

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

**FINANCIAL STATEMENTS**

for the years ended December 31, 2007 and 2006





Mary Taylor, CPA  
Auditor of State

The Honorable Board of County Commissioners  
Metropolitan Sewer District of Greater Cincinnati  
1600 Guest Street  
Cincinnati, Ohio 45202

We have reviewed the *Independent Auditors' Report* of the Metropolitan Sewer District of Greater Cincinnati, Hamilton County, prepared by Foxx & Company, for the audit period January 1, 2007 through December 31, 2007. 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.

*Mary Taylor*

Mary Taylor, CPA  
Auditor of State

August 20, 2008

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**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**

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## 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, 2007 and 2006 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, 2007 and 2006 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 changes 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 June 13, 2008 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.

A handwritten signature in black ink that reads "Foxx & Company". The signature is written in a cursive, flowing style.

Cincinnati, Ohio  
June 13, 2008

# **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 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 \$557,053,000 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 (49%) 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)**

	<b>2007</b>	<b>Percentage Increase (Decrease) over 2006</b>	<b>2006</b>	<b>Percentage Increase (Decrease) over 2005</b>	<b>2005</b>
Current and other assets	\$ 405,424	12.3%	\$ 361,019	20.3%	\$ 300,112
Capital assets	<u>872,661</u>	5.5%	<u>827,402</u>	5.1%	<u>787,583</u>
Total assets	<u>\$ 1,278,085</u>	7.5%	<u>\$ 1,188,421</u>	9.3%	<u>\$ 1,087,695</u>
Long-term debt	\$ 695,707	6.9%	\$ 648,779	10.9%	\$ 585,207
Other liabilities	<u>25,325</u>	(4.3%)	<u>26,452</u>	23.5%	<u>21,416</u>
Total liabilities	<u>\$ 721,032</u>	6.4%	<u>\$ 675,231</u>	11.3%	<u>\$ 606,623</u>
Invested in capital assets					
Net of related debt	\$ 271,762	(9.7%)	\$ 303,621	8.8%	\$ 279,131
Restricted	5,810	26.8%	4,581	0.8%	5,301
Unrestricted	<u>279,481</u>	35.2%	<u>204,988</u>	3.8%	<u>196,640</u>
Total net assets	<u>\$ 557,053</u>	8.5%	<u>\$ 513,190</u>	6.7%	<u>\$ 481,072</u>

Net assets increased \$43.9 million in 2007 and \$32.1 million in 2006. 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)**

	<b>2007</b>	<b>Percentage Increase (Decrease) over 2006</b>	<b>2006</b>	<b>Percentage Increase (Decrease) over 2005</b>	<b>2005</b>
Operating revenues	\$ 176,933	8.1%	\$ 163,647	6.1%	\$ 154,171
Nonoperating revenues	<u>15,061</u>	27.2%	<u>11,842</u>	97.4%	<u>5,999</u>
Total revenues	<u>191,994</u>	9.4%	<u>175,489</u>	9.6%	<u>160,170</u>
Depreciation expense	31,507	3.1%	30,552	4.3%	29,295
Other operating expense	98,256	1.3%	97,006	10.1%	88,115
Nonoperating expense	<u>25,449</u>	5.6%	<u>24,090</u>	10.8%	<u>21,746</u>
Total expenses	<u>155,212</u>	2.4%	<u>151,648</u>	9.0%	<u>139,156</u>
Income before capital contributions	36,782	54.3%	23,841	13.5%	21,014
Capital contributions	<u>7,081</u>	(14.4%)	<u>8,277</u>	4.6%	<u>7,910</u>
Change in net assets	43,863	36.3%	32,118	11.0%	28,924
Beginning net assets	<u>513,190</u>	6.7%	<u>481,072</u>	6.4%	<u>452,148</u>
Ending net assets	<u>\$ 557,053</u>	8.5%	<u>\$ 513,190</u>	6.7%	<u>\$ 481,072</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 2007 total revenues increased 9.4 percent or \$16.5 million and expenses increased 2.4 percent or \$356 million. During 2006 total revenues increased 9.6 percent or \$15.3 million and expenses decreased 9.0 percent or \$12.5 million. The major factors which contributed to these results include:

- Operating revenues reflect an 8.6 percent rate increase implemented January 9, 2007 and a 4 percent rate increase implemented January 9, 2006.
- Nonoperating revenues increased in 2007 and 2006 due to an increase in interest rates.
- Operating expenses increased 1.3 percent or \$1.2 million in 2007. Increases in pension contribution and utilities were offset by decreases in equipment repairs and contract services. Operating expenses increased 10.1 percent or \$8.9 million in 2006. Increases in fringe benefits costs, and repair/upgrade costs were major factors in the increase. Nonoperating expense for 2007 increased 5.6 percent or \$1.4 million due to an increase

in interest expense. Nonoperating expense for 2006 decreased 10.8 percent or \$2.3 million due to an increase in interest expense.

- Capital contributions will fluctuate depending on building activity and assessment projects completed.

## **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 2007 expenses were 4.5 percent under the approved budget and the 2006 expenses were 4.0 percent under the approved budget. The principal areas of savings in both years were reduced Water-In-Basement costs and reduced debt service due to later debt issuance than budgeted.

## **CAPITAL ASSETS AND DEBT ADMINISTRATION**

### **Capital Assets**

As of December 31, the District's investment in capital assets amounted to \$873 million and \$827 million (net of accumulated depreciation) as shown in Table C for 2007 and 2006, respectively. In 2007, the District spent about \$67 million on capital improvement projects and received about \$7 million in capital contributions. In 2006, the District spent about \$58 million on capital improvement projects and received about \$8 million in capital contributions.

Sewer replacement and improvement projects were about three-fourths of the program in 2007 and two-thirds of the program in 2006.

**Table C**  
**Capital Assets**  
**(In Thousands)**

	<b>2007</b>	<b>Percentage Increase (Decrease) over 2006</b>	<b>2006</b>	<b>Percentage Increase (Decrease) over 2005</b>	<b>2005</b>
Land	\$ 4,977	0.0%	\$ 4,977	0.0%	\$ 4,977
Buildings & structures	812,974	3.0%	789,603	5.0%	752,249
Processing systems	269,811	1.4%	266,033	3.0%	258,388
Office & service equipment	38,854	7.9%	36,010	6.0%	33,977
Construction in progress	<u>273,101</u>	19.9%	<u>227,777</u>	10.6%	<u>205,943</u>
Subtotal	1,399,717	5.7%	1,324,400	5.5%	1,255,534
Less accumulated depreciation	<u>527,056</u>	6.0%	<u>496,998</u>	6.2%	<u>467,951</u>
Net capital assets	<u>\$ 872,661</u>	5.5%	<u>\$ 827,402</u>	5.2%	<u>\$ 748,727</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 2008 is \$178,655,140 which is \$6.4 million more than the 2007 budget. The increase of the 2008 operating budget reflects increases in debt service, and fringe benefits. Rate increases of 12 and 8.6 percent were approved effective January 9, 2008 and January 9, 2007, respectively.

The capital plan was submitted and accepted for the years 2008 through 2012. The plan contemplates issuing an average of about \$120 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, 2007 and 2006**  
**(all amounts expressed in thousands)**

**ASSETS**

	<u>2007</u>	<u>2006</u>
<b>Current assets:</b>		
Cash, cash equivalents and pooled investments held by the City of Cincinnati (Note 2)	\$ 16,231	\$ 15,823
Accounts receivable (Note 3)	31,770	29,774
Prepaid expenses and other	<u>4,564</u>	<u>5,090</u>
<b>Total current assets</b>	<u>52,565</u>	<u>50,687</u>
<b>Noncurrent assets:</b>		
Restricted assets:		
Cash, cash equivalents, and pooled investments held by the City of Cincinnati:		
Construction account (Note 2)	20,866	6,965
Amount to be transferred to surplus account (Note 2)	20,877	18,099
Held by trustee: (Note 4)		
Cash and cash equivalents (Note 2)	38,541	33,058
Investments - Held to maturity (Note 2)	<u>265,924</u>	<u>245,545</u>
<b>Total restricted assets</b>	<u>346,208</u>	<u>303,667</u>
Other assets:		
Unamortized financing costs	5,853	5,710
Other	<u>798</u>	<u>955</u>
<b>Total other assets</b>	<u>6,651</u>	<u>6,665</u>
Capital assets: (Note 5)		
Land	4,977	4,977
Buildings and structures	812,974	789,603
Processing systems	269,811	266,033
Office and service equipment	38,854	36,010
Construction in progress	<u>273,101</u>	<u>227,777</u>
	1,399,717	1,324,400
Less accumulated depreciation	<u>(527,056)</u>	<u>(496,998)</u>
<b>Net capital assets</b>	<u>872,661</u>	<u>827,402</u>
<b>Total noncurrent assets</b>	<u>1,225,520</u>	<u>1,137,734</u>
<b>Total assets</b>	<u>\$ 1,278,085</u>	<u>\$ 1,188,421</u>

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, 2007 and 2006**  
**(all amounts expressed in thousands)**

**LIABILITIES**

	<b>2007</b>	<b>2006</b>
<b>Current liabilities:</b>		
Payable from current assets:		
Current portion of long-term debt (Note 6)	\$ 31,655	\$ 27,938
Accounts payable	5,485	7,210
Accrued payroll expenses	2,285	1,583
Total current liabilities payable from current assets	39,425	36,731
Payable from restricted assets:		
Construction accounts payable	7,913	7,873
Accrued interest payable	2,821	2,810
Total current liabilities payable from restricted assets	10,734	10,683
<b>Total current liabilities</b>	<b>50,159</b>	<b>47,414</b>
<b>Noncurrent liabilities:</b>		
Accrued compensated absences (Note 7)	6,821	6,976
Long-term debt (Note 6)	664,052	620,841
<b>Total noncurrent liabilities</b>	<b>670,873</b>	<b>627,817</b>
<b>Total liabilities</b>	<b>721,032</b>	<b>675,231</b>
<b>Net assets:</b>		
Invested in capital assets, net of related debt	271,762	303,621
Restricted	5,810	4,581
Unrestricted	279,481	204,988
<b>Total net assets</b>	<b>\$ 557,053</b>	<b>\$ 513,190</b>

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, 2007 and 2006**  
**(all amounts expressed in thousands)**

	<u>2007</u>	<u>2006</u>
<b>Operating revenues:</b>		
Sewerage service charges	\$ 156,742	\$ 143,509
Sewer surcharges	16,115	17,235
All other revenues	<u>4,076</u>	<u>2,903</u>
<b>Total operating revenues</b>	<u>176,933</u>	<u>163,647</u>
<b>Operating expenses:</b>		
Personnel services	41,591	38,264
Purchased services	26,961	28,901
Utilities, fuel and supplies	21,025	20,785
Depreciation	31,507	30,552
Other expenses	<u>8,679</u>	<u>9,056</u>
<b>Total operating expenses</b>	<u>129,763</u>	<u>127,558</u>
<b>Operating income</b>	<u>47,170</u>	<u>36,089</u>
<b>Nonoperating revenues (expenses):</b>		
Interest income	15,061	11,842
Change in fair value of investments	(3)	619
Interest expense	(25,486)	(24,786)
Retirement of fixed assets	<u>40</u>	<u>77</u>
<b>Total nonoperating revenues (expenses)</b>	<u>(10,388)</u>	<u>(12,248)</u>
<b>Income from operations</b>	36,782	23,841
Capital contributions	<u>7,081</u>	<u>8,277</u>
<b>Change in net assets</b>	43,863	32,118
<b>Total net assets, beginning</b>	<u>513,190</u>	<u>481,072</u>
<b>Total net assets, ending</b>	<u>\$ 557,053</u>	<u>\$ 513,190</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, 2007 and 2006**  
**(all amounts expressed in thousands)**

	<u>2007</u>	<u>2006</u>
<b>Cash Flows from Operating Activities</b>		
Cash received from customers	\$ 174,853	\$ 162,870
Cash payments for goods and services	(55,465)	(53,803)
Cash payments for personnel costs	(41,043)	(38,059)
Other operating revenues	<u>4,229</u>	<u>2,903</u>
<b>Net Cash Provided by Operating Activities</b>	<b>82,574</b>	<b>73,911</b>
 <b>Cash Flows from Capital and Related Financing Activities</b>		
Principal and interest payments on long-term debt	(57,402)	(52,570)
Acquisition and construction of capital assets	(76,459)	(70,075)
Loan proceeds	246	2,816
Revenue bond proceeds	75,942	86,909
Revenue bond issuance costs	(473)	(906)
Tap-in fees	3,401	4,677
Gain/loss from sale of property, plant and equipment	<u>63</u>	<u>77</u>
<b>Net Cash (Used) by Capital and Related Financing Activities</b>	<b>(54,682)</b>	<b>(29,072)</b>
 <b>Cash Flows from Investing Activities</b>		
Purchase of government securities	(443,053)	(319,002)
Maturity of redemption of government securities	423,216	262,479
Net increase in fair value of pooled cash and investments held by City of Cincinnati	(546)	186
Interest earned on investments	<u>15,061</u>	<u>11,093</u>
<b>Net Cash Provided (Used) by Investing Activities</b>	<b>(5,322)</b>	<b>(45,244)</b>
 <b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	<b>22,570</b>	<b>(405)</b>
 <b>Cash and Cash Equivalents at January 1</b>	<u>73,945</u>	<u>74,350</u>
<b>Cash and Cash Equivalents at December 31</b>	<u>\$ 96,515</u>	<u>\$ 73,945</u>
 <b>Reconciliation of Operating Income to Net Cash Provided by Operating Activities:</b>		
Income from operations	\$ 47,170	\$ 36,089
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	31,507	30,552
Changes in assets and liabilities:		
Net change in customer accounts receivable	1,996	2,126
Net change in other assets	(321)	1,726
Net change in operating accounts payable	1,674	2,951
Net change in accrued payroll and related expenses	<u>548</u>	<u>467</u>
<b>Net Cash Provided by Operating Activities</b>	<u>\$ 82,574</u>	<u>\$ 73,911</u>
 <b>Non-cash Transactions:</b>		
Structures donated as contributed capital in aid of construction	<u>\$ 2,566</u>	<u>\$ 2,246</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, 2007 and 2006**

**NOTE 1 - ACCOUNTING POLICIES**

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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.

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, 2007 and 2006**

**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 include property, plant and equipment. Capital assets are defined as assets with an initial, individual cost of more than \$5,000.

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.

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, 2007 and 2006**

**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.

The implementation of GASB Statement No. 40 and GASB Statement No. 42 did not have an effect on the financial statements of MSD, however additional note disclosure can be found in Note 2.

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**NOTE 2 - DEPOSITS AND INVESTMENTS**

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**Deposits**

State statutes classify monies held by the District into three categories.

Active deposits are public deposits necessary to meet current demands on the treasury. Such monies must be maintained either as cash in the District's Treasury, in commercial accounts payable or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts, or in money market deposit accounts.

Inactive deposits are public deposits that the District has identified as not required for use within the current two year period of designation of depositories. Inactive deposits must either be evidenced by certificates of deposit maturing not later than the end of the current period of designation of depositories, or by savings or deposit accounts including, but not limited to, passbook accounts.

Interim deposits are deposits of interim monies. Interim monies are those monies which are not needed for immediate use but which will be needed before the end of the current period of designation of depositories. Interim deposits must be evidenced by time certificates of deposit maturing not more than one year from the date of deposit or by savings or deposit accounts including passbook accounts.

Protection of the District's deposits is provided by the Federal Deposit Insurance Corporation (FDIC), by eligible securities pledged by financial institution as security for repayment, by surety company bonds deposited with the finance director by the financial institution or by a single collateral pool established by the financial institution to secure the repayment of all public monies deposited with the institution.

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. The District's policy for deposits is collateral is required for demand deposits and certificates of deposit at 105 percent of all deposits not covered by federal deposit insurance. Obligations that may be pledged as collateral are obligations of the United States and its agencies and obligations of the State and its municipalities, school districts, and district corporations. Obligations pledged to secure deposits must be delivered to a bank other than the institution in which the deposit is made. Written custodial agreements are required. The District is required to categorize deposits and investments according to GASB Statement No. 3 *Deposits with Financial Institutions, Investments, and Reverse Purchase Agreements*. The carrying value of the District's deposits was \$57,974,000 and \$40,887,000 at December 31, 2007 and 2006, 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. For GASB 40 disclosure requirements, refer to the financial statements as of December 31, 2007 for the City of Cincinnati.

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Although the pledging bank has an investment and securities pool used to collateralize all public deposits, which held in the financial institution's name, noncompliance with federal requirements could potentially subject the District to a successful claim by the FDIC. The deposits not covered by federal depository insurance are considered uninsured and uncollateralized under the provisions of Statement No. 3 and subject to custodial credit risk.

**Investments**

State Statute and board Resolutions authorize the district to invest in obligations of U. S. Treasury, agencies and instrumentalities, certificates of deposit, repurchase agreements, money market deposit accounts, municipal depository funds, super NOW accounts, sweep accounts, separate trading of registered interest and principal of securities, mutual funds, bonds and other obligations of this State, and the State Treasurer's investment pool. Repurchase agreements are limited to 30 days and the market value of the securities must exceed the principal value of the agreement by at least 2 percent and be marked to market daily. Investments in stripped principal or interest obligations reverse repurchase agreements and derivatives are prohibited. The issuance of taxable notes for the purpose of arbitrage, the use of leverage and short selling are also prohibited. An investment must mature within five years from the date of purchase unless matched to a specific obligation or debt of the District, and must be purchased with the expectation that it will be held to maturity. Investments may only be made through specified dealers and institutions. Payment for investments may be made only upon delivery of the securities representing the investments to the finance director or, if the securities are not represented by a certificate, upon receipt of confirmation of transfer from the custodian. The District has no investment policy that addresses interest rate risk.

Custodial Credit Risk – For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty the district will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Federal National Mortgage Association Notes, Federal Home Loan Mortgage Corporation Notes, and the Federal Home Loan Bank Notes are exposed to custodial credit risk in that they are uninsured, unregistered, and held by the counterparty's trust department or agent but not in the District's name. The District has no investment policy dealing with investment custodial risk beyond the requirement in state statute that prohibits payment for investments prior to the delivery of the securities representing such investments to the Treasurer or qualified trustee.

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

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not evidenced by securities that exist in physical or book entry form. As stated in GASB Statement No. 40, obligations of the U. S. government or obligations explicitly guaranteed by the U. S. government are not considered to have credit risk and do not require disclosure of credit quality.

The money market funds are invested in a treasury obligation fund with a Moody's credit rating of Aaa.

*Concentration of Credit Risk:* The Metropolitan Sewer District uses the City of Cincinnati's Investment Policy which addresses concentration of credit risk by requiring investments to be diversified to reduce risk of loss resulting from over concentration of assets in a specific issue or class of security. The following table includes the percentage of each investment type held by MSD at December 31, 2007.

<u>Investment Type</u>	<u>Fair Value</u>	<u>% of Total</u>
Investments held by the City of Cincinnati	\$ 57,974	12.79
U. S. Government Security	265,924	76.86
Money Market Funds	38,541	10.35
	<u>\$ 362,439</u>	<u>100.00</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, 2007</u>	<u>Cash and Cash</u>	
	<u>Equivalents</u>	<u>Investments</u>
GASB Statement No. 9	\$ 96,515	\$ 265,924
Money Market Funds	<u>(38,541)</u>	<u>38,541</u>
Total	<u>\$ 57,974</u>	<u>\$ 304,465</u>

(all amounts in thousands)

<u>December 31, 2006</u>	<u>Cash and Cash</u>	
	<u>Equivalents</u>	<u>Investments</u>
GASB Statement No. 9	\$ 73,945	\$ 245,545
Money Market Funds	<u>(33,058)</u>	<u>33,058</u>
Total	<u>\$ 40,887</u>	<u>\$ 278,603</u>

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**NOTE 3 - ACCOUNTS RECEIVABLE**

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Accounts receivable consist of the following:

(all amounts in thousands)

	<b>2007</b>	<b>2006</b>
Sewer charges and surcharges:		
Unbilled amount	\$ 17,179	\$ 15,479
Billed amount	18,355	17,535
Less allowance for doubtful accounts	(5,000)	(4,500)
Other	1,236	1,260
Total	\$ 31,770	\$ 29,774

**NOTE 4 - RESTRICTED ASSETS**

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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.

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, 2007 and 2006 the following balances (at fair value) were maintained in the trust accounts:

(all amounts in thousands)

	<b>2007</b>	<b>2006</b>
Held by trustee:		
Reserve	\$ 63,922	\$ 56,771
Replacement and improvement	5,466	5,168
Bond retirement	5,810	5,335
Surplus	229,267	211,329
Total	\$ 304,465	\$ 278,603

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**NOTE 5 - CAPITAL ASSETS**

The following summarizes the changes in capital assets during 2007:

(all amounts in thousands)				
<u>December 31, 2007</u>	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Capital assets not being depreciated:				
Land	\$ 4,977	\$ -	\$ -	\$ 4,977
Construction in progress	227,777	78,079	(32,755)	273,101
	<u>232,754</u>	<u>78,079</u>	<u>(32,755)</u>	<u>278,078</u>
Capital assets being depreciated:				
Buildings and structures	789,603	23,371	-	812,974
Processing systems	266,033	4,437	(659)	269,811
Office and service equipment	36,010	3,327	(483)	38,854
	<u>1,091,646</u>	<u>31,135</u>	<u>(1,142)</u>	<u>1,121,639</u>
Total Capital Assets	1,324,400	109,214	(33,897)	1,399,717
Less accumulated depreciation	<u>496,998</u>	<u>30,518</u>	<u>(460)</u>	<u>527,056</u>
Net capital assets	<u>\$ 827,402</u>	<u>\$ 78,696</u>	<u>\$ (33,437)</u>	<u>\$ 872,661</u>

The following summarizes the changes in capital assets during 2006:

(all amounts in thousands)				
<u>December 31, 2006</u>	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Capital assets not being depreciated:				
Land	\$ 4,977	\$ -	\$ -	\$ 4,977
Construction in progress	205,943	70,000	(48,166)	227,777
	<u>210,920</u>	<u>70,000</u>	<u>(48,166)</u>	<u>232,754</u>
Capital assets being depreciated:				
Buildings and structures	752,249	37,354	-	789,603
Processing systems	258,388	8,233	(588)	266,033
Office and service equipment	33,977	2,654	(621)	36,010
	<u>1,044,614</u>	<u>48,241</u>	<u>(1,209)</u>	<u>1,091,646</u>
Total Capital Assets	1,255,534	118,241	(49,375)	1,324,400
Less accumulated depreciation	<u>467,951</u>	<u>29,668</u>	<u>(621)</u>	<u>496,998</u>
Net capital assets	<u>\$ 787,583</u>	<u>\$ 88,573</u>	<u>\$ (48,754)</u>	<u>\$ 827,402</u>

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**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>2007</u>	<u>2006</u>
Revenue Bonds					
2007 (a)	\$ 72,385	3.50-5.25	2032	\$ 72,385	\$ -
2006 (b)	83,045	4.00-5.00	2031	81,335	83,045
2005 (c)	170,560	2.50-5.00	2030	166,500	168,680
2004 (d)	46,385	2.00-5.00	2017	41,875	44,135
2003 (e)	215,575	1.50-5.25	2028	206,175	207,515
2001 (f)	76,000	2.30-5.25	2026	32,505	34,030
2000 (g)	40,085	4.50-5.75	2025	6,345	7,440
1997 (h)	105,245	3.85-5.13	2017	11,595	16,525
1993 (i)	171,790	2.45-5.60	2016	<u>23,855</u>	<u>34,880</u>
				642,570	596,250
Ohio Water Development					
Authority Contracts	41,830	2.00-7.49	2016	747	857
Ohio Water and Sewer					
Rotary Commission	-	-	-	50	50
Ohio Public Works Commssion	-	3.54-4.80	2017	3,491	3,769
Water Pollution Control Loan Fund	-	0.00-3.00	2018	<u>23,429</u>	<u>24,668</u>
Total obligations				670,287	625,594
Bond discounts				(111)	(201)
Bond premiums				32,699	32,208
Deferred loss on defeasance				(7,168)	(8,822)
Current maturities				<u>(31,655)</u>	<u>(27,938)</u>
Long-term portion				<u>\$ 664,052</u>	<u>\$ 620,841</u>

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

(all amounts in thousands except percents)

Year	Revenue Bonds		OWDA		OPWC		WPCLF*	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2008	28,825	31,037	114	27	283	69	2,434	1,748
2009	30,235	29,721	118	23	288	64	2,523	1,658
2010	31,845	28,399	122	19	294	58	2,616	1,566
2011	33,310	26,940	126	15	300	52	3,718	2,206
2012	34,830	25,307	131	10	301	46	3,846	2,078
2013-2017	199,720	99,775	136	5	1,418	138	19,624	8,385
2018-2022	95,965	61,141	-	-	563	33	19,330	5,179
2023-2027	118,770	35,073	-	-	44	1	17,764	2,118
2028-2032	69,070	8,194	-	-	-	-	4,980	247
	<u>\$ 642,570</u>	<u>\$ 345,587</u>	<u>\$ 747</u>	<u>\$ 99</u>	<u>\$ 3,491</u>	<u>\$ 461</u>	<u>\$ 76,835</u>	<u>\$ 25,185</u>

\*This amount represents the total amount of the loans, some of which have not been fully drawdown or finalized.  
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Bond discount, premium, loss on defeasance activity for the year:

<u>December 31, 2007</u>	<u>Beginning Balance</u>	<u>Amortized</u>	<u>Refunded</u>	<u>Issued</u>	<u>Ending Balance</u>
Bond discount	\$ (201)	\$ 90	\$ -	\$ -	\$ (111)
Bond premium	32,208	(2,887)	-	3,378	32,699
Loss on defeasance	(8,822)	1,654	-	-	(7,168)
Total	<u>\$ 23,185</u>	<u>\$ (1,143)</u>	<u>\$ -</u>	<u>\$ 3,378</u>	<u>\$ 25,420</u>

  

<u>December 31, 2006</u>	<u>Beginning Balance</u>	<u>Amortized</u>	<u>Refunded</u>	<u>Issued</u>	<u>Ending Balance</u>
Bond discount	\$ (317)	\$ 116	\$ -	\$ -	\$ (201)
Bond premium	31,163	(2,668)	-	3,713	32,208
Loss on defeasance	(10,477)	1,655	-	-	(8,822)
Total	<u>\$ 20,369</u>	<u>\$ (897)</u>	<u>\$ -</u>	<u>\$ 3,713</u>	<u>\$ 23,185</u>

Long-term debt activity for the year:

<u>December 31, 2007</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Revenue Bonds	\$ 596,250	\$ 72,385	\$ 26,065	\$ 642,570
Ohio Water Development Authority	857	-	110	747
Ohio Water and Sewer Rotary Commission	50	-	-	50
Ohio Public Works Commission	3,769	-	278	3,491
Water Pollution Control Loan Fund	24,668	246	1,485	23,429
Total	<u>\$ 625,594</u>	<u>\$ 72,631</u>	<u>\$ 27,938</u>	<u>\$ 670,287</u>

  

<u>December 31, 2006</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Revenue Bonds	\$ 536,335	\$ 83,045	\$ 23,130	\$ 596,250
Ohio Water Development Authority	963	-	106	857
Ohio Water and Sewer Rotary Commission	50	-	-	50
Ohio Public Works Commission	4,041	-	272	3,769
Water Pollution Control Loan Fund	23,449	2,649	1,430	24,668
Total	<u>\$ 564,838</u>	<u>\$ 85,694</u>	<u>\$ 24,938</u>	<u>\$ 625,594</u>

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**Revenue Bonds**

- a) Effective December 20, 2007, MSD issued \$72,385,000 Series A Sewer System Improvement Revenue Bonds dated December 1, 2007. The proceeds from the 2007 Series A bonds were used to permanently fund certain previous capital expenditures, fund the new bond reserve requirements and pay the cost of issuance. The 2007 Series A 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, 2000, 2001, 2003A, 2003B, 2004, 2005A , 2005B and 2006 bonds, secured equally and ratably under the Trust Agreement.
- b) Effective November 15, 2006, MSD issued \$83,045,000 Series A Sewer System Improvement Revenue Bonds dated November 1, 2006. The proceeds from the 2005 Series B bonds were used to permanently fund certain previous capital expenditures, fund the new bond reserve requirements and pay the cost of issuance. The 2006 Series A 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, 2000, 2001, 2003A, 2003B, 2004, 2005A and 2005B bonds, secures equally and ratably under the Trust Agreement.
- c) Effective March 30, 2005, MSD issued \$86,960,000 Series A, Sewer System Refunding Revenue Bonds dated March 1, 2005. The proceeds from the 2005 bonds were used to defease portions of the 1997, 2000 and 2001 revenue bonds and pay for the cost of issuance. The 2005A bonds are special obligations of the District, payable solely form the net revenues of the District and were issued on parity with the 1993, 1995, 1997, 2000, 2001, 2003A, 2003B and 2004 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 \$46,980,000 of outstanding 1997 Series A Bonds, \$20,665,000 of outstanding 2000 Series A Bonds and \$19,280,000 of outstanding 2001 Series A Bonds. As a result, these bonds are considered defeased and the liability for those bonds removed from the balance sheet.

Although the refunding resulted in the recognition of an accounting loss of \$5,211,000 in accordance with GASB 23, the District in effect reduced its aggregate debt service payments by \$5,201,000 and obtained an economic gain (difference between the present values of the old and new debt service payments) of \$3,748,000.

Effective November 9, 2005, MSD issued \$83,600,000 Series B Sewer System Improvement Revenue Bonds dated November 1, 2005. The proceeds from the 2005 Series B bonds were used to permanently fund certain previous capital expenditures, fund the new bond reserve requirements and pay the cost of issuance. The 2005 Series B bonds are special obligations of the District, payable solely from the net revenues of the District

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and were issued on a parity with the 1993, 1995, 1997, 2000, 2001, 2003A, 2003B, 2004 and 2005A bonds, secured equally and ratably under the Trust Agreement.

- d) 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.

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.

- e) 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.

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

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

- f) 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.
- g) 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.
- h) 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.
- i) 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 parity with the 1993 Series A bonds, secured equally and ratably under the Trust Agreement.
- j) 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.

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The 2007, 2006, 2005, 2004, 2003, 2001, 2000, 1997 and 1993 Bonds may be redeemed prior to their maturities in accordance with provisions of the bond resolutions. The redemption process for the bonds includes declining premiums up to 2 percent of principal.

For December 31, 2007 and December 31, 2006 the amount of defeased debt outstanding was \$46,345,000 and \$99,605,000 respectively.

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

(all amounts in thousands)									
Year	2007 Bonds	2006 Bonds	2005 Bonds	2004 Bonds	2003 Bonds	2001 Bonds	2000 Bonds	1997 Bonds	1993 Bonds
2008	1,615	1,955	7,235	2,200	1,475	1,585	1,145	-	11,615
2009	1,760	2,035	7,575	2,260	1,500	1,660	1,205	-	12,240
2010	1,820	2,115	2,355	-	16,910	1,740	1,265	5,640	-
2011	1,885	2,200	2,445	-	17,690	1,805	1,330	5,955	-
2012	1,950	2,290	2,560	6,165	18,585	1,880	1,400	-	-
2013-2017	10,850	12,970	59,900	31,250	82,235	2,515	-	-	-
2018-2022	13,355	16,345	38,650	-	22,340	5,275	-	-	-
2023-2027	17,150	20,765	29,820	-	34,990	16,045	-	-	-
2028-2032	22,000	20,660	15,960	-	10,450	-	-	-	-
	<u>\$ 72,385</u>	<u>\$ 81,335</u>	<u>\$ 166,500</u>	<u>\$ 41,875</u>	<u>\$ 206,175</u>	<u>\$32,505</u>	<u>\$ 6,345</u>	<u>\$ 11,595</u>	<u>\$23,855</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**  
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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)

	<b>2007</b>	<b>2006</b>
Revenues:		
Total operating revenues	\$ 176,933	\$ 163,647
Interest income	15,061	11,842
Capitalized interest income	2,188	1,001
Tap-in/connection fees	3,401	4,677
Total pledged revenue	197,583	181,167
Total operating and maintenance expenses less depreciation and amortization	(98,256)	(97,005)
Half of pledged revenues transferred to surplus account	10,438	9,049
Net income available for debt service (a)	\$ 109,765	\$ 93,211
Principal and interest requirement on revenue bonds (b)	\$ 55,184	\$ 49,348
Principal and interest requirements on obligations (c)	\$ 58,176	\$ 52,340
Debt service coverage		
Revenue bonds (a) divided by (b)	199%	189%
All obligations (a) divided (c)	189%	178%
Maximum debt service coverage required on revenue bonds	125%	125%

**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.

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

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
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**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)

	<b>2007</b>	<b>2006</b>
Interest incurred	\$ 29,150	\$ 26,823
Less Interest capitalization	(3,664)	(2,037)
Interest expense	\$ 25,486	\$ 24,786

**NOTE 7 – COMPENSATED ABSENCES**

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**Compensated Absences**

Compensated absences consist of vacation time, sick pay and compensatory time. The following is a summary of activity for 2007 and 2006.

(all amounts in thousands)

	<b>Beginning Balance</b>	<b>Increase</b>	<b>Decrease</b>	<b>Ending Balance</b>
2007	\$ 6,976	\$ 3,804	\$ 3,959	\$ 6,821
2006	\$ 6,581	\$ 3,820	\$ 3,425	\$ 6,976

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**  
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**NOTE 8 - PENSION AND RETIREMENT**

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**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 2007, the required contribution rates were 21.77 percent for MSD and 7 percent for employees. For 2006, the required contribution rates were 17 percent for MSD and 7 percent for employees. MSD's contributions to CRS for the years ending December 31, 2007 and 2006 were \$5,993,000 and \$4,584,000, 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 METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**for the years ended December 31, 2007 and 2006**

The actuarial assumptions used for the December 31, 2007 valuation included an assumption for hospital and surgical benefits recognizing adjusted premiums, based on experience from recent years, adjusted to current year by assumed annual increases in premium costs. The cost of coverage is recognized as an expense as claims are paid. CRS has 4,483 active contributing participants of which 497 are MSD employees. For 2007, MSD's contribution was 16 percent of the total employers' contribution.

**NOTE 9 - RELATED PARTY TRANSACTIONS**

Cincinnati Water Works provides billing and collection services on customers' accounts for MSD. Fees for these services for 2007 and 2006 were \$5,192,000 and \$4,791,000 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 2007 and 2006 were \$2,270,000 and \$2,080,000 respectively. In addition, the City's Municipal Garage provides gasoline and repairs vehicles for MSD. Fees for these services were \$1,474,000 and \$1,518,000 for 2007 and 2006, respectively.

**NOTE 10 - 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, still to be approved, would cost about \$2.5 billion through 2035 measured in 2008 dollars. The consent decree documents are posted on the MSD web site, [msdgc.org](http://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 \$115 million as of December 31, 2007.

**THE METROPOLITAN SEWER DISTRICT OF GREATER CINCINNATI**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**for the years ended December 31, 2007 and 2006**

**NOTE 11 - RISK MANAGEMENT**

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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 12 - SUBSEQUENT EVENTS**

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The Hamilton County Board of Commissioners has approved a 12 percent sewerage rate increase effective January 9, 2008.



**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS 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, 2007, and have issued our report thereon dated June 13, 2008. 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.

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the MSD's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the MSD's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the MSD's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the MSD's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the MSD's financial statements that is more than inconsequential will not be prevented or detected by the MSD's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the MSD's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the MSD's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, 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 or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, County Commissioners and the Auditor of State and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink that reads "Fox & Company". The signature is written in a cursive, flowing style.

Cincinnati, Ohio  
June 13, 2008





**Mary Taylor, CPA**  
Auditor of State

**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**  
**SEPTEMBER 2, 2008**