposited in an irrevocable trust with an escrow agent to provide for all future debt service to refund \$111,430,000 of outstanding 1993 Series A Bonds and \$17,125,000 of outstanding 1995 Series A Bonds. As a result, these bonds are considered defeased and the liability for those bonds removed from the balance sheet.

- c) Although the advance refunding resulted in the recognition of an accounting loss of \$7,154,000 to be amortized over future periods in accordance with GASB 23, the District in effect reduced its aggregate debt service payments by \$19,250,000 and obtained an

economic gain (difference between the present values of the old and new debt service payments) of \$14,719,000.

Effective November 14, 2001, MSD issued \$76,000,000 County of Hamilton, Ohio 2001 Series A Sewer System Improvement and Refunding Revenue bonds dated November 1, 2001. The proceeds from the 2001 bonds were used to permanently fund certain previous capital expenditures, defease a portion of the 1991 Series A bond issue, fund the new bond reserve requirement and pay for the cost of issuance. The 2001 bonds are special obligations of the District, payable solely from the net revenues of the District and were issued on a parity with the 1993, 1995, 1997 and 2000 Series A bonds, secured equally and ratably under the Trust Agreement.

- d) Effective June 29, 2000, MSD issued \$40,085,000 County of Hamilton, Ohio 2000 Series A Sewer System Improvement Revenue bonds dated June 1, 2000. The proceeds from the 2000 bonds were used to permanently fund certain previous capital expenditures, fund the new bond reserve requirement and pay the cost of issuance. The 2000 bonds are special obligations of the District, payable solely from the net revenues of the District and were issued on a parity with the 1993, 1995 and 1997 Series A bonds, secured equally and ratably under the Trust Agreement.
- e) Effective October 22, 1997, MSD issued \$105,245,000 County of Hamilton, Ohio 1997 Series A Sewer System Improvement Revenue bonds dated October 1, 1997. The proceeds from the 1997 bonds were used to permanently fund certain previous expenditures, fund the new bond reserve requirement and pay the cost of issuance. The 1997 bonds are special obligations of the District, payable solely from the net revenues of the District and were issued on a parity with the 1993, and 1995 Series A bonds, secured equally and ratably under the Trust Agreement.
- f) Effective August 31, 1995, MSD issued \$85,800,000 County of Hamilton, Ohio 1995 Series A Sewer System Improvement and Refunding Revenue bonds dated August 15, 1995. The proceeds from the 1995 bonds were used to permanently fund certain previous capital expenditures, provide funds for new projects, defease a portion of the 1986 and 1991 Series A bond issues, fund the new bond reserve requirement and pay the cost of issuance. The 1995 bonds are special obligations of the District payable solely from the net revenues of the District and were issued on a parity with the 1993 Series A bonds, secured equally and ratably under the Trust Agreement.
- g) Effective May 4, 1993, MSD issued \$171,790,000 County of Hamilton, Ohio 1993 Series A Sewer System Improvement and Refunding Revenue bonds dated April 15, 1993. The proceeds from the 1993 Bonds were used to permanently fund certain previous capital expenditures, provide funds for new projects, defease a portion of the 1986 and 1991 Series A bond issues, fund the new bond reserve requirement, and pay the cost of issuance. The

1993 bonds are special obligations of the District payable solely from the net revenues of the District, secured equally and ratably under the Trust Agreement.

The 2004, 2003, 2001, 2000, 1997, 1995, and 1993 Bonds may be redeemed prior to their maturities in accordance with provisions of the bond resolutions. The redemption process for the bonds include declining premiums up to 2 percent of principal.

At December 31, 2004 and 2003 the amount of defeased debt outstanding was \$64,020,000 and \$17,125,000, respectively.

Maturities for bonds over the next five years and thereafter are shown below:

(all amounts in thousands)

	<u>2004</u> <u>Bonds</u>	<u>2003</u> <u>Bonds</u>	<u>2001</u> <u>Bonds</u>	<u>2000</u> <u>Bonds</u>	<u>1997</u> <u>Bonds</u>	<u>1995</u> <u>Bonds</u>	<u>1993</u> <u>Bonds</u>
2005	125	4,270	5,720	995	4,495	4,680	-
2006	2,125	1,420	1,480	1,040	4,720	-	10,465
2007	2,260	1,340	1,525	1,095	4,930	-	11,025
2008	2,200	1,475	1,585	1,145	5,150	-	11,615
2009	2,260	1,500	1,660	1,205	5,390	-	12,240
2010-2014	8,945	93,190	9,455	3,995	25,115	-	-
2015-2019	28,470	50,530	12,845	5,785	22,920	-	-
2020-2024	-	24,550	17,845	12,040	-	-	-
2025-2029	-	34,930	8,395	2,840	-	-	-
	<u>\$ 46,385</u>	<u>\$213,205</u>	<u>\$ 60,510</u>	<u>\$ 30,140</u>	<u>\$ 72,720</u>	<u>\$ 4,680</u>	<u>\$45,345</u>

Under the terms of the amended revenue bond trust indenture, MSD has agreed to certain covenants, among other things, to restrict additional borrowing, maintain rates sufficient to meet debt service requirements, and maintain specified fund balances under trust agreements.

The Revenue bond issues as discussed above contain covenants which require the MSD to maintain a level of debt service coverage. The following calculation reflects MSD's debt service coverage.

(all amounts in thousands except percents)

	<u>2004</u>	<u>2003</u>
Revenues:		
Total operating revenues	\$ 145,291	\$ 128,579
Interest income	4,077	4,649
Capitalized interest income	376	537
Tap-in/connection fees	<u>4,696</u>	<u>4,623</u>
Total pledged revenues	154,440	138,388
Total operating and maintenance expenses less depreciation and amortization	(87,670)	(79,995)
Half of pledged revenues transferred to surplus account	<u>8,710</u>	<u>4,612</u>
Net income available for debt service (a)	<u>\$ 75,480</u>	<u>\$ 63,005</u>
Principal and interest requirements on revenue bonds (b)	<u>\$ 42,011</u>	<u>\$ 41,165</u>
Principal and interest requirements on all obligations (c)	<u>\$ 43,857</u>	<u>\$ 43,001</u>
Debt service coverage:		
Revenue Bonds (a) divided (b)	<u>180%</u>	<u>153%</u>
All obligations (a) divided (c)	<u>172%</u>	<u>147%</u>
Maximum debt service coverage required on revenue bonds	<u>125%</u>	<u>125%</u>

Ohio Water Development Authority Contracts

All contracts between the Ohio Water Development Authority (OWDA) and the Metropolitan Sewer District require MSD to prescribe and charge such rates for sewer usage which are sufficient (after expenses of operation and maintenance) to pay principal and interest on OWDA contracts. The principal is repayable in equal semi-annual installments to maturity.

Ohio Water and Sewer Rotary Commission

Advances from Ohio Water and Sewer Rotary Commission represent tap-in fees and acreage assessments to be forwarded to the Commission upon collection from customers. Such advances do not bear interest unless they are determined to be in default.

Ohio Public Works Commission

The MSD has entered into agreements with the Ohio Public Works Commission (OPWC) for financing of certain qualified capital projects. As the projects progress the commitments are

drawn down as funds are paid by OPWC directly to the contractors. The principal is repayable in semi-annual installments to the date of maturity for each project.

Water Pollution Control Loan Fund

The MSD has received low interest loan commitments from the Ohio Water Pollution Control Loan fund for certain qualified projects. As the projects progress the commitments are drawn down. The principal is repayable in semi-annual installments to the date of maturity for each project.

Interest on Long-Term Obligations

The following interest costs were incurred and expensed or capitalized as part of the cost of MSD's additions to capital assets.

	(all amounts in thousands)	
	<u>2004</u>	<u>2003</u>
Interest incurred	\$ 24,918	\$ 24,302
Less interest capitalization	<u>(2,133)</u>	<u>(2,396)</u>
Interest expense	<u>\$ 22,785</u>	<u>\$ 21,906</u>

Compensated Absences

Compensated absences consist of vacation time, sick pay and compensatory time. The following is a summary of activity for 2004 and 2003.

	(all amounts in thousands)			
	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
2004	\$ 5,891	\$ 4,471	\$ 4,016	\$ 6,346
2003	\$ 6,276	\$ 4,173	\$ 4,558	\$ 5,891

NOTE 7 - PENSION AND RETIREMENT

City of Cincinnati Retirement System

The majority of MSD full-time employees participate in the Retirement System of the City of Cincinnati (CRS). CRS is a cost-sharing, multiple-employer, defined benefit, public employee retirement system. The plan provides retirement, disability and death benefits to plan members and beneficiaries. CRS also provides health care benefits to vested retirees. Benefits provided under the plan are established by the Cincinnati Municipal Code. CRS issues a separate, publicly available financial report that includes financial statements and required supplementary

information. That report may be obtained from the City of Cincinnati Retirement System, 801 Plum Street, Cincinnati, Ohio 45202 or by calling (513) 352-3227.

The Cincinnati Municipal Code provides statutory authority for employee and employer contribution rates. For 2004 and 2003, the required, actuarially determined contribution rates were 11 and 7 percent for MSD and 7 percent for employees. MSD's contributions to CRS for the years ending December 31, 2004, 2003 and 2002 were \$2,908,000 and \$1,898,000, \$1,963,000, respectively, equal to the required contribution for each year.

Public Employees' Retirement System

A limited number of MSD employees participate in the Public Employee' Retirement System administrated by the State of Ohio. PERS is not material to the financial statements of MSD and additional disclosures concerning PERS, including other post-employment benefit information, can be found in the plan's annual financial statements. Interested parties may obtain a copy by written request to 277 East Town Street, Columbus, Ohio 43215-4642 or by calling (614) 466-2085.

Other Postemployment Benefit Information

CRS provides hospital and surgical insurance to retired members who have earned fifteen years credited service at the time of termination or terminate after age sixty with five years credited service. Those who are receiving survivor benefits of eligible members are entitled to have their hospital and surgical insurance premiums paid by the CRS. When benefits would be reduced by reason of the retired member's eligibility for hospital and medical benefits under federal social security laws, CRS will pay whatever additional fees are required for the Federal medical coverage.

The health care coverage provided by the CRS is advance-funded on an actuarial determined basis as a portion of the employer contribution requirement to the System. The Cincinnati Municipal Code provides authority for employer contributions.

The actuarial assumptions used for the December 31, 2003, valuation of unfunded liabilities (latest information available) included an assumption recognizing medical benefits at current premium costs with projected increases of 15 percent per annum. The cost of coverage is recognized as an expense as claims are paid. CRS has 5,051 active contributing participants of which 549 are MSD employees. For 2003, MSD's contribution was 16 percent of the total employers' contribution.

NOTE 8 - RELATED PARTY TRANSACTIONS

Cincinnati Water Works provides billing and collection services on customers' accounts for MSD. Fees for these services for 2004 and 2003 were \$4,600,000 and \$4,303,000 respectively. Fees are also paid to other municipalities and villages within Hamilton County for collection of sewerage bills.

The City of Cincinnati provides "overhead" services to MSD, such as check disbursement, investment and legal services, etc. The fees for these services for 2004 and 2003 were \$1,896,000 and \$2,203,000 respectively. In addition, the City's Municipal Garage provides gasoline and repairs vehicles for MSD. Fees for these services were \$1,257,000 and \$1,101,000 for 2004 and 2003, respectively.

NOTE 9 - COMMITMENTS AND CONTINGENCIES

The City of Cincinnati and the Board of County Commissioners of Hamilton County, Ohio are parties to an Interim Partial Consent Decree on Sanitary Sewer Overflows, which was lodged on February 15, 2002, with the U.S. District Court for the Southern District of Ohio, Western Division. This Decree provides for, among other things, the scheduled elimination of sixteen "highly active" sanitary sewer overflows. On December 4, 2003, a Global Consent Decree was lodged with the U.S. District Court for the Southern District of Ohio, Western Division. This decree focuses on combined sewer overflows, the implementation of the Sanitary Sewer Overflow Correction plan established in the Interim Partial Consent Decree, and other wet weather issues. The court approved the decrees on June 9, 2004. It is estimated that the program would cost about \$1.5 billion through 2022. The consent decree documents are posted on the MSD web site, msdgc.org, under consent decree.

As part of MSD's capital improvement program, MSD has entered into a number of contracts for construction, design, and other services. Commitments under these contracts aggregate approximately \$52 million as of December 31, 2004.

NOTE 10 - RISK MANAGEMENT

MSD is part of the City of Cincinnati Risk Management Program. The City purchases commercial insurance to cover losses due to: theft of, damage to, or destruction of assets and purchases general liability insurance for specific operations and professional liability insurance for certain operations. All other risks of loss are self-insured. Separately, MSD carries property insurance pursuant to an all-risk policy on MSD's buildings and equipment per the revenue bond trust agreement. There has been no reduction in insurance coverage from coverage in 2003. Insurance settlements for claims resulting from risks covered by commercial insurance have not exceeded the insurance coverage in any of the past three years.

NOTE 11 - SUBSEQUENT EVENTS

The Hamilton County Board of Commissioners have approved a 12 percent sewerage rate increase effective March 31, 2005.



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**METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI
HAMILTON COUNTY**

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

**CERTIFIED
AUGUST 25, 2005**