

RACINE WASTEWATER UTILITY
Racine, Wisconsin

FINANCIAL STATEMENTS
December 31, 2006 and 2005

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Independent Auditor's Report

Board of Commissioners
Racine Wastewater Utility
Racine, Wisconsin

We have audited the accompanying statements of net assets, the related statements of revenues, expenses and changes in net assets, and cash flows of the Racine Wastewater Utility, an enterprise fund of the City of Racine, as of and for the years ended December 31, 2006 and 2005, which collectively comprise Racine Wastewater Utility's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Utility's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes 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 audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Racine Wastewater Utility and do not purport to, and do not, present fairly the financial position of the City of Racine, Wisconsin, as of December 31, 2006 and 2005, and the changes in its financial position and cash flows, where applicable, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Racine Wastewater Utility as of December 31, 2006 and 2005, and the results of its operations and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The Racine Wastewater Utility has not presented the management's discussion and analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be a part of, the basic financial statements.

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

Clifton Gunderson LLP

Racine, Wisconsin
June 15, 2007

**RACINE WASTEWATER UTILITY
STATEMENTS OF NET ASSETS
December 31, 2006 and 2005**

ASSETS

	<u>2006</u>	<u>2005</u>
CURRENT ASSETS		
Cash and cash equivalents	\$ 1,991,093	\$ 2,552,977
Investments	5,033,700	3,957,785
Accrued interest receivable	22,845	8,871
Accounts receivable, less allowance for doubtful accounts of \$1,000 in 2006 and 2005:		
Consumers	1,957,135	1,955,118
Other	1,412,020	1,002,958
Delinquent billings receivable - tax roll	1,292,775	1,109,536
Due from other funds	1,846,188	1,935,289
Inventories	<u>53,734</u>	<u>46,919</u>
Total current assets	<u>13,609,490</u>	<u>12,569,453</u>
 RESTRICTED ASSETS		
Cash and cash equivalents	41,984	43,080
Investments	6,774,054	5,331,156
Accrued interest receivable	52,006	38,962
Plant capacity receivable, current portion	2,235,930	2,807,518
Interest receivable - plant capacity	197,877	170,921
Plant capacity receivable, long term portion	<u>42,182,848</u>	<u>44,088,425</u>
Total restricted assets	<u>51,484,699</u>	<u>52,480,062</u>
 CAPITAL ASSETS		
Utility plant in service	144,660,103	143,844,178
Less: accumulated depreciation	<u>(41,598,184)</u>	<u>(37,538,477)</u>
Net depreciated value	103,061,919	106,305,701
Land	99,950	99,950
Construction in progress	<u>144,448</u>	<u>361,201</u>
Total capital assets	<u>103,306,317</u>	<u>106,766,852</u>
 OTHER ASSETS		
Due from other funds	1,733,428	2,288,332
Deferred debt expense	<u>78,861</u>	<u>92,278</u>
Total other assets	<u>1,812,289</u>	<u>2,380,610</u>
 TOTAL ASSETS	 <u>\$170,212,795</u>	 <u>\$174,196,977</u>

LIABILITIES AND NET ASSETS

	<u>2006</u>	<u>2005</u>
CURRENT LIABILITIES		
Accounts payable	\$ 276,638	\$ 232,794
Due to other funds	672,152	624,510
Advances from other funds, current portion	22,838	21,000
Accrued compensated absences, current portion	49,521	31,310
Accrued liabilities	<u>216,557</u>	<u>283,004</u>
Total current liabilities	<u>1,237,706</u>	<u>1,192,618</u>
 CURRENT LIABILITIES - PAYABLE FROM RESTRICTED ASSETS		
Accrued interest payable	381,172	393,722
Long term debt, current portion	4,572,520	4,376,358
Deferred capacity revenue, current portion	<u>1,043,782</u>	<u>1,043,940</u>
Total current liabilities - payable from restricted assets	<u>5,997,474</u>	<u>5,814,020</u>
 NONCURRENT LIABILITIES		
Accrued compensated absences, long term portion	357,784	385,104
Advances from other funds, long term portion	809,288	832,125
Long term debt	75,740,161	78,873,687
Deferred capacity revenue, long-term portion	<u>45,933,552</u>	<u>46,977,334</u>
Total noncurrent liabilities	<u>122,840,785</u>	<u>127,068,250</u>
Total liabilities	<u>130,075,965</u>	<u>134,074,888</u>
 NET ASSETS		
Invested in capital assets, net of related debt	26,584,584	27,317,586
Restricted	6,061,477	4,592,311
Unrestricted	<u>7,490,769</u>	<u>8,212,192</u>
Total net assets	<u>40,136,830</u>	<u>40,122,089</u>
 TOTAL LIABILITIES AND NET ASSETS	 <u>\$170,212,795</u>	 <u>\$174,196,977</u>

These financial statements should be read only in connection with
the accompanying notes to financial statements.

**RACINE WASTEWATER UTILITY
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
Years Ended December 31, 2006 and 2005**

	<u>2006</u>	<u>2005</u>
OPERATING REVENUES	<u>\$ 12,473,984</u>	<u>\$ 12,319,348</u>
OPERATING EXPENSES		
Operation and maintenance	7,216,624	6,762,802
Depreciation	4,376,589	3,858,542
Taxes	<u>180,760</u>	<u>182,272</u>
Total operating expenses	<u>11,773,973</u>	<u>10,803,616</u>
OPERATING INCOME	<u>700,011</u>	<u>1,515,732</u>
NONOPERATING REVENUE (EXPENSES)		
Investment earnings	590,563	374,663
Interest expense	(2,287,743)	(2,163,637)
Household hazardous waste program revenue	158,961	-
Household hazardous waste program expense	(218,511)	-
Intergovernmental interest reimbursement	1,302,535	1,239,921
Plant capacity income	1,043,940	1,043,941
Amortization of bond issuance costs	(13,417)	(13,417)
Gain on disposal of fixed assets	26,039	71,555
Miscellaneous income	<u>202,419</u>	<u>174,206</u>
Total nonoperating revenues (expenses)	<u>804,786</u>	<u>727,232</u>
Income before transfers	1,504,797	2,242,964
TRANSFER OUT	<u>(1,490,056)</u>	<u>(1,656,641)</u>
CHANGE IN NET ASSETS	14,741	586,323
NET ASSETS, BEGINNING OF YEAR	<u>40,122,089</u>	<u>39,535,766</u>
NET ASSETS, END OF YEAR	<u>\$ 40,136,830</u>	<u>\$ 40,122,089</u>

These financial statements should be read only in connection with
the accompanying notes to financial statements.

**RACINE WASTEWATER UTILITY
STATEMENTS OF CASH FLOWS
Years Ended December 31, 2006 and 2005**

	<u>2006</u>	<u>2005</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Received from customers and users	\$ 12,694,592	\$ 11,183,502
Paid to suppliers	(4,299,698)	(6,426,918)
Paid to employees	<u>(3,088,571)</u>	<u>(2,338,438)</u>
Net cash flows provided by operating activities	<u>5,306,323</u>	<u>2,418,146</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Transfers out	(1,490,056)	(1,656,641)
Advances from other funds	(20,999)	(19,425)
Interest paid on advance from other funds	(44,081)	(44,558)
Miscellaneous receipts	<u>142,868</u>	<u>174,204</u>
Net cash flows used in noncapital financing activities	<u>(1,412,268)</u>	<u>(1,546,420)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of utility plant	(926,462)	(3,589,276)
Received from sale of capital assets	36,447	154,533
Principal paid on long-term debt	(4,376,358)	(4,152,828)
Proceeds from issuance of long-term debt	1,438,994	3,921,869
Interest paid on long-term debt	(2,256,212)	(2,123,010)
Intergovernmental interest reimbursement	1,302,535	1,239,921
Proceeds from plant capacity	<u>2,279,288</u>	<u>1,572,492</u>
Net cash flows used in capital and related financing activities	<u>(2,501,768)</u>	<u>(2,976,299)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Investments purchased	(40,889,569)	(30,145,240)
Investments sold and matured	38,370,757	32,218,734
Investment income	<u>563,545</u>	<u>355,515</u>
Net cash flows provided by (used in) investing activities	<u>(1,955,267)</u>	<u>2,429,009</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	(562,980)	324,436
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>2,596,057</u>	<u>2,271,621</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 2,033,077</u>	<u>\$ 2,596,057</u>

	<u>2006</u>	<u>2005</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Operating income	\$ 700,011	\$ 1,515,732
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation	4,376,589	3,858,542
Effects of changes in operating assets and liabilities:		
Accounts receivable	(423,397)	(444,889)
Inventories	(6,815)	(18,121)
Due from other funds	644,005	(690,956)
Prepaid expenses and other assets	-	1
Compensated absences	(9,109)	(4,288)
Accounts payable	43,844	(1,893,165)
Accrued liabilities	(66,447)	109,415
Due to other funds	47,642	-
Advances from other funds	-	(14,125)
	<u> </u>	<u> </u>
Net cash flows from operating activities	<u>\$ 5,306,323</u>	<u>\$ 2,418,146</u>
 RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE STATEMENT OF NET ASSETS		
Cash and cash equivalents - unrestricted	\$ 1,991,093	\$ 2,552,977
Cash and cash equivalents - restricted	<u>41,984</u>	<u>43,080</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 2,033,077</u>	<u>\$ 2,596,057</u>

These financial statements should be read only in connection with the accompanying notes to financial statements.

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Racine Wastewater Utility is an Enterprise Fund of the City of Racine. These financial statements present the financial position, results of operations, and cash flows of the City of Racine Wastewater Utility only and do not include transactions of any other City Funds. The Racine Wastewater Utility provides sewer service to the territory which includes the corporate limits of the City of Racine, Village of Mount Pleasant, Village of North Bay, Village of Elmwood Park, Village of Sturtevant, and Village of Caledonia. The Utility has the responsibility to determine and levy sewer user charges in order to apportion all operation and maintenance expenses and debt service charges in its service territory.

The Utility is managed by eleven Commissioners. Rates are established through the budget process on an annual basis to recover operating expenses, debt service and replacement charges, after giving effect to prior year surpluses or deficits. The rates are billed to the municipal entities in proportion to each user's contribution to total wastewater flow and loading into the treatment system. The Utility has the authority to finance its operations through the use of a user charge.

The significant accounting principles and policies utilized by the utility are described below.

BASIS OF ACCOUNTING

The Utility prepares its financial statements in accordance with generally accepted accounting principles for enterprise funds as formulated by the Government Accounting Standards Board. The financial statements reflect the full accrual method of accounting whereby revenues are recognized when earned and expenses are recorded as liabilities when incurred. The Utility applies all applicable Statements and Interpretations of the Financial Accounting Standards Board (FASB), Accounting Principles Board (APB) Opinions and Accounting Research Bulletins issued on or before November 30, 1989 unless they conflict Government Accounting Standards Board (GASB) pronouncements. The Utility has elected not to follow the FASB and APB Standards after November 30, 1989.

USE OF ESTIMATES IN PREPARING FINANCIAL STATEMENTS

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.

CASH EQUIVALENTS

For purposes of reporting cash flows, cash equivalents include any highly liquid investments purchased with a maturity of three months or less when acquired.

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

INVESTMENTS

Investments are stated at fair value, which is the amount at which an investment could be exchanged in a current transaction between willing parties. Fair value is determined by quoted market prices. No investments are reported at amortized cost.

ACCOUNTS RECEIVABLE

Accounts receivable is composed of charges to customers for sewer services and receivables for sundry bill charges that cannot be attached to the property. The year-end balance includes unpaid charges and a year-end estimate of the receivables that will be billed in the first quarter of the subsequent year.

Customer accounts receivable are stated at invoice plus accrued interest. Unpaid accounts over twenty days bear interest at 1% per month. Sundry bill charges bear no interest.

Interest continues to accrue on customer delinquent accounts until it is placed in the tax roll at which time a 10% penalty is assessed to the account. Payments to an accounts receivable are applied to specific invoices identified on the customer's remittance advice or, if unspecified, to the earliest unpaid invoices.

The carrying amount of accounts receivable is reduced by a valuation allowance that reflects management's best estimate of sundry bill charges that will not be collected. The allowance for doubtful accounts is based on management's assessment of the collectability of specific customer accounts and the aging of the accounts receivable. All accounts or portions thereof deemed to be uncollectible or to require an excessive collection cost are written off to the allowance for doubtful accounts.

INVENTORIES

Inventories of materials and supplies are stated at the lower of cost or market with cost determined on a first in, first out (FIFO) basis.

RESTRICTED ASSETS

Mandatory segregations of assets are presented as restricted assets. Such segregations are required by bond agreements and other external parties. Current liabilities payable from these restricted assets are so classified.

OPERATIONS

Metered service sales to customers are billed at rates determined by the Utility Commissioners. Most customers, with exception of industrial, are billed every three months for services rendered. Industrial customers are billed monthly. The month billed is dependent on the district in which the customer resides. All delinquent wastewater accounts receivable balances less than \$7,500 at the time of the property tax lien date are placed on the customer's tax bill and collected through the normal collection process.

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CAPITAL ASSETS

Capital assets are generally defined by the Utility as assets with an initial, individual cost of more than \$1,000 and estimated useful life in excess of one year.

Capital assets of the utility are recorded at cost or the fair market value at the time of contribution to the Utility. Major outlays for utility plant are capitalized as projects are constructed. Interest incurred during the construction phase is reflected in the capitalized value of the capital assets constructed, net of interest earned on the invested proceeds over the same period. Capital assets in service are depreciated using the straight – line method over useful lives ranging from five to one hundred years.

LONG-TERM OBLIGATIONS

Long-term debt and other obligations are reported as utility liabilities. Bond premiums and discounts as well as issuance costs are deferred and amortized over the life of the bonds using the straight-line method. Gains or losses on prior refundings are amortized over the remaining life of the old debt or the life of the new debt, which ever is shorter.

COMPENSATED ABSENCES

Vacation is recorded as expense when paid. Vacation pay is earned on a monthly basis during the calendar year and is forfeited if not taken by the end of the year. Sick leave is earned at a rate of one day per month. Unused sick pay is allowed to accumulate to 156 working days. In general, upon death, retirement or total disability, an employee is entitled to a sum equal to 50% of total such leave accumulated up to a maximum of 140 days. Accumulated sick leave earned but not taken and any salary related benefits thereon have been reported as accrued compensated absences.

REVENUES AND EXPENSES

The Utility distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. The principal operating revenues of the Utility are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

TRANSFERS

Transfers include payments made from its reserve accounts to the City of Racine with respect to the Racine Public Library, Racine Zoo and the Charles A. Wustum Museum of Fine Arts totaling \$812,650 and an equity transfer to the City of Racine of \$653,474 and the payment in lieu of taxes of \$23,932.

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

EQUITY CLASSIFICATIONS

Equity is classified as net assets and displayed in three components.

- a. Invested in capital assets, net of related debt – Consists of capital assets including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets less any unspent debt proceeds.
- b. Restricted net assets – Consists of net assets with constraints placed on their use by 1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments or, 2) law through constitutional provisions or enabling legislation.
- c. Unrestricted net assets – All other net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

COMPARATIVE DATA

Certain amounts presented in the prior year data have been reclassified in order to be consistent with the current year’s presentation.

NOTE 2 - CASH AND INVESTMENTS

The Utility had the following deposits and investments as of December 31, 2006 and 2005.

	<u>2006</u>	<u>2005</u>
Demand deposits	\$ 2,033,077	\$ 2,596,077
Certificate of deposit	100,000	-
U.S. Government agency securities	<u>11,707,754</u>	<u>9,288,941</u>
	<u>\$ 13,840,831</u>	<u>\$ 11,885,018</u>
	<u>2006</u>	<u>2005</u>
Reconciliation to the financial statements		
Per statement of net assets		
Unrestricted cash and cash equivalents	\$ 1,991,093	\$ 2,552,997
Unrestricted investments	5,033,700	3,957,785
Restricted cash and cash equivalents	41,984	43,080
Restricted investments	<u>6,774,054</u>	<u>5,331,156</u>
Total Cash and Investments	<u>\$ 13,840,831</u>	<u>\$ 11,885,018</u>

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 2 - DEPOSITS AND INVESTMENTS (CONTINUED)

Deposits in each local and area bank are insured by the FDIC in the amount of \$100,000 for interest bearing accounts and \$100,000 for noninterest bearing accounts.

Bank accounts are also insured by the State Deposit Guarantee Fund in the amount of \$400,000. However, due to the relatively small size of the Guarantee Fund in relationship to the total deposits covered and other legal implications, recovery of material principal losses may not be significant to individual entities. This coverage has not been considered for custodial credit risk below.

Investment Policy

The Utility has not adopted a formal investment policy; however, the Utility invests in accordance with Wisconsin State Statutes. Under state statute, investments are limited to:

- Time deposits in any credit union, bank, savings bank, trust company, or savings and loan association;
- Bonds or securities of any county, city, drainage Utility, vocational, technical, and adult education (VTAE) Utility, village, town or school Utility of the state;
- Bonds or securities issued or guaranteed by the Federal government; and
- The state local government investment pool.
- Any security maturing in seven years or less and having the highest or second highest rating category of a nationally recognized rating agency.
- Securities of an open-end management investment company or investment trust subject to various conditions and investment options.
- Repurchase agreements with public depositories with certain conditions.

Custodial Credit Risk for Deposits

Custodial credit risk for deposits is the risk that in the event of the failure of a depository financial institution, the Utility will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The Utility does not have a formal policy addressing this type of deposit risk.

As of December 31, 2006 and 2005, the Utility's carrying value of the deposits was \$2,033,077 and \$2,596,077 as compared to bank balances of \$2,198,225 and \$2,763,649, respectively. Of the bank balances at December 31, 2006 and 2005, \$100,000, was covered by federal depository insurance. The remaining balances at December 31, 2006 and 2005 were collateralized by securities held by the bank or its correspondent bank but not in the Utility's name.

Custodial Credit Risk for Investments

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the Utility will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Utility does not have a formal policy addressing this type of investment risk.

As of December 31, 2006 and 2005, the Utility's carrying value of the investments were \$11,807,754 and \$9,288,941 for 2006 and 2005, respectively. Of the investment balances at December 31, 2006 and 2005, \$100,000, was collateralized by federal depository insurance. The remaining balances at December 31, 2006 and 2005 were collateralized by securities are held by an agent in the Utility's name.

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 2 - DEPOSITS AND INVESTMENTS (CONTINUED)

Credit Risk

Credit risk is the risk that, an issuer or other counterparty to an investment will not fulfill its obligations to the Utility. The Utility does not have a formal policy addressing this type of investment risk.

The Utility invests solely in U.S. government agency obligations. These types of investments are explicitly guaranteed by the U.S. government and are not considered subjected to credit risk. As of December 31, 2006 and 2005, the Utility had \$11,707,754 and \$9,288,941, respectively, in these types of investments.

Concentration of Credit Risk

Concentration of credit risk refers to risk of loss attributed to the Utility investment in a single issuer. The Utility does not have a formal policy addressing this type of investment risk. As of December 31, 2006 and 2005, the Utility invests solely in U.S. government agency securities which are not considered subject to credit risk.

Interest Rate Risk

Interest rate risk is the risk that, changes in interest rates will adversely affect the fair value of an investment. The Utility does not have a formal policy addressing this type of investment risk. As of December 31, 2006 and 2005, the Utility had the following investments and maturities.

2006		
Type of Investment	Fair Value	Average Maturities
U.S. Government agency securities	\$ 11,707,754	180 days
Certificate of Deposit	100,000	8 months
2005		
Type of Investment	Fair Value	Average Maturities
U.S. Government agency securities	\$ 9,288,941	180 days

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 3 - RESTRICTED ASSETS

Certain proceeds of the utility's revenue bonds, as well as certain resources set aside for their repayment, are classified as restricted assets on the statement of net assets because their use is limited by applicable bond covenants. The following revenue bond accounts are reported as restricted assets:

Bond redemption fund – Used to segregate resources accumulated for debt service payments over the next twelve months.

Reserve fund – Used to report resources set aside to make up potential future deficiencies in the redemption account.

Depreciation fund – Used to report resources set aside to fund plant renewals and replacement or make up potential future deficiencies in the redemption account

DNR replacement fund – As a condition of receiving state and federal funds for wastewater plant construction, the utility has established an account for replacement of certain mechanical equipment.

A summary of restricted assets is as follows:

	<u>2006</u>	<u>2005</u>
Cash and investments:		
Bond redemption fund	\$ 2,490,428	\$ 1,023,233
DNR replacement fund	2,924,880	2,945,480
Depreciation fund	976,087	979,191
Reserve fund	424,643	426,332
Total cash and investments	<u>6,816,038</u>	<u>5,374,236</u>
Accrued interest receivable:		
Bond redemption fund	14,224	8,221
DNR replacement fund	35,302	27,926
Depreciation fund	1,728	2,815
Reserve fund	752	-
Total accrued interest receivable	<u>52,006</u>	<u>38,962</u>
Plant capacity		
Current portion	2,235,930	2,807,518
Long term portion	42,380,725	44,088,425
Total plant capacity	<u>44,616,655</u>	<u>46,895,943</u>
Interest receivable - plant capacity	<u>-</u>	<u>170,921</u>
Total restricted assets	<u>\$ 51,484,699</u>	<u>\$ 52,480,062</u>

RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005

NOTE 4 - CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2006 and 2005 was as follows:

	2006			Ending Balance
	Beginning Balance	Increases	Decreases	
Capital assets not being depreciated:				
Land	\$ 99,950	\$ -	\$ -	\$ 99,950
Construction in progress	<u>361,201</u>	<u>1,273,751</u>	<u>(1,490,504)</u>	<u>144,448</u>
Total capital assets not being depreciated	<u>461,151</u>	<u>1,273,751</u>	<u>(1,490,504)</u>	<u>244,398</u>
Capital assets being depreciated:				
Buildings and system	75,408,383	-	-	75,408,383
Improvements other than buildings	22,231,669	-	-	22,231,669
Machinery and equipment	<u>46,204,126</u>	<u>1,143,215</u>	<u>(327,290)</u>	<u>47,020,051</u>
Total capital assets being depreciated	<u>143,844,178</u>	<u>1,143,215</u>	<u>(327,290)</u>	<u>144,660,103</u>
Less accumulated depreciation for:				
Buildings and system	(18,329,816)	(1,824,928)	-	(20,154,744)
Improvements other than buildings	(10,014,343)	(168,840)	-	(10,183,183)
Machinery and equipment	<u>(9,194,318)</u>	<u>(2,382,821)</u>	<u>316,882</u>	<u>(11,260,257)</u>
Total accumulated depreciation	<u>(37,538,477)</u>	<u>(4,376,589)</u>	<u>316,882</u>	<u>(41,598,184)</u>
Total capital assets being depreciated, net	<u>106,305,701</u>	<u>(3,233,374)</u>	<u>(10,408)</u>	<u>103,061,919</u>
Capital assets, net	<u>\$ 106,766,852</u>	<u>\$ (1,959,623)</u>	<u>\$ (1,500,912)</u>	<u>\$ 103,306,317</u>

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 4 - CAPITAL ASSETS (CONTINUED)

	2005			
	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets not being depreciated:				
Land	\$ 81,950	\$ 18,000	\$ -	\$ 99,950
Construction in progress	<u>53,246,672</u>	<u>5,662,296</u>	<u>(58,547,767)</u>	<u>361,201</u>
Total capital assets not being depreciated	<u>53,328,622</u>	<u>5,680,296</u>	<u>(58,547,767)</u>	<u>461,151</u>
Capital assets being depreciated:				
Buildings and system	40,611,758	34,798,425	(1,800)	75,408,383
Improvements other than buildings	21,989,583	242,086	-	22,231,669
Machinery and equipment	<u>25,313,008</u>	<u>21,416,238</u>	<u>(525,120)</u>	<u>46,204,126</u>
Total capital assets being depreciated	<u>87,914,349</u>	<u>56,456,749</u>	<u>(526,920)</u>	<u>143,844,178</u>
Less accumulated depreciation for:				
Buildings and system	(16,724,712)	(1,606,904)	1,800	(18,329,816)
Improvements other than buildings	(9,846,713)	(167,630)	-	(10,014,343)
Machinery and equipment	<u>(7,552,451)</u>	<u>(2,084,008)</u>	<u>442,141</u>	<u>(9,194,318)</u>
Total accumulated depreciation	<u>(34,123,876)</u>	<u>(3,858,542)</u>	<u>443,941</u>	<u>(37,538,477)</u>
Total capital assets being depreciated, net	<u>53,790,473</u>	<u>52,598,207</u>	<u>(82,979)</u>	<u>106,305,701</u>
Capital assets, net	<u>\$ 107,119,095</u>	<u>\$58,278,503</u>	<u>\$(58,630,746)</u>	<u>\$ 106,766,852</u>

NOTE 5 - LONG-TERM DEBT

Long-term debt activity for the years ended December 31, 2006 and 2005 was as follows:

	2006				
	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due in One Year</u>
Revenue Bonds:					
Bonds payable	\$1,030,000	\$ -	\$ 405,000	\$ 625,000	\$ 415,000
Clean Water Fund loans	<u>82,220,045</u>	<u>1,438,994</u>	<u>3,971,358</u>	<u>79,687,681</u>	<u>4,157,520</u>
Total revenue bonds	83,250,045	1,438,994	4,376,358	80,312,681	4,572,520
Compensated absences	<u>416,413</u>	<u>28,007</u>	<u>37,115</u>	<u>407,305</u>	<u>49,521</u>
Total long-term liabilities	<u>\$83,666,458</u>	<u>\$1,467,001</u>	<u>\$4,413,473</u>	<u>\$80,719,986</u>	<u>\$4,622,041</u>

RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005

NOTE 5 - LONG-TERM DEBT (CONTINUED)

	2005				
	Beginning Balance	Additions	Reductions	Ending Balance	Due in One Year
Revenue Bonds:					
Refunding revenue bond	\$1,420,000	\$ -	\$ 390,000	\$1,030,000	\$ 405,000
Clean Water Fund loans	<u>82,061,004</u>	<u>3,921,869</u>	<u>3,762,828</u>	<u>82,220,045</u>	<u>3,971,358</u>
Total revenue bonds	83,481,004	3,921,869	4,152,828	83,250,045	4,376,358
Compensated absences	<u>420,701</u>	<u>-</u>	<u>4,288</u>	<u>416,413</u>	<u>31,310</u>
 Total long-term liabilities	 <u>\$83,901,705</u>	 <u>\$3,921,869</u>	 <u>\$4,157,116</u>	 <u>\$83,666,458</u>	 <u>\$4,407,668</u>

	2006				
	Date of Issue	Final Maturity	Interest Range	Original Indebt- edness	Balance 12/31/06
Revenue Bonds					
Clean Water Fund loans	11/01/94	05/01/13	3.190%	\$2,701,745	\$1,186,495
Clean Water Fund loans	03/26/97	05/01/16	2.998%	1,158,993	690,159
Clean Water Fund loans	05/27/98	05/01/18	2.640%	854,147	564,696
Clean Water Fund loans	10/29/99	05/01/19	2.640%	797,249	569,077
Clean Water Fund loans	09/27/00	05/01/20	2.970%	805,113	610,855
Clean Water Fund loans	04/10/02	05/01/21	2.750%	4,073,012	3,402,168
Clean Water Fund loans	12/22/04	05/01/21	2.860%	17,943,748	15,916,427
Clean Water Fund loans	11/27/02	05/01/22	2.867%	60,724,848	56,747,804
Refunding Revenue Bond	11/05/04	12/15/08	2.5-3.0%	<u>1,420,000</u>	<u>625,000</u>
 Total revenue bonds				 <u>\$90,478,855</u>	 <u>\$80,312,681</u>

	2005				
	Date of Issue	Final Maturity	Interest Range	Original Indebt- edness	Balance 12/31/05
Revenue Bonds					
Clean Water Fund loans	11/01/94	05/01/13	3.190%	\$2,701,745	\$1,335,693
Clean Water Fund loans	03/26/97	05/01/16	2.998%	1,158,993	748,614
Clean Water Fund loans	05/27/98	05/01/18	2.640%	854,147	604,261
Clean Water Fund loans	10/29/99	05/01/19	2.640%	797,249	605,381
Clean Water Fund loans	09/27/00	05/01/20	2.970%	805,113	645,646
Clean Water Fund loans	04/10/02	05/01/21	2.750%	4,073,012	3,583,482
Clean Water Fund loans	12/22/04	05/01/21	2.860%	17,943,748	16,503,389
Clean Water Fund loans	11/27/02	05/01/22	2.867%	60,724,848	58,193,579
Refunding Revenue Bond	11/05/04	12/15/08	2.5-3.0%	<u>1,420,000</u>	<u>1,030,000</u>
 Total revenue bonds				 <u>\$ 90,478,855</u>	 <u>\$83,250,045</u>

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 5 - LONG-TERM DEBT (CONTINUED)

The debt service requirements for all debt outstanding as of December 31, 2006 is as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2007	\$ 4,572,520	\$ 2,241,414	\$ 6,813,934
2008	4,486,879	2,107,891	6,594,770
2009	4,399,666	1,977,039	6,376,705
2010	4,525,981	1,849,210	6,375,191
2011	4,655,926	1,717,099	6,373,025
2012-2016	24,769,318	7,508,925	32,278,243
2017-2021	27,336,356	2,783,612	30,119,968
2022	<u>5,566,035</u>	<u>79,746</u>	<u>5,645,781</u>
Total	<u>\$ 80,312,681</u>	<u>\$ 20,264,936</u>	<u>\$100,577,617</u>

There are a number of limitations and restrictions contained in the various bond indentures and loan agreements. The Utility believes it is in compliance with all significant limitations, restrictions, including federal arbitrage regulations.

NOTE 6 - NET ASSETS

The following is the detail of capital assets, net of related debt and restricted net assets.

	<u>2006</u>	<u>2005</u>
Invested in capital assets, net of related debt:		
Capital assets, net of accumulated depreciation	\$ 103,306,317	\$106,766,851
Less long-term debt outstanding	(80,312,681)	(83,250,045)
Plus non-capital debt proceeds	3,165,553	3,373,615
Plus unspent capital related debt proceeds	<u>425,395</u>	<u>427,165</u>
Total invested in capital assets net of related debt	<u>\$ 26,584,584</u>	<u>\$ 27,317,586</u>
Restricted net assets:		
Bond redemption fund	\$ 2,504,652	\$ 1,030,621
DNR replacement fund	2,960,182	2,973,406
Depreciation fund	<u>977,815</u>	<u>982,006</u>
Total restricted net assets	6,442,649	4,986,033
Less: accrued interest payable from restricted assets	<u>381,172</u>	<u>393,722</u>
Restricted net assets	<u>\$ 6,061,477</u>	<u>\$ 4,592,311</u>

Excluded from invested in capital assets, net of related debt, is \$3,165,553 and \$3,373,615 of revenue bonds that relates to financing of special projects that the Utility performs for the City of Racine for 2006 and 2005, respectively. These amounts are not used to finance Utility purchases of capital assets. Also excluded are reserve fund assets which were borrowed of \$425,395.

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 7 - EMPLOYEE RETIREMENT SYSTEM

The Wastewater Utility participates in the Wisconsin Retirement System ("WRS") as part of the City of Racine Group of employees. The Utility's contributions were \$249,921 and \$236,528 for 2006 and 2005, respectively. Information regarding the plan can be found in the City of Racine financial statements for the years ended December 31, 2006 and 2005. Information related solely to the Wastewater Utility is not available from WRS.

NOTE 8 - INTERFUND RECEIVABLES/PAYABLES

During 2006 and 2005, the Utility had the following interfund receivables and payables with affiliated entities:

	<u>2006</u>	<u>2005</u>
City of Racine		
Due from City of Racine - total	\$ 2,190,100	\$ 2,734,379
Due to City of Racine	(57,155)	(40,987)
Delinquent billings receivable - tax roll	1,289,607	1,107,341
Racine Water Utility		
Due from Water Utility	1,389,516	1,489,242
Due to Water Utility	(614,997)	(583,522)
Interfund Advances		
	<u>2006</u>	<u>2005</u>
Advance from City of Racine - total	\$ <u>(832,126)</u>	\$ <u>(853,125)</u>

The following repayment schedule has been established for advances made to the Racine Wastewater Utility for the Utility's percentage of the pension liability.

2007	\$ 66,204
2008	67,406
2009	68,466
2010	69,809
2011	70,885
2012-2016	374,810
2017-2021	412,075
2022-2023	<u>176,355</u>
Subtotal	1,306,010
Less amount representing interest	<u>473,884</u>
	832,126
Current portion	<u>22,838</u>
Long-term portion	<u>\$ 809,288</u>

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

NOTE 9 - RISK MANAGEMENT

The Utility is exposed to various risks of losses including general liability, property and casualty, workers' compensation, and employee health and accident. The Utility is involved in an intergovernmental insurance commission for general liability and auto insurance. There is a \$175,000 self-insured retention for each occurrence with this agreement. The Utility purchases commercial insurance for property and casualty claims.

The Utility participates in the City of Racine self-insurance plan for employee health insurance benefits. The plan is responsible for a specified amount of covered claims. Claims in excess of that amount are covered by purchased insurance. At December 31, 2006 and 2005, the Utility has accrued a liability of \$69,000 and \$47,000 respectively, to cover future claims.

In the ordinary course of conducting business, the Utility occasionally becomes involved in legal proceedings relating to contracts, environmental issues, or other matters. While any proceedings or litigation has an element of uncertainty, management of the Utility believes that the outcome of any pending or threatened actions will not have a material adverse effect on the business or financial condition of the Utility.

NOTE 10 - INTERGOVERNMENTAL SANITARY SEWER SERVICE AGREEMENT

The Racine Wastewater Utility entered into an intergovernmental sanitary sewer service agreement with the surrounding local municipalities. The agreement was reached to provide for an equitable allocation of the cost of the expansion of the existing sewer service facilities, which were necessary to continue providing high quality, reliable sewer service, and allow for future growth needs. The agreement allocates treatment capacity to each of the participating municipalities based on their future estimated usage. In return for such treatment capacity allocations each participating municipality is required to pay the Racine Wastewater Utility its proportionate share of the capital cost of improvements to be made.

The municipalities agreed to participate in a loan from the Clean Water Fund to pay for their share of the capital costs. As such, the agreement calls for each municipality to timely pay to the Racine Wastewater Utility its proportionate share of debt and any related debt service costs on a payment schedule approved by the Racine Wastewater Utility.

In 2005, the plant expansion was complete and the accounts receivable and deferred revenue were recognized for the plant capacity allocated to the participating municipalities in the amount of \$49,065,215.

Interest payments under the agreement are recorded as revenue when due. Principal payments are recorded as reductions of the accounts receivable - capacity rights account. The deferred revenue will be amortized on a straight-line basis over the term of the agreement. The capacity revenue recognized was \$1,043,940 and \$1,043,941 for the year ended December 31, 2006 and 2005 respectively.

The agreement also calls for revenue sharing payments to be made between participating municipalities based on current year's municipal budgets and the prior year's municipal populations and equalized valuations. The agreement requires the Racine Wastewater Utility to collect revenue sharing payments from the contributing municipalities and distribute them to recipient municipalities.

**RACINE WASTEWATER UTILITY
NOTES TO FINANCIAL STATEMENTS
December 31, 2006 and 2005**

**NOTE 10 - INTERGOVERNMENTAL SANITARY SEWER SERVICE
AGREEMENT (CONTINUED)**

The agreement also requires the Racine Wastewater Utility to make payments from its reserve accounts to the City of Racine with respect to the Racine Public Library, Racine Zoo, and the Charles A. Wustum Museum of Fine Arts which were determined to be regional cultural services and facilities which benefit the outlying parties. These payments in the amount of \$812,650 and \$973,055 for 2006 and 2005, respectively, are reported as transfers to other funds in the statement of revenues, expenses and changes in fund net assets.

NOTE 11 - INFILTRATION/INFLOW REMOVAL AGREEMENT

In 1994, the Utility entered into an agreement with the City of Racine to periodically replace the manholes and upgrade other structures to promote infiltration/inflow removal in the City of Racine. As part of the agreement, the Utility paid the construction cost for the manhole replacement and upgrades and was allowed to place a special charge on the bills of City residents to recover its costs. At December 31, 2006 and 2005 the Utility had unrecovered cost of \$2,171,304 and \$2,710,642, respectively, which was reported as due from the City of Racine.

NOTE 12 - LEASES

The Utility leases a parcel of land from the Racine Commercial Airport Corporation. The lease, which is for 50 years expiring in 2052, is classified as an operating lease. Lease payments are the greater of \$35,000 adjusted annually for inflation or half of the property taxes levied on the Airport's real property. Rent expense for the lease was \$39,062 and \$39,533 in 2006 and 2005, respectively.

Future minimum payments for the next five years under the lease:

2007	\$ 35,000
2008	35,000
2009	35,000
2010	35,000
2011	35,000
Thereafter	<u>1,400,000</u>
Total	<u>\$ 1,575,000</u>

NOTE 13 - MAJOR CUSTOMERS

One major customer accounted for 15% of gross sales aggregating \$1,860,447 and 13% of gross sales aggregating \$1,599,100 in 2006 and 2005, respectively.

This information is an integral part of the accompanying financial statements.

SUPPLEMENTAL INFORMATION

**RACINE WASTEWATER UTILITY
SCHEDULES OF OPERATING INCOME
Years Ended December 31, 2006 and 2005**

	<u>2006</u>	<u>2005</u>
OPERATING REVENUES		
Measured service to general customers		
Residential	\$ 4,104,432	\$ 4,672,648
Commercial	1,766,532	1,772,055
Industrial	633,475	774,636
Municipal	4,525,786	3,750,430
Public authorities	<u>1,175,263</u>	<u>1,117,359</u>
Total measured service to general customers	<u>12,205,488</u>	<u>12,087,128</u>
Other operating revenues		
Forfeited discounts	227,504	194,006
Other sewer revenues	<u>40,992</u>	<u>38,214</u>
Total operating revenues	<u>12,473,984</u>	<u>12,319,348</u>
 OPERATING EXPENSES		
Operation and maintenance expenses:		
Personnel services	2,408,264	2,334,150
Contractual services	2,241,043	2,211,051
Materials and supplies expense	478,462	437,898
Customer account expenses	462,115	456,630
Administrative and general	<u>1,626,740</u>	<u>1,323,073</u>
Total operation and maintenance expenses	<u>7,216,624</u>	<u>6,762,802</u>
Depreciation	4,376,589	3,858,542
Taxes	<u>180,760</u>	<u>182,272</u>
Total operating expenses	<u>11,773,973</u>	<u>10,803,616</u>
 OPERATING INCOME	 <u>\$ 700,011</u>	 <u>\$ 1,515,732</u>

RACINE WASTEWATER UTILITY
SCHEDULES OF OPERATION AND MAINTENANCE EXPENSES
Years Ended December 31, 2006 and 2005

	2006	2005
OPERATION AND MAINTENANCE EXPENSES		
Personnel services		
Salaries and wages	\$ 2,289,186	\$ 2,202,254
Overtime	94,849	102,246
Extra help	24,229	29,650
Total personnel services	2,408,264	2,334,150
Contractual services		
Professional services	142,496	269,439
Equipment repairs	208,820	181,726
Building repairs	6,013	9,449
Vehicle repairs	4,893	8,072
Telephone	10,350	9,538
Natural gas service	353,537	383,507
Electric services	655,231	524,650
Water and wastewater service	166,121	120,807
Sewer system repairs	13,599	17,573
Interceptor maintenance	41,943	61,449
Sludge and grit disposal	638,040	624,841
Total contractual services	2,241,043	2,211,051
Material and supplies		
Office supplies	12,523	11,317
Gasoline and diesel	26,219	20,875
Lubricants	17,601	16,349
Janitorial supplies	10,702	17,303
Operating chemicals	292,505	250,709
Plant and system supplies	58,585	68,771
Sewer maintenance supplies	3,852	1,330
Laboratory supplies	42,410	40,881
Computer supplies	14,065	10,363
Total material and supplies	478,462	437,898

RACINE WASTEWATER UTILITY
SCHEDULES OF OPERATION AND MAINTENANCE EXPENSES
(concluded)
Years Ended December 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Customer account expense		
Meter operations	\$ 100,421	\$ 80,856
Meter maintenance	25,891	29,211
Meter reading	57,187	59,397
Customer records and collections	116,883	128,824
Depreciation on meters	96,310	92,471
Return on meter investment	<u>65,423</u>	<u>65,871</u>
Total customer account expense	<u>462,115</u>	<u>456,630</u>
Administrative and general		
Dues, publications and subscriptions	34,934	29,743
Property and liability insurance	70,780	79,862
Workers compensation insurance	71,956	89,854
Office rent	22,290	21,281
Wisconsin retirement	249,921	236,528
Medical expenses	862,548	553,907
Life insurance	18,469	17,657
Safety programs	3,177	2,586
City departmental charges	68,049	66,067
DNR permit fee	157,758	164,367
Airport lease	39,062	39,533
Training programs	10,944	11,100
Stormwater fees	<u>16,852</u>	<u>10,588</u>
Total administrative and general	<u>1,626,740</u>	<u>1,323,073</u>
TOTAL OPERATION AND MAINTENANCE EXPENSE	<u>\$ 7,216,624</u>	<u>\$ 6,762,802</u>