

**CITY OF PROVIDENCE, RHODE ISLAND**  
**WATER SUPPLY BOARD**

FINANCIAL STATEMENTS  
FOR THE FISCAL YEARS ENDED  
JUNE 30, 2011 AND 2010

**CITY OF PROVIDENCE, RHODE ISLAND**  
**WATER SUPPLY BOARD**

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**YEARS ENDED JUNE 30, 2011 AND 2010**

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**REPORT OF INDEPENDENT AUDITORS**

To the Board of Directors of  
Providence Water Supply Board  
Providence, Rhode Island

We have audited the accompanying statements of net assets of the Providence Water Supply Board (the "Water Supply Board") (an enterprise fund of the City of Providence, Rhode Island) as of June 30, 2011 and 2010, and the related statements of revenues and expenses and changes in fund net assets and cash flows for the years then ended. These financial statements are the responsibility of the Water Supply Board'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 provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Water Supply Board and do not purport to, and do not, present fairly the financial position of the City of Providence, Rhode Island, as of June 30, 2011 and 2010, and the changes in its financial position, or, where applicable its cash flows 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 Water Supply Board as of June 30, 2011 and 2010, and the respective changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with "Government Auditing Standards", we have also issued our report dated December 21, 2011 on our consideration of the Water Supply Board's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with "Government Auditing Standards", and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 2 through 5 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting in an appropriate operational, economic, or historical context. We have applied certain limited procedures, to the required supplementary information in accordance with accounting standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

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Providence



**PROVIDENCE WATER SUPPLY BOARD**  
***(An enterprise fund of the City of Providence, Rhode Island)***

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**JUNE 30, 2011 AND 2010**

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The management of the Providence Water Supply Board (the "Water Supply Board") offers readers of our financial statements the following narrative overview and analysis of our financial activities for the years ended June 30, 2011 and 2010.

**Financial Statements**

Our financial statements are prepared using proprietary fund (enterprise fund) accounting that uses the same basis of accounting as private-sector business enterprises. Under this method of accounting an economic resources measurement focus and the accrual basis of accounting is used.

Revenue is recorded when earned and expenses are recorded when incurred. The financial statements include statements of net assets, statements of revenues, expenses and changes in net assets, and statements of cash flows. These statements are followed by notes to the financial statements.

- The statements of net assets present information on the assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Water Supply Board is improving or deteriorating.
- The statements of revenues, expenses, and changes in net assets report the operating and non-operating revenues and expenses of the Water Supply Board for the fiscal year with the difference – the net income or loss – being combined with any capital contributions to determine the net change in assets for the fiscal year. That change combined with the previous year-end net assets total reconciles to the net assets at the end of the fiscal year.
- The statements of cash flows report cash and cash equivalents activity for the fiscal year resulting from operating activities, non-capital financing activities, capital and related financing activities, and investing activities. The net result of these activities added to the beginning of the year cash balance reconciles to the cash and cash equivalents balance at the end of the fiscal year.

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**PROVIDENCE WATER SUPPLY BOARD**  
*(An enterprise fund of the City of Providence, Rhode Island)*

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**JUNE 30, 2011 AND 2010**

**Condensed Financial Information (in thousands)**

Condensed financial information from the statements of net assets and revenues, expenses, and changes in net assets is presented below.

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Current assets	\$ 40,695	\$ 49,147	\$ 60,976
Capital assets, net	254,291	235,100	204,233
<b>Total assets</b>	<u>294,986</u>	<u>284,247</u>	<u>265,209</u>
Current liabilities	12,780	17,235	12,450
Noncurrent liabilities	51,896	53,780	43,465
<b>Total liabilities</b>	<u>64,676</u>	<u>71,015</u>	<u>55,915</u>
Net assets:			
Invested in capital assets, net of related debt	201,281	179,800	159,670
Restricted	18,028	28,395	43,780
Unrestricted	11,001	5,037	5,844
<b>Total net assets</b>	<u>\$ 230,310</u>	<u>\$ 213,232</u>	<u>\$ 209,294</u>
Operating revenues	<u>\$ 64,017</u>	<u>\$ 54,976</u>	<u>\$ 59,575</u>
Operating expenses	34,674	39,447	38,150
Depreciation	<u>11,380</u>	<u>11,421</u>	<u>10,646</u>
<b>Total operating expenses, including depreciation</b>	<u>46,054</u>	<u>50,868</u>	<u>48,796</u>
<b>Operating income</b>	17,963	4,108	10,779
Nonoperating expense	(1,395)	(943)	(1,813)
Capital grants and contributions	<u>510</u>	<u>773</u>	<u>775</u>
<b>Increase in net assets</b>	<u>\$ 17,078</u>	<u>\$ 3,938</u>	<u>\$ 9,741</u>

(CONTINUED)

**PROVIDENCE WATER SUPPLY BOARD**  
*(An enterprise fund of the City of Providence, Rhode Island)*

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**JUNE 30, 2011 AND 2010**

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**Financial Highlights**

The Water Supply Board's net assets totaled \$ 230 million at June 30, 2011. Total net assets increased by \$17 million, or about 8% from June 30, 2010.

During the year, the Water Supply Board had operating revenues that exceeded operating expenses by \$18 million. This is primarily due to the large commitment to the replacement of infrastructure included in water rates.

At June 30, 2011, the Water Supply Board's net assets totaled \$ 230 million. Total assets were \$295 million, up \$ 10.8 million from last year's total assets of \$ 284.2 million.

At June 30, 2010, the Water Supply Board's net assets totaled \$ 213 million. Total assets were \$284.2 million, up \$ 19 million from the prior year's total assets of \$ 265.2 million.

The Water Supply Board's total operating revenues were \$64 million at June 30, 2011, which increased from \$54.9 million at June 30, 2010. The total cost of operating the water system, including property taxes and depreciation, was \$46 million. This resulted in an operating income of \$18 million. Non-operating revenue consists of interest and dividend income. Interest on long-term restricted debt is the largest non-operating expense, followed by miscellaneous and other expenses. Non-operating income for the fiscal year totaled (\$1.4) million, with capital grants of \$.5 million. The total increase in net assets was \$17.1 million.

The increase in revenue in 2011 was attributable to an across the board increase in rates that was in place for all of 2011. The decrease in expenditures in 2011 was a result of negotiated adjustments to salaries, the reduction of some benefits, a reduction in property taxes and a reduction of bad debt expense.

The Water Supply Board's total operating revenues were \$ 55 million at June 30, 2010, which decreased from \$59.6 million at June 30, 2009. The total cost of operating the water system, including property taxes and depreciation, was \$ 50.9 million. This resulted in an operating income of \$ 4.1 million. Non-operating revenue consists of interest and dividend income. Interest on long-term restricted debt is the largest non-operating expense, followed by miscellaneous and other expenses. Non-operating income for the fiscal year totaled (\$.9) million, with capital grants of \$ .8 million. The total increase in net assets was \$ 4 million.

The decrease in revenue in 2010 was attributable to the one time revenue in 2009 that did not re-occur in 2010. The increase in expenditures in 2010 was a result of normal inflation, contractual and external factors.

**Capital Assets and Debt Administration**

**Capital Assets**

At June 30, 2011, the Water Supply Board had \$ 254.2 million invested in various capital assets, including land, buildings and improvements, transmission and distribution reservoirs, mains, services, hydrants and appurtenances, machinery and equipment and construction work in progress. This amount represents a net increase of \$ 19.2 million, or 8.2%, over last year.

At June 30, 2010, the Water Supply Board had \$ 235.1 million invested in various capital assets, including land, buildings and improvements, transmission and distribution reservoirs, mains, services, hydrants and appurtenances, machinery and equipment and construction work in progress. This amount represents a net increase of \$ 30.9 million, or 15.1%, over the prior year.

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**PROVIDENCE WATER SUPPLY BOARD**  
*(An enterprise fund of the City of Providence, Rhode Island)*

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**JUNE 30, 2011 AND 2010**

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**Major project expenditures included (in millions):**

- Various distribution improvements, \$0.1
- Replace valves, \$0.2
- Replace fire hydrants, \$0.4
- Valve & Hydrant Assessment, \$0.5
- Replace lead services, \$6.7
- Sludge Maintenance, \$1.0
- Geographic Info. Systems (GIS), \$0.1
- Replace water mains, \$8.6
- 102" aqueduct improvements, \$1.5
- Sand Filters, \$6.8
- Access Roads, fencing and security, \$0.3
- Electrical and process control upgrades, \$0.1
- Storage facilities, \$0.1
- CO<sup>2</sup> system, \$2.8
- Mlog Leak Detection system, \$0.5
- Source Water Improvements, \$0.3

The Water Supply Board's fiscal 2012 capital budget includes projected expenditures of \$28 million for infrastructure and capital projects. The major projects are filter replacements, pump station upgrades, sludge removal and disposal, Source Water Improvements and Treatment Plant system upgrades, meter, lead service and water main replacements, transmission main inspection and rehabilitation, valve and hydrant maintenance, GIS system, Mlog installation and land acquisition. Other projects will be funded from bond proceeds available from bonds issued in prior fiscal years and with restricted cash funding from rate revenues. The majority of infrastructure projects are financed on a pay-as-you-go, cash basis. New capital additions, that benefit the ratepayers for many years, are paid for with debt financing on an as needed basis.

**Debt**

At June 30, 2011, the Water Supply Board had \$ 53 million in bonds and notes outstanding versus \$ 55.3 million in the previous year. This represented a decrease of \$ 2.3 million or 4.2%. The 1996 PPBA bond was refinanced in November 2010. No additional debt was issued in 2011.

At June 30, 2010, the Water Supply Board had \$ 55.3 million in bonds and notes outstanding versus \$ 43.6 million in the previous year. This represented an increase of \$ 11.7 million or 26.8%.

\$ 13.25 million in new debt was issued in 2010 to fund water main replacements, meters and electronic radio transmitters, hydrant locks and Mlog leak detection devices.

**Contacting Providence Water's Financial Management**

This financial report is designed to provide our customers, investors and creditors with a general overview of the Water Supply Board's finances and to show the Water Supply Board's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Finance Director at the Providence Water Supply Board, 552 Academy Avenue, Providence, RI 02908.

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**PROVIDENCE WATER SUPPLY BOARD**  
**(An enterprise fund of the City of Providence, Rhode Island)**

**STATEMENT OF NET ASSETS**  
**JUNE 30, 2011 AND 2010 (000's)**

	2011	2010
<b>ASSETS</b>		
<b>Current unrestricted assets</b>		
Cash and cash equivalents (Note 3)	\$ 3,948	\$ 2,811
Accounts receivable, net of allowance for uncollectible accounts of \$2,378 in 2011 and \$3,122 in 2010	9,257	7,653
Accounts receivable - unbilled	4,752	3,319
Inventory	711	851
Other assets	487	523
<b>Total current unrestricted assets</b>	19,155	15,157
 <b>Current restricted assets (Note 2)</b>		
Cash and cash equivalents (Note 3)	17,215	27,844
Investments (Note 3)	4,304	4,303
Accounts receivable	21	547
Due from City of Providence General Fund (Note 6)	-	1,296
<b>Total current restricted assets</b>	21,540	33,990
<b>Total current assets</b>	40,695	49,147
 <b>Capital Assets (Note 9)</b>		
Land	19,305	13,574
Building and improvements	55,263	48,637
Improvements other than buildings	225,819	217,731
Machinery and equipment	27,239	26,554
Assets under capital leases (Note 7)	13,846	13,846
Scituate Reservoir Project	18,682	18,682
Construction in progress	52,543	43,102
	412,697	382,126
Less accumulated depreciation and amortization	158,406	147,026
<b>Total capital assets, net</b>	254,291	235,100
<b>Total assets</b>	294,986	284,247

(CONTINUED)

The accompanying notes are an integral part of these financial statements.

**PROVIDENCE WATER SUPPLY BOARD**  
*(An enterprise fund of the City of Providence, Rhode Island)*

**STATEMENT OF NET ASSETS**  
**JUNE 30, 2011 AND 2010 (000's)**

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	<u>2011</u>	<u>2010</u>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Due to City of Providence General Fund (Note 6)	544	315
Accounts payable	1,021	1,674
Accrued expenses	2,216	4,837
Unearned revenues	1,966	1,945
Current portion of long-term debt (Note 5)	3,521	2,869
	<u>9,268</u>	<u>11,640</u>
 <b>Amounts to be paid from current restricted assets (Note 2)</b>		
Due to Water Resources Board	347	354
Accounts payable	3,165	5,241
	<u>3,512</u>	<u>5,595</u>
 <b>Total current liabilities</b>	 <u>12,780</u>	 <u>17,235</u>
 <b>Non-current liabilities</b>		
General revenue bonds (Note 5)	49,489	52,430
Other post employment benefits (Note 10)	2,407	1,350
<b>Total non-current liabilities</b>	<u>51,896</u>	<u>53,780</u>
 <b>Total liabilities</b>	 <u>64,676</u>	 <u>71,015</u>
 <b>NET ASSETS</b>		
Invested in capital assets, net of related debt	201,281	179,800
Restricted	18,028	28,395
Unrestricted	11,001	5,037
 <b>Total net assets</b>	 <u>\$ 230,310</u>	 <u>\$ 213,232</u>

(CONCLUDED)

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The accompanying notes are an integral part of these financial statements.

**PROVIDENCE WATER SUPPLY BOARD**  
 (An enterprise fund of the City of Providence, Rhode Island)

**STATEMENTS OF REVENUES AND EXPENSES AND CHANGES IN FUND NET ASSETS  
 FOR THE YEARS ENDED JUNE 30, 2011 AND 2010 (000's)**

	<u>2011</u>	<u>2010</u>
<b>Operating Revenues</b>		
Charges for services:		
Water sales (Note 1):		
General customers	\$ 42,266	\$ 36,362
Other local water suppliers	17,301	14,294
Fire protection services	2,060	1,815
Maintenance charges and other revenue	2,390	2,505
<b>Total operating revenues</b>	<u>64,017</u>	<u>54,976</u>
 <b>Operating Expenses</b>		
Source of supply	2,183	2,322
Pumping operations	871	780
Water treatment	6,038	7,829
Transmission and distribution	3,578	5,149
Charge for services provided by other City departments (Note 6)	839	839
Customer accounts and service	2,829	2,712
Administrative and general	12,080	13,122
Depreciation and amortization	11,380	11,421
Property taxes - other local governments	6,256	6,694
<b>Total operating expenses</b>	<u>46,054</u>	<u>50,868</u>
 <b>Operating income</b>	<u>17,963</u>	<u>4,108</u>
 <b>Nonoperating Revenues (Expenses)</b>		
Interest income	34	492
Interest expense and other	(1,429)	(1,435)
<b>Net nonoperating expenses</b>	<u>(1,395)</u>	<u>(943)</u>
 <b>Capital Grants and Contributions</b>	<u>510</u>	<u>773</u>
 <b>Change in net assets</b>	17,078	3,938
 <b>Net Assets, beginning of year</b>	<u>213,232</u>	<u>209,294</u>
 <b>Net Assets, end of year</b>	<u>\$ 230,310</u>	<u>\$ 213,232</u>

The accompanying notes are an integral part of these financial statements.



**PROVIDENCE WATER SUPPLY BOARD**  
*(An enterprise fund of the City of Providence, Rhode Island)*

**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED JUNE 30, 2011 AND 2010 (000's)**

	2011	2010
<b>Cash Flows From Operating Activities</b>		
Cash received from customers	\$ 61,563	\$ 54,665
Cash paid to vendors	(26,058)	(20,412)
Cash paid to employees	(12,776)	(13,334)
<b>Net cash provided by operating activities</b>	<b>22,729</b>	<b>20,919</b>
 <b>Cash Flows From Non-Capital and Related Financing Activities</b>		
Due to/from other funds	1,525	(3,048)
 <b>Cash Flows From Capital and Related Financing Activities</b>		
Acquisition and construction of capital assets	(30,571)	(42,288)
Interest paid on debt	(1,429)	(1,435)
Repayment of long-term debt	(3,345)	(2,513)
Proceeds from long-term debt	1,056	21,364
Capital grants	510	773
<b>Net cash used in capital and related financing activities</b>	<b>(33,779)</b>	<b>(24,099)</b>
 <b>Cash Flows From Investing Activities</b>		
Purchase of investment securities	(1)	(3,094)
Investment income (loss)	34	492
<b>Net cash provided by (used in) investing activities</b>	<b>33</b>	<b>(2,602)</b>
 <b>Net decrease in cash and cash equivalents</b>	<b>(9,492)</b>	<b>(8,830)</b>
 <b>Cash and cash equivalents</b>		
Beginning	30,655	39,485
Ending	<b>\$ 21,163</b>	<b>\$ 30,655</b>
 Unrestricted cash and cash equivalents	\$ 3,948	\$ 2,811
Restricted cash and cash equivalents	17,215	27,844
	<b>\$ 21,163</b>	<b>\$ 30,655</b>
 <b>Reconciliation of Operating Income to</b>		
<b>Net Cash Provided by Operating Activities:</b>		
Operating income	\$ 17,963	\$ 4,108
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	11,380	11,421
Changes in assets and liabilities:		
Accounts receivable	(2,511)	(210)
Inventories	140	(372)
Other assets	36	(143)
Accounts payable and accrued expenses	(4,300)	6,073
Unearned revenue	21	42
<b>Net cash provided by operating activities</b>	<b>\$ 22,729</b>	<b>\$ 20,919</b>

The accompanying notes are an integral part of these financial statements.

**PROVIDENCE WATER SUPPLY BOARD**  
***(An enterprise fund of the City of Providence, Rhode Island)***

**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2011 AND 2010 (000's)**

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**1. NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES**

Reporting entity

The Providence Water Supply Board, an enterprise fund of the City of Providence, (the "Water Supply Board") was created in 1940 by Chapter 832 of the Public Laws of the State of Rhode Island. Membership of the Water Supply Board is comprised of four persons appointed by the Mayor, who serve for four-year staggered terms and two City Council members elected by the City Council who serve during their four-year City Council term. The Finance Director of the City of Providence also serves as an ex-officio Water Supply Board member.

The Water Supply Board provides water supply services through metered sales in Providence and parts of the surrounding communities of North Providence, Johnston and Cranston. The Water Supply Board also sells water to other local water supply systems on a wholesale basis. The Water Supply Board's source of water supply is the Scituate Reservoir, located in the Town of Scituate, Rhode Island, and five tributary reservoirs.

Significant accounting policies are as follows:

Basis of Presentation

The Water Supply Board is considered an enterprise fund of the City of Providence (the "City"). The operations of the Water Supply Board are accounted for with a separate set of self-balancing accounts organized on a Proprietary Fund type (Enterprise Fund) basis.

Enterprise Funds are used to account for operations (a) that are financed and operated in a manner similar to private business enterprises where the intent of the governing body is that the costs (including depreciation) of providing goods and services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

The Water Supply Board utilizes the accrual basis of accounting, under which revenues are recognized when earned and expenses are recognized when incurred.

Regulations and Operation

The Water Supply Board is subject, as to rates, and other matters, to the regulatory authority of the State of Rhode Island Public Utilities Commission (PUC).

Cash equivalents

The Water Supply Board considers all highly liquid debt instruments with an original maturity of three months or less, when purchased, to be cash equivalents.

Investments

The Water Supply Board accounts for investments at fair values which are established by quoted market prices.

Inventory

Inventory, consisting of materials and supplies, is valued at the lower of average cost or market using the first-in, first-out method.

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**PROVIDENCE WATER SUPPLY BOARD**  
*(An enterprise fund of the City of Providence, Rhode Island)*

**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2011 AND 2010 (000's)**

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**1. NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

Capital assets, depreciation and amortization

Capital assets owned by the Water Supply Board are stated at cost. They are defined as assets with an initial cost of more than \$3,000 and an estimated useful life in excess of 1 year. Depreciation and amortization is provided over the estimated useful lives using the straight-line method. The estimated useful lives are as follows:

Building, source of supply structures, and improvements	5-75 years
Improvements other than buildings	3-75 years
Equipment	3-50 years

Depreciation expense is not reflected for construction in progress until such time as it is placed in service. Assets under capital leases are amortized under the Water Supply Board's normal depreciation policies for similar assets.

Restricted funds for construction of assets

Restricted funds for construction of assets represent unexpended revenue bond proceeds obtained specifically for construction of water facilities. These funds are included in restricted assets.

Capital contributions

Capital contributions consist of property and equipment paid for by customers for water installations. Once the installation is complete, the property and equipment transfers to the Water Supply Board at fair value.

Revenues, operating revenues and expenses

Revenues include amounts billed and unbilled to all customers, including those customers outside the City of Providence, Rhode Island. All billed charges are based on rates approved by the PUC. Revenues for unbilled amounts to general customers are estimated based on billing amounts subsequent to year-end. The Water Supply Board distinguishes operating revenues and expenses from non-operating. Operating revenues result from charges to customers for water and related services. Operating expenses include the cost of operations, maintenance, sales and service, administrative expenses and depreciation. All revenues and expenses not meeting this definition are reported as non-operating or capital contributions.

Proprietary fund accounting

The Water Supply Board has implemented Statement No. 20 of the Governmental Accounting Standards Board (GASB), "Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting." This Statement provides guidance on the applicability of accounting pronouncements from other standard setting organizations. Under the Board's election, it must apply all GASB pronouncements and the following pronouncements issued before November 30, 1989 unless they contradict GASB pronouncements: Statements and Interpretations of the Financial Accounting Standards Board, Accounting Principles Board Opinions, and Accounting Research Bulletins of the committee on Accounting Procedures.

Concentration of credit risk

The Water Supply Board's financial instruments that are exposed to concentrations of credit risk consist primarily of accounts receivable. Exposure to losses on receivables is principally dependent on each customer's financial condition. Concentration of credit risk with respect to receivables is limited due to the large number of customers. The Water Supply Board monitors its exposure for credit losses and maintains allowances for anticipated losses.

(CONTINUED)



**PROVIDENCE WATER SUPPLY BOARD**  
**(An enterprise fund of the City of Providence, Rhode Island)**

**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2011 AND 2010 (000's)**

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**1. NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

Use of estimates

The preparation of the financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of 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.

Compensated absences

Employees accumulate sick leave hours for subsequent use or for payment upon retirement. Sick leave and vacation vest and may be carried forward into the following calendar year, but not to exceed 135 days and 30 days, respectively.

Vested sick leave and accumulated vacation leave are recorded as expenses and liabilities as the benefits accrue to employees.

**2. RESTRICTED ASSETS**

The State of Rhode Island enacted the Public Drinking Water Protection Act of 1987 (the "Act") that empowers suppliers of public drinking water to levy a surcharge (the "surcharge") on one cent (\$0.01) per hundred gallons of water for all customers. The surcharge has been amended several times since 1987. The last increase was on July 1, 2002, when the surcharge increased to \$0.0292 per hundred gallons of water for all customers. In addition to the increase, the Water Supply Board will retain 36.1% of the surcharge in its Water Quality Protection fund, remit 57.0% to the State Water Resources Board and retain 6.9% for general operations. The funds collected in the Water Quality Protection fund are to be expended in the following manner:

- 1) at a minimum, 55% of the funds are to be spent for the acquisition of land or land rights or physical improvements to acquired land to protect the quality of the raw water of the water supply system;
- 2) 35% may be used to acquire a fee simple interest or a conservation restriction that directly protects the quality and safety of the public drinking water supply; and 3) 10% may be used by the supplier for any purpose relating to its operations.

The restricted investments are pooled with the cash and cash equivalents and investments of other funds maintained by the City of Providence. The earnings from investments are allocated in proportion to each fund's balance.

**3. CASH AND INVESTMENTS**

The following is a summary of cash and investments:

	Fair Value
Cash and cash equivalents	\$ 3,948
Restricted cash and cash equivalents	17,215
Equity Mutual Funds	4,304
Total	<u>\$ 25,467</u>

(CONTINUED)

**PROVIDENCE WATER SUPPLY BOARD**  
**(An enterprise fund of the City of Providence, Rhode Island)**

**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2011 AND 2010 (000's)**

**3. CASH AND INVESTMENTS (CONTINUED)**

Responsibility for custodial credit risk of deposits and investments and interest rate risk and risk and concentration of investments rests with the City; accordingly separate disclosure is not possible. The City's financial statements should be read to determine the associated risks of the Water Supply Board's deposits and investments.

**4. PENSION PLANS**

Substantially all employees of the Water Supply Board participate in the Employees' Retirement System of the City of Providence (the "Plan"), a defined-benefit, single-employer plan. Disclosures about this plan, as a whole, are presented in the City of Providence, Rhode Island's basic financial statements. As of June 30, 2011 and 2010, the City recorded a liability for unpaid pension contributions of \$136,115 and \$132,767, respectively. Separate actuarial information related to the Water Supply Board employees is not available. Accordingly, only disclosures about the Water Supply Board's participation in the Plan are presented herein.

Water Supply Board employees participating in the Plan are eligible to retire at age 55 if hired prior to July 1, 2004, at age 60 if hired between July 1, 2004 and June 30, 2009, at age 62 with 10 years of service if hired on or after July 1, 2009 or at any age after 25 years of service if hired prior to July 1, 1995, or at any age after 30 years of service if hired on or after July 1, 1995. The total retirement allowance is equal to an annuity, which is the actuarial equivalent of accumulated contributions at the time of retirement, plus a pension which when added together either; 1) equals 1/40 of final compensation for each year of total service up to 20 years and 1/50 of final compensation for each year of service in excess of 20 years if hired prior to July 1, 1996 or; 2) equals 1/50 of final compensation for each year of total service credited if hired on or after July 1, 1996. These benefit provisions and all other requirements are established by City ordinance.

The Water Supply Board's allocation of the actuarial required contribution and amount contributed for the year ended June 30, 2011 were \$2,589 and \$1,624, respectively. The Water Supply Board's allocation of the actuarial required contribution and amount contributed for the year ended June 30, 2010 were \$2,235 and \$2,788, respectively. The overpayment of \$553 for the year ended June 30, 2010 and overpayments totaling \$412 for previous years were applied in 2011. The employer and employees contribution rates are approximately 25% and 23%, respectively, for both 2011 and 2010.

The historical schedules of employer contributions and funding progress for the Plan are included in the City of Providence, Rhode Island's basic financial statements.

**5. LONG-TERM DEBT**

Long-term liability activity for the years ended June 30, 2011 and 2010 were as follows:

	2011				
	Beginning Balance	Increases	Decreases	Ending Balance	Due Within One Year
Bonds payable:					
Revenue bonds	\$ 55,299	\$ 1,056	\$ (3,345)	\$ 53,010	\$ 3,521
Total bonds	55,299	1,056	(3,345)	53,010	3,521
Total long-term liabilities	\$ 55,299	\$ 1,056	\$ (3,345)	\$ 53,010	\$ 3,521

(CONTINUED)



**PROVIDENCE WATER SUPPLY BOARD**  
 (An enterprise fund of the City of Providence, Rhode Island)

**NOTES TO FINANCIAL STATEMENTS**  
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**5. LONG-TERM DEBT (CONTINUED)**

	2010				
	Beginning Balance	Increases	Decreases	Ending Balance	Due Within One Year
Bonds payable:					
Revenue bonds	\$ 43,572	\$ 13,250	\$ (1,523)	\$ 55,299	\$ 2,869
Total bonds	43,572	13,250	(1,523)	55,299	2,869
Total long-term liabilities	\$ 43,572	\$ 13,250	\$ (1,523)	\$ 55,299	\$ 2,869

The following is a summary of bonds and notes outstanding at June 30, 2011 and 2010:

Description	June 30, 2011	
	Interest Rate	Balance
Revenue bonds:		
Safe Drinking Water Bonds (CWFA FY2002)	2.97%	\$ 1,563
Scituate Reservoir Project (PPBA FY 2011)	5.42%	996
Safe Drinking Water Bonds (CWFA FY2005)	2.25%	3,500
Safe Drinking Water Bonds (CWFA FY2008)	2.85%	33,702
Safe Drinking Water Bonds (CWFA FY2010)	2.21%	13,249
		\$ 53,010

Description	June 30, 2010	
	Interest Rate	Balance
Revenue bonds:		
Safe Drinking Water Bonds (CWFA FY2002)	2.97%	\$ 1,678
Scituate Reservoir Project (PPBA 1996)	5.40%	1,057
Safe Drinking Water Bonds (CWFA FY2005)	2.25%	4,314
Safe Drinking Water Bonds (CWFA FY2008)	2.85%	35,000
Safe Drinking Water Bonds (CWFA FY2010)	2.21%	13,250
		\$ 55,299

(CONTINUED)



**PROVIDENCE WATER SUPPLY BOARD**  
*(An enterprise fund of the City of Providence, Rhode Island)*

**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2011 AND 2010 (000's)**

**5. LONG-TERM DEBT (CONTINUED)**

Scheduled principal maturities of long-term debt are as follows:

Fiscal year ending June 30:	ARRA Principal			
	Principal	Forgiveness	Interest	Total
2012	\$ 3,521	\$ (260)	\$ 1,403	\$ 4,664
2013	3,601	(263)	1,437	4,775
2014	3,691	(268)	1,384	4,807
2015	3,790	(273)	1,293	4,810
2016	2,953	(279)	1,210	3,884
20167-2021	11,328	(486)	5,059	15,901
2022-2026	12,204	(569)	3,166	14,801
2027-2031	11,922	(424)	908	12,406
	<u>\$ 53,010</u>	<u>\$ (2,822)</u>	<u>\$ 15,860</u>	<u>\$ 66,048</u>

**In-Substance Defeasance Prior-Years**

In prior years, the Water Supply Board has defeased various bond issues by creating separate irrevocable trust funds. New debt has been issued and the proceeds have been used to purchase U.S. government securities that were placed in the trust funds. The investments and fixed earnings from the investments are sufficient to fully service the defeased debt until the debt is called or matures. For financial reporting purposes, the debt has been considered defeased and therefore removed as a liability from the financial statements. As of June 30, 2011, the amount of defeased debt outstanding but removed from the Water Supply Board's statements was \$3,710.

**6. TRANSACTIONS WITH CITY OF PROVIDENCE, RHODE ISLAND**

The City of Providence performs various services for the Water Supply Board including certain accounting, personnel and cash management services and working capital support. The total billing to the Water Supply Board for services performed amounted to \$839 for each of the years ended June 30, 2011 and 2010, respectively. This amount is established by the City, approved by the Water Supply Board and ultimately approved by the PUC. The Water Supply Board also provides services to various City funds and departments, the charges for which have been included as revenue in the accompanying financial statements. Included within the Due To City of Providence General Fund balance on the statement of net assets are the related balances due for these services, pension and post employment benefit payments which at June 30, 2011 and 2010 totaled \$544 and \$315, respectively. Included within the Due From City of Providence General Fund balance on the statement of net assets at June 30, 2010 are \$1,296 of depreciation funds that were transferred by the City in error and returned after the end of the year.

(CONTINUED)

**PROVIDENCE WATER SUPPLY BOARD**  
***(An enterprise fund of the City of Providence, Rhode Island)***

**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2011 AND 2010 (000's)**

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**7. LEASES**

The assets and liabilities under all capital leases are recorded at the present value of the minimum lease payments. Amortization of these assets charged to expense amounted to \$185 for each of the years ended June 30, 2011 and 2010. Summary of book value is as follows:

	<u>2011</u>	<u>2010</u>
Cost	\$ 13,846	\$ 13,846
Accumulated amortization	<u>(3,437)</u>	<u>(3,253)</u>
Book value	<u>\$ 10,409</u>	<u>\$ 10,593</u>

**8. COMMITMENTS AND CONTINGENCIES**

Risk Management

The Water Supply Board has a complete comprehensive insurance program protecting all facilities, employees and liability claims.

The Water Supply Board is subject to various claims and litigation that arise in the ordinary course of its operations. Legal counsel and management are of the opinion that the Water Supply Board's liabilities in such cases, if decided adversely to the Water Supply Board, would not materially affect the financial statements.

Union Contract

The labor force of the Water Supply Board, with the exception of management, is covered by a union contract which is effective for the period January 1, 2011 to June 30, 2015.

Contingent Liability to City of Providence per Rhode Island G.L.

A law passed in 2003 (R.I.G.L. § 39-3-11.3 and § 46-15.3-21) required an annual payment by the Water Supply Board to the City of Providence of 5% of the Board's gross revenues for the fiscal years ending June 30, 2004, 2005 and 2006. The law specifically provides that this payment shall not be included as part of the Water Supply Board's rates for these years. These payments would total approximately \$2,500 per year.

The Water Supply Board has no material funds (other than revenues from rates) from which to make these payments and therefore has not made the payments. Further, since the payments can not be made from rate revenues the Board believes it is not liable for any amount to the City and therefore has not accrued an amount for the potential liability.

No action has been taken by either the City of Providence or the Rhode Island Public Utilities Commission concerning this matter.

(CONTINUED)



**PROVIDENCE WATER SUPPLY BOARD**  
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**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2011 AND 2010 (000's)**

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**8. COMMITMENTS AND CONTINGENCIES (CONTINUED)**

Lead Service Replacement Program

The Water Supply Board is required to test for lead and copper in its water. In August 2006, 16 of 100 samples taken throughout the water system tested for trace lead levels higher than 15 parts per billion (ppb). The U.S. Environmental Protection Agency (EPA) regulations mandate specific actions that need to be taken by water utilities when more than 10% of test samples exceed the 15 ppb lead level. While there is no detectable lead in the drinking water that leaves the Water Supply Board's treatment plant, some older homes with lead pipes and lead connections to the water main in the street can show trace amounts of lead in the water.

Due to the results of the testing, the Water Supply Board was required by the U.S EPA, through the Rhode Island Department of Health (RIDOH), to engage in public education efforts related to lead in water, and to replace a minimum of 7% (1,800 services) of the 25,600 active lead services in its system by September 30, 2007, and 7% each year thereafter. The Water Supply Board entered into a consent agreement with RIDOH to replace 14% of its active lead services by September 30, 2008, and to then continue on with a minimum of 7% in each ensuing year.

In July 2007, the Water Supply Board embarked on a Lead Service Replacement (LSR) program and engaged an engineering firm for a period of three years to provide assistance in managing the LSR program, and contracted with three construction firms for two-year periods to perform the actual replacement work. The Water Supply Board entered into contracts not to exceed \$22 million with these firms, and not only met but exceeded the requirement for the 3,600 service replacements to be completed by September 30, 2008.

The lead service replacement has been continuing ever since, with new construction contracts having been awarded. As of the end of November 2011, approximately 9,900 lead services have been replaced since the start of the program effort, at a total cost of nearly \$41 million.

Retirees Health Care

During 2006 the City of Providence, as well as the Water Supply Board, discovered that the City was not charging the Water Supply Board for the health care costs for retired Water Supply Board employees. All City retirees are placed into a separate retirement payroll with associated fringe benefits. Former Water Supply Board employees were not separately tracked.

A schedule was prepared of the Water Supply Board's retiree's health care costs for 2006, which was paid to the City of Providence. A schedule was also prepared including the Water Supply Board's actual retiree's health care costs for 2004 and 2005 and the calculated costs for the years from 1997 through 2003. This amount was included in the Water Supply Board's rate filing to the RI Public Utilities Commission (PUC) in March of 2007. During discovery for the rate case, the outstanding obligation amount was revised to \$1,489. The Water Supply Board agreed with the Division of Public Utilities, to a repayment term of six years, without interest. The RI PUC at an open meeting on October 30, 2007 denied the Water Supply Board's request to repay the City of Providence. The City appealed the decision to the Supreme Court which in the fiscal year ended June 30, 2010 upheld the RI PUC ruling.

A liability for \$1,489 was included in Due to City of Providence General Fund on the Statement of Net Assets as of June 30, 2009. As a result of the Supreme Court decision, the Water Supply Board reversed the \$1,489 liability and adjusted operating expenses for the year ended June 30, 2010.

(CONTINUED)



**PROVIDENCE WATER SUPPLY BOARD**  
**(An enterprise fund of the City of Providence, Rhode Island)**

**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2011 AND 2010 (000's)**

**9. CAPITAL ASSETS**

The following is a summary of the activity in capital assets as of June 30, 2011:

	Balance June 30, 2010	Additions	Disposals	Balance June 30, 2011
Capital assets not being depreciated:				
Land	\$ 13,574	\$ 5,731	\$ -	\$ 19,305
Scituate Reservoir Project	18,682	-	-	18,682
Construction in progress	43,103	9,440	-	52,543
Total capital assets not being depreciated	<u>75,359</u>	<u>15,171</u>	<u>-</u>	<u>90,530</u>
Capital assets being depreciated:				
Buildings and improvements	48,637	6,626	-	55,263
Improvements other than buildings	217,730	8,089	-	225,819
Machinery and equipment	26,554	685	-	27,239
Assets under capital lease	13,846	-	-	13,846
	<u>306,767</u>	<u>15,400</u>	<u>-</u>	<u>322,167</u>
Less accumulated depreciation for:				
Buildings and improvements	28,557	5,255	-	33,812
Improvements other than buildings	91,880	5,169	-	97,049
Machinery and equipment	23,336	772	-	24,108
Assets under capital lease	3,253	184	-	3,437
	<u>147,026</u>	<u>11,380</u>	<u>-</u>	<u>158,406</u>
Total capital assets being depreciated, net	<u>159,741</u>	<u>4,020</u>	<u>-</u>	<u>163,761</u>
Total capital assets, net	<u>\$ 235,100</u>	<u>\$ 19,191</u>	<u>\$ -</u>	<u>\$ 254,291</u>

(CONTINUED)

**PROVIDENCE WATER SUPPLY BOARD**  
**(An enterprise fund of the City of Providence, Rhode Island)**

**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2011 AND 2010 (000's)**

**9. CAPITAL ASSETS (CONTINUED)**

The following is a summary of the activity in capital assets as of June 30, 2010:

	Balance June 30, 2009	Additions	Disposals	Balance June 30, 2010
Capital assets not being depreciated:				
Land	\$ 12,551	\$ 1,023	\$ -	\$ 13,574
Scituate Reservoir Project	18,682	-	-	18,682
Construction in progress	32,601	40,509	30,007	43,103
Total capital assets not being depreciated	63,834	41,532	30,007	75,359
Capital assets being depreciated:				
Buildings and improvements	37,038	11,599	-	48,637
Improvements other than buildings	198,827	18,903	-	217,730
Machinery and equipment	26,293	261	-	26,554
Assets under capital lease	13,846	-	-	13,846
Total capital assets being depreciated	276,004	30,763	-	306,767
Less accumulated depreciation for:				
Buildings and improvements	25,454	3,103	-	28,557
Improvements other than buildings	84,540	7,340	-	91,880
Machinery and equipment	22,543	793	-	23,336
Assets under capital lease	3,068	185	-	3,253
	135,605	11,421	-	147,026
Total capital assets being depreciated, net	140,399	19,342	-	159,741
Total capital assets, net	\$ 204,233	\$ 60,874	\$ 30,007	\$ 235,100

(CONTINUED)

**PROVIDENCE WATER SUPPLY BOARD**  
*(An enterprise fund of the City of Providence, Rhode Island)*

**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2011 AND 2010 (000's)**

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**10. POST EMPLOYMENT BENEFITS**

The Water Supply Board follows GASB Statement No. 45 "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions".

The Water Supply Board's Post-Retirement Benefits Program of the City of Providence (the "Program") is a defined-benefit, single-employer post-retirement health and life insurance program. The Program provides lifetime health care and life insurance benefits to substantially all retired employees and their spouses. Disclosures about this program, as a whole, are presented in the City of Providence, Rhode Island's basic financial statements. As of June 30, 2011 and 2010, the City recorded a liability for unpaid post-retirement contributions of \$98,408 and \$63,980, respectively. Separate actuarial information related to the Water Supply Board employees is not available. Accordingly, only disclosures about the Water Supply Board's participation in the Plan are presented herein.

The Water Supply Board's allocation of the actuarial required contribution was \$1,476 and \$419 was contributed for the year ended June 30, 2011.

The Water Supply Board's allocation of the actuarial required contribution was \$1,018 and \$1,085 was contributed for the year ended June 30, 2010.

The unpaid balance of the actuarial required contribution at June 30, 2011 and June 30, 2010 of \$2,407 and \$1,350, respectively, is included in non-current liabilities on the Statement of Net Assets.

The historical schedules of employer contributions and funding progress for the Program are included in the City of Providence, Rhode Island's basic financial statements.

**11. RECLASSIFICATIONS**

Certain 2010 financial statement amounts have been reclassified to conform to the 2011 presentation. There is no change in the reported total net assets.

(CONCLUDED)



**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**

To the Water Supply Board  
City of Providence, Rhode Island

We have audited the financial statements of the Providence Water Supply Board (the "Water Supply Board"), as of and for the year ended June 30, 2011, and have issued our report thereon dated December 21, 2011. 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

Management of the Water Supply Board is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Water Supply Board's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Water Supply Board's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Water Supply Board's internal control over financial reporting.

A deficiency in internal control 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 material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

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 deficiencies, 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.

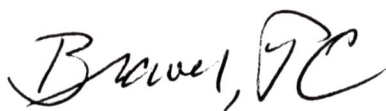
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Boston  
Concord  
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Compliance and Other Matters

As part of obtaining reasonable assurance about whether Water Supply Board'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*.

We noted certain matters that we reported to management of the Water Supply Board, in a separate letter dated December 21, 2011.

This report is intended solely for the information and use of management and the Water Supply Board 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 "Brewster, PC". The signature is written in a cursive style with a large, stylized "B" and "C".

Providence, Rhode Island

December 21, 2011