

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

FINANCIAL STATEMENTS  
AND  
SUPPLEMENTAL INFORMATION

For the Years Ended December 31, 2011 and 2010

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

AUDIT REPORT  
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## MANAGEMENT'S DISCUSSION AND ANALYSIS

As Management of the Authority, we offer readers of the Authority's financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal year ended December 31, 2011. We encourage readers to consider the information presented here in conjunction with the Authority's financial statements as presented elsewhere in this report.

### A. Financial Highlights

1. The assets of the Authority exceeded its liabilities at the close of the most recent fiscal year by \$54,460,496 (net assets) compared to \$55,535,022 for the prior fiscal year.

The Authority's unrestricted/restricted cash and cash equivalent and investment balance at December 31, 2011 was \$4,166,958 representing a decrease of \$797,918 from the prior fiscal year. The decrease primarily funded the Waste Water Treatment Plant Upgrade Project and other capital improvements. The cash balance of \$4,166,958 has been programmed by the Authority for future capital improvements and working capital.

2. The Authority had Total Operating Revenues of \$9,539,674 and Total Operating Expenses of \$10,368,727 (which includes a charge to operations of \$736,857 for unfunded post retirement medical benefits for the year ended December 31, 2011).
3. The Authority's cash capital outlays for the fiscal year were \$1,699,431.
4. On July 10, 2008, the Authority Commissioners approved a resolution to authorize the authority to sell Sewer Revenue Bonds as part of the State of New Jersey Environmental Infrastructure Trust. In connection with the offering, \$7,595,000 of 2008A Sewer Revenue Bonds were sold with an average fixed coupon of approximately 5.25%. Additionally, the Authority has issued the 2008B Sewer Revenue Bonds in the amount of \$7,627,686 which is an interest free loan. The Bonds mature 20 years from date of issue. The proceeds of the loans were used solely for the Authority's Waste Water Treatment Plant Upgrade Project which became operational at the end of 2010. The 2008A and 2008B Sewer Revenue Bonds are secured by the assets of the Authority including its restricted and unrestricted cash balances.

### B. Using the Annual Report

1. Management's Discussion and Analysis

The Management's Discussion and Analysis is intended to serve as an introduction to the Authority's Financial Statements. The Authority's Financial Statements and Notes to Financial Statements included in this report were prepared in accordance with Generally Accepted Accounting Principles applicable to governmental entities in the United States of America.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### B. Using the Annual Report (Continued)

#### 2. Financial Statements

The Financial Statements are designed to provide readers with a broad overview of the Authority's finances, in a manner similar to a private-sector business. They consist of Comparative Balance Sheets, Comparative Statements of Revenue, Expense and Changes in Net Assets, and Comparative Statements of Cash Flows.

The Balance Sheets present information on all the Authority's assets and liabilities, with the difference between the two reported as net assets.

The Comparative Statements of Revenue, Expense, and Changes in Net Assets present information showing how the Authority's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of unrelated cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., depreciation and earned but unused vacation leave).

The Financial Statements report on the Authority's activities. The activities are primarily supported by user charges. The Authority's function is to provide a service to the community. The Authority's Financial Statements can be found in Exhibits A, B, and C of this Report.

#### 3. Notes to Financial Statements

The Notes to Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements. The Notes to Financial Statements can be found in this report after the Financial Statements.

### C. The Authority as a Whole

The Authority's net assets decreased during the current fiscal year as detailed below. The Authority's revenues are principally from user charges. The Authority's revenues were sufficient to cover all of the cash operating expenses.

The largest portion of the Authority's equity reflects its investment in capital assets (e.g., land, buildings, equipment, and the collection system). The Authority uses these capital assets to provide services to the community. The unrestricted net assets of the Authority are available for future use to provide services.

MANAGEMENT'S DISCUSSION AND ANALYSIS

C. The Authority as a Whole (Continued)

COMPUTATIONS OF NET EQUITY

	December 31,	
	<u>2011</u>	<u>2010</u>
Cash and other assets	\$ 1,664,586	\$ 1,547,890
Restricted assets - cash	3,943,219	4,697,343
Capital assets - net	<u>64,980,620</u>	<u>65,903,416</u>
Total Assets	70,588,425	72,148,649
Less: Total liabilities	<u>16,127,929</u>	<u>16,613,627</u>
Net Assets	<u>\$54,460,496</u>	<u>\$55,535,022</u>
Net assets - unrestricted	\$50,591,158	\$50,903,651
Net assets - restricted	<u>3,869,338</u>	<u>4,631,371</u>
Net Assets	<u>\$54,460,496</u>	<u>\$55,535,022</u>

COMPUTATIONS OF CHANGE IN EQUITY

	December 31,	
	<u>2011</u>	<u>2010</u>
REVENUES		
User charges	\$ 9,182,609	\$ 9,010,432
Connection fees	300,465	364,838
Other revenues	<u>56,600</u>	<u>70,554</u>
Total Operating Revenue	<u>9,539,674</u>	<u>9,445,824</u>
EXPENSES		
Total operating expenses	8,075,393	7,449,218
Depreciation expense	<u>2,293,334</u>	<u>1,804,843</u>
Total Operating Expense	10,368,727	9,254,061
Operating (loss) income	(829,053)	191,763
Non-operating revenue (expense) net	<u>(245,473)</u>	<u>183,826</u>
Net (loss) income	(1,074,526)	375,589
Net Assets beginning of year	<u>55,535,022</u>	<u>55,159,433</u>
Net Assets end of year	<u>\$54,460,496</u>	<u>\$55,535,022</u>

## MANAGEMENT'S DISCUSSION AND ANALYSIS

### D. Budgetary Highlights

For the year ended December 31, 2011 budgets were prepared by the Authority and were approved by the Division of Community Affairs of the State of New Jersey. The budgets were primarily used as a management tool. The budgets were prepared in accordance with the accounting procedures prescribed by the Division of Local Government Services of the State of New Jersey.

As indicated by the excess of expenses over revenues, when adjusted by depreciation and the provision for post retirement medical expenses, the Authority's equity as adjusted would have increased during the fiscal year. This increase is indicative of the Authority operating within its budgetary limitations in total, for all its programs.

### E. Capital Assets and Debt Administration

#### 1. Capital Assets

As of December 31, 2011, the Authority's investment in capital assets was \$64,901,910 (net of accumulated depreciation). This investment in capital assets includes land, buildings, equipment, collection systems, and vehicles.

Capital expenditures during the year ended December 31, 2011 aggregated \$1,699,431 compared to \$10,063,911 in 2010 (excluding developers' contributions of \$100,000 for the year ended December 31, 2011).

Additional information on the Authority's capital assets can be found in the notes to the Financial Statements, which is included in this Report.

### F. Economic Factors and Next Year's Budgets and Rates

The following factors were considered in preparing the Authority's budget for the fiscal year ending December 31, 2011:

1. The state of the economy.
2. The ability to control expenditures.

### G. Contacting the Authority's Financial Management

The financial report is designed to provide a general overview of the Authority's finances for all those with an interest. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Patrick W. Parkinson, Executive Director, Township of Middletown Sewerage Authority, Center Avenue, Belford, NJ 07718.

To the Board of Commissioners  
Township of Middletown Sewerage Authority  
Belford, New Jersey

We have audited the accompanying balance sheets of the Township of Middletown Sewerage Authority at December 31, 2011 and 2010 and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Authority's Management. Our responsibility is to express an opinion on these financial statements based on our 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 and in compliance with audit requirements as prescribed by the Local Finance Board, Department of Community Affairs, State of New Jersey. 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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Township of Middletown Sewerage Authority at December 31, 2011 and 2010, and the results of its operations and its cash flows for each of the two years then ended, in conformity with accounting principles generally accepted in the United States of America and practices prescribed by the Local Finance Board.

In accordance with *Government Auditing Standards*, we have also issued a report dated April 7, 2012, on our consideration of the Township of Middletown Sewerage Authority's internal control over financial reporting and 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 related audit.

Our audit has been made primarily for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying supplementary information is not a required part of the financial statements of the Township of Middletown Sewerage Authority but are presented as additional analytical data, as required by the Local Finance Board. Such supplementary information has been subjected to the procedures applied in the audits of the basic financial statements and in our opinion, is fairly stated all material respects in relation to the basic financial statements taken as a whole.

This report is intended for the information of the Members of the Board and Management of the Township of Middletown Sewerage Authority and trustee banks, and for filing with the Division of Local Government services, Department of Community affairs, State of New Jersey. However, this report is a matter of public record and its distribution is not limited.

*Meyler & Company, LLC*  
Meyler & Company, LLC

Middletown, New Jersey  
April 7, 2012



TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY  
COMPARATIVE BALANCE SHEETS

ASSETS

	December 31,	
	2011	2010
<b>Current Assets</b>		
<b>Unrestricted assets</b>		
Cash and cash equivalents	\$ 223,739	\$ 267,534
Accounts receivable-sewer rents	1,122,693	1,004,383
Supplies inventory	318,154	275,973
Total Current Unrestricted Assets	1,664,586	1,547,890
<b>Restricted Assets</b>		
Cash held by Authority	3,943,219	4,697,342
Cash equivalents held by Trustee		1
Total Current Restricted Assets	3,943,219	4,697,343
Total Current Assets	5,607,805	6,245,233
<b>Property, Plant and Equipment</b>		
Net of accumulated depreciation of \$42,049,549 and \$39,829,015 at December 31, 2011 and 2010, respectively	64,901,910	65,820,076
<b>Other Assets</b>		
Bond issuance costs net of amortization of \$13,890 and \$9,260 at December 31, 2011 and 2010, respectively	78,710	83,340
Total Assets	\$70,588,425	\$72,148,649

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

## TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

COMPARATIVE BALANCE SHEETS  
LIABILITIES AND FUND EQUITY

	<u>December 31,</u>	
	<u>2011</u>	<u>2010</u>
<b>Current Liabilities</b>		
Payable from unrestricted assets		
Accounts payable - operations	\$ 331,632	\$ 789,632
Prepaid sewer rents	33,456	30,434
Accrued expenses	<u>288,013</u>	<u>274,093</u>
Total Liabilities Payable from Unrestricted Assets	<u>653,101</u>	<u>1,094,159</u>
Payable from Restricted Assets		
Reserve deposits	73,881	65,971
Revenue bonds payable - current portion	660,182	652,028
Accrued interest payable	<u>151,740</u>	<u>156,815</u>
Total Liabilities Payable from Restricted Assets	<u>885,803</u>	<u>874,814</u>
<b>Long-Term Liabilities</b>		
Long-term portion of bonds payable	13,078,803	13,738,985
Unfunded post retirement medical benefits	1,316,101	700,129
Premium on issuance of bonds net of amortization of \$22,838 and \$11,419 at December 31, 2011 and 2010, respectively	<u>194,121</u>	<u>205,540</u>
Total Liabilities	<u>16,127,929</u>	<u>16,613,627</u>
<b>Net Assets</b>		
Net Assets - unrestricted	50,591,158	50,903,651
Net Assets - restricted	<u>3,869,338</u>	<u>4,631,371</u>
Total Net Assets	<u>54,460,496</u>	<u>55,535,022</u>
Total Liabilities and Fund Equity	<u>\$70,588,425</u>	<u>\$72,148,649</u>

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

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

COMPARATIVE STATEMENTS OF REVENUE, EXPENSES AND  
CHANGES IN NET ASSETS

	<u>Year Ending December 31,</u>	
	<u>2011</u>	<u>2010</u>
Operating Revenue		
User charges	\$ 9,182,609	\$ 9,010,432
Connection fees	300,465	364,838
Other revenues	<u>56,600</u>	<u>70,554</u>
Total operating revenues	<u>9,539,674</u>	<u>9,445,824</u>
Operating Expenses		
Cost of providing services, administrative and general expenses	8,075,393	7,449,218
Depreciation	<u>2,293,334</u>	<u>1,804,843</u>
Total Operating Expenses	<u>10,368,727</u>	<u>9,254,061</u>
Operating (Loss) Income	<u>(829,053)</u>	<u>191,763</u>
Non-Operating Revenues (expenses)		
Interest income	19,838	177,037
Interest expense	(372,100)	
Amortization of bond issuance costs	(4,630)	(4,630)
Amortization of premium on issuance of bonds	<u>11,419</u>	<u>11,419</u>
Net Non-Operating Revenue	<u>(345,473)</u>	<u>183,826</u>
Developer Contributions	<u>100,000</u>	<u>          </u>
Net (Loss) Income	(1,074,526)	375,589
Net Assets, Beginning of Year	<u>55,535,022</u>	<u>55,159,433</u>
Net Assets, End of Year	<u>\$54,460,496</u>	<u>\$55,535,022</u>

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

## TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

## COMPARATIVE STATEMENTS OF CASH FLOWS

	Year Ending December 31,	
	2011	2010
Cash flows from operating activities:		
Receipts from user charges	\$ 9,476,723	\$ 9,664,008
Receipts from interest income	19,838	177,037
Payments to suppliers and employees	(7,943,020)	(7,117,770)
Other		(4,551)
Net cash provided from operating activities	<u>1,553,541</u>	<u>2,718,724</u>
Cash flows from investing activities:		
Reduction in cash equivalents held by trustee		8,411,026
Capital expenditures paid	<u>(1,699,431)</u>	<u>(10,063,911)</u>
Net cash used in investing activities	<u>(1,699,431)</u>	<u>(1,652,885)</u>
Cash flows from financing activities:		
Bond principal paid	<u>(652,028)</u>	<u>(635,336)</u>
Net Cash used in financing activities	<u>(652,028)</u>	<u>(635,336)</u>
Net (decrease) increase in cash	(797,918)	430,503
Cash and cash equivalents at beginning of year	<u>4,964,876</u>	<u>4,534,373</u>
Cash and cash equivalents at end of year	<u>\$ 4,166,958</u>	<u>\$ 4,964,876</u>
Reconciliation of operating (loss) income to net cash provided by operating activities:		
Net (loss) income	\$ (1,074,526)	\$ 375,589
Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities:		
Developers contribution	(100,000)	
Depreciation	2,293,334	1,804,843
Amortization of:		
Bond issuance costs	4,630	4,630
Premium on issuance of bonds	(11,419)	(11,419)
Decrease (increase) in accounts receivable	(118,310)	164,741
Decrease in supplies inventory	(42,181)	31,508
Increase (decrease) in accounts payable	(33,736)	19,931
Increase in unfunded post retirement medical benefits	615,972	309,007
(Decrease) increase in accrued bond interest	(5,075)	(5,445)
Decrease in reserve deposits	7,910	(7,076)
Decrease in prepaid sewer rents	3,022	6,917
Increase (decrease) in accrued expenses	13,920	25,498
Net cash provided from operating activities	<u>\$ 1,553,541</u>	<u>\$ 2,718,724</u>

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

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY  
 COMPARATIVE STATEMENTS OF CASH FLOWS (CONTINUED)

Supplemental Cash Flow Information

Interest expense paid on the revenue bonds aggregated \$377,175 and \$389,425 at December 31, 2011 and 2010 respectively. In 2011, developers contributed \$100,000 to infrastructure capital.

Non-Cash Activities

	<u>Year Ending December 31,</u>	
	<u>2011</u>	<u>2010</u>
Accounts payable	\$(424,264)	\$(892,065)
Property, Plant and Equipment	424,264	892,065

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

## TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

## NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 2011

## NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Township of Middletown Sewerage Authority hereafter referred to as the "Authority" is a public body, politic and corporate created on February 13, 1966 by the Township of Middletown, hereafter referred to as the "Township." It is authorized and empowered to acquire, construct, maintain, operate and improve works for the collection, treatment, purification and disposal of sewage or other waste.

The ordinance creating the Authority provides that the governing body of the Authority shall consist of five members and two alternates appointed by the Township governing body.

The Township and the Authority have entered into a Service Agreement dated August, 1, 1969 which was modified on May 10, 1993. Pursuant to Article 3, Section 302 of the Service Agreement the Authority agrees to impose charges, connection fees, or rentals, as defined in the "Service Agreement", in compliance with all applicable rules and regulations of the Township, State and County, and will collect from the users all sums due it, such that the receipts of the Authority in each fiscal year shall be sufficient (1) to pay or provide for the expenses of operations, maintenance and debt service, (2) to maintain such reserves or sinking funds as may be required by any contract of the Authority, and (3) to comply in all respects with the terms and provisions of any Bond Resolution and the Municipal and Country Utility Authorities Law.

Pursuant to Section 302 of the Service Agreement, the Township agrees to pay all amounts of interest and principal on the bonds should the funds available to the Authority be insufficient to cover such obligation, subject to certain notice and consent provisions. The Authority is obligated to repay the Township out of surplus funds within one year from the time received pursuant to the Service Agreement.

The Township has also adopted an ordinance compelling connection to the Authority's system. Upon failure to comply with such ordinance, the Township may proceed to make such connection, or cause same to be made, and charge and assess the cost thereof against such property pursuant to the revised Statute of New Jersey.

As a public body, under existing statute, the Authority is exempt from both Federal and state income taxes.

The following is a summary of the Authority's significant accounting policies applied in the preparation of the financial statements.

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Financial Statements

The financial statements of the Authority have been prepared on the accrual basis of accounting in accordance with generally accepted accounting principles, government auditing standards, and the requirement of the Division of Local Government Services of the State of New Jersey.

Use of Estimates

The preparation of the financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Investment Securities

Investment securities are stated at cost which approximates fair value. The cost of securities sold for purposes of computing gains or losses is determined by the specific identification method.

Revenue Recognition/Accounts Receivable-Sewer Rents

Accounts receivable consists of amounts due the Authority for user charges. Accounts are billed quarterly on a cycle basis. Revenue is recognized on a quarterly basis based upon bills sent out to each lot and block in the Township of Middletown at the specified rate approved by the Board of Commissioners. Additionally, revenue is recognized from connection fees when new facilities connect to the system. This is a one time fee recalculated annually based upon NJ statutes.

Restricted Accounts

In accordance with the July 10, 2008 Trust Resolution, the Authority has established the following restricted funds consisting of cash and investments:

<u>Fund</u>	<u>Description</u>	<u>Purpose</u>
Revenue Fund	All Revenue received by the Authority	Authorized operating expenses and, required transfers to the various accounts described below.

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

<u>Fund</u>	<u>Description</u>	<u>Purpose</u>
Bond service Fund (Current Debt Service)	Amount needed to pay matured principal and interest plus principal and interest due on or before the following February 1 <sup>st</sup> and August 1 <sup>st</sup> .	Principal and interest on the bonds
Renewal and Replacement Fund	Amount needed to increase the balance to the extent required to be current, certified by the consulting engineer upon completion of project.	Cost of extraordinary repairs, renewals, and replacements.
Operating Fund	Amounts needed to pay for the operation, the maintenance or the repair of the System and for reasonable and necessary Operating Expenses.	Cost of reasonable and necessary Operating Expenses.
Bond Service Reserve	No requirement	Transfers to meet levels required in the debt service or any sinking fund. Any excess may be transferred into the Revenue Fund
General Fund	Balance after all other requirements are met.	Make-up deficiencies in other funds, capital additions, redemption bonds.
Construction	Proceeds of debt issued.	Construction costs.



TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Unamortized Debt Issue Cost

Debt issue costs consist of underwriting, legal, engineering, and accounting fees, printing, and other financial costs incurred in connection with the issuance of the bonds net of accumulated amortization. These costs are being amortized over the life of the Bond issue.

Interfunds Receivable and Payable

During the course of its operations, the Authority has numerous transactions between funds to finance operations, provide services, construct assets, and service debts. To the extent that certain transactions between the accounts had not been paid or received as of the balance sheet dates, balances of interfund amounts receivable and payable have been recorded.

Grants

Contributions, received from various governmental sources as grants, are recorded in the period received. Developer construction contributions towards system infrastructure are recorded in the period in which applicable construction costs are incurred. Donated assets are recorded at fair market value at the date of gift. Grants not externally restricted and utilized to finance operations are identified as non-operating revenues.

Inventory

The Authority's inventory consists of plant supplies and replacement parts, fuel and chemicals for the treatment of sewerage. The inventory is stated at cost, determined on a first in, first out basis.

Cash Equivalents

The Authority considers all highly liquid investments with a maturity date of three months or less, at the time of purchase, to be cash equivalents.

Premium on Sale of Bonds

The Authority amortizes the premium it received on the sale of bonds over the life of the bonds which is 20 years.

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property, Plant and Equipment

Property, plant and equipment are stated at cost which includes direct construction costs, other expenditures related to construction, and certain professional and administrative costs.

System construction costs are charged to construction in progress until such time as given segments of the system are completed and put into operation. Depreciation is determined on a straight-line basis for all plant and equipment.

Depreciation is provided over the following estimated lives:

Building and plants	40 years
Machinery and equipment	15-40 years
Collection system	40 years
Vehicles and office equipment	3-10 years

NOTE 2 - INVESTMENTS

Investments are stated at cost which approximates fair value. The Authority's investments are limited to obligations of or guaranteed by the State Government or State of New Jersey, bonds, notes or other indebtedness of an agency or instrumentality of the State government, bank certificates of deposit or time savings account and deposits in interest-bearing accounts of any bank. At December 31, 2011 and 2010 all cash is in a money market account with a bank that is part of the Government Unit Protection Act (GUPA).

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 4 - BONDS PAYABLE (CONTINUED)

Sewer Revenue Bonds are secured by the assets of the Authority including its restricted and unrestricted cash balances.

Bond principal amortization and annual interest rates relating to the 2008A and 2008B Sewer Revenue Bonds are as follows:

Year	2008A Sewer Revenue Bonds			Total Debt Service	2008B
	Principal	Interest Rate	Interest		Sewer Revenue Bonds Principal
2012	\$ 270,000	5.000%	\$ 364,175	\$ 634,175	\$ 390,182
2013	285,000	5.000%	350,675	635,675	391,105
2014	300,000	5.000%	336,425	636,425	391,566
2015	315,000	5.000%	321,425	636,425	391,566
2016	330,000	5.000%	305,675	635,675	391,105
2017	345,000	5.000%	289,175	634,175	390,182
2018	365,000	5.000%	271,925	636,925	391,874
2019	380,000	5.250%	253,675	633,675	389,875
2020	400,000	5.500%	233,725	633,725	389,905
2021	425,000	5.500%	211,725	636,725	391,751
2022	450,000	5.500%	188,350	638,350	392,751
2023	470,000	5.500%	163,600	633,600	389,828
2024	500,000	5.000%	137,750	637,750	392,382
2025	525,000	5.000%	112,750	637,750	392,382
2026	550,000	5.000%	86,500	636,500	391,613
2027	575,000	5.000%	59,000	634,000	390,074
2028	605,000	5.000%	30,250	635,250	390,844
	<u>\$7,090,000</u>		<u>\$3,716,800</u>	<u>\$10,806,800</u>	<u>\$6,648,985</u>

391,105  
285  
676,105

NOTE 5 - PENSION PLANS

The Authority participates in the Public Employees' Retirement System of the State of New Jersey which is part of the Division of Pensions in the Treasury, State of New Jersey. The Plan is funded annually based on the projected benefit method with aggregate level normal cost and frozen initial unfunded benefit method with aggregate level normal cost and frozen initial unfunded accrued liability. The Plan, which covers public employees throughout the State, does not maintain separate records for each reporting unit and, accordingly, the actuarial data for the employees of the Authority who are members of the Plan is not available. Funding of the Plan is done on a fiscal year ended June 30 and resulted in a required funding of \$209,641 and \$164,074 for 2011 and 2010, respectively.

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 6 – POST EMPLOYMENT RETIREMENT MEDICAL BENEFITS

Plan Description

The Township of Middletown Sewerage Authority (“Authority”) is a single-employer defined benefit healthcare plan and is administered by the Authority. The Authority provides medical insurance benefits to eligible retirees and their spouses. Employees retiring after reaching age 62 and completing at least 15 years of service with the Authority or upon reaching age 55 and having worked for 25 years in the New Jersey pension system, who participate in the Authority’s health care plan at the time of retirement, receive a one-time opportunity to elect continued coverage of benefits subsequent to retirement under the health care plan then in effect for active employees, at no cost to the employee.

Funding Policy

The Authority is responsible for the entire cost required to fund the post retirement medical benefits. The annual required contribution is based upon projected pay-as-you-go financing requirements. For the year ended December 31, 2011 and 2010, the Authority contributed \$120,885 and \$130,006, respectively towards the annual required contribution.

Annual Post Employment Medical Benefit Cost

The Authority’s annual Other Post Employment Benefit (OPEB) for medical cost is calculated based on the Annual Required Contribution of the employer (ARC), an amount actuarially determined in accordance within the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years.

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 6 – POST EMPLOYMENT RETIREMENT MEDICAL BENEFITS (CONTINUED)

Annual Post Employment Medical Benefit Cost (Continued)

The following table shows the components of the Authority's annual OPEB cost for the years ended December 31, 2011 and 2010 and the amount actually contributed to the plan:

	<u>Year</u>	
	<u>2011</u>	<u>2010</u>
Annual OPEB cost	\$736,857	\$439,144
Contribution made	<u>120,885</u>	<u>130,137</u>
Net OPEB obligation	<u>\$615,972</u>	<u>\$309,007</u>

The Authority's OPEB cost, the percentage of annual OPEB cost contributed to the plan and the OPEB obligation for 2011 and 2010 is as follows:

	<u>Year</u>	
	<u>2011</u>	<u>2010</u>
Annual OPEB cost	\$736,857	\$439,144
Percentage of annual OPEB cost contributed	16.41%	29.63%
Net OPEB obligation	\$615,972	\$309,007

At December 31, 2011, the date of the most recent actuarial valuation, the plan had an unfunded liability of \$9,689,250 which is being accrued over 30 years. Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actuarial results are compared with post expectations and new estimates are made about the future.

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 6 – POST EMPLOYMENT RETIREMENT MEDICAL BENEFITS (CONTINUED)

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the type of benefits provided at the time of each valuation and the historical pattern of costs. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short term volatility in accrued liabilities and the actuarial values of assets consistent with long-term perspective of the calculations.

In December 31, 2011, actuarial valuation, the Entry Age Actuarial Cost Method and the Level Percentage of Payroll Amortization Method were used in accordance with GASB 45. The actuarial assumption included a 2% investment rate of return which is a blended rate of the expected long term investment returns and an annual healthcare cost trend rate of 5%. The unfunded Actuarial Accrued Liability of \$9,689,250 is being amortized over 30 years.

NOTE 7 - FAIR VALUE MEASUREMENTS AND DISCLOSURES

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. *Fair Value Measurements and Disclosures* also establish a fair value hierarchy that prioritizes the inputs used in valuation methodologies into the following three levels:

- Level 1 Inputs - Unadjusted quoted prices in active markets for identical assets or liabilities
- Level 2 Inputs – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, or other inputs that can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 Inputs – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash value methodologies or other valuation techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 7 - FAIR VALUE MEASUREMENTS AND DISCLOSURES (CONTINUED)

The fair value of the Corporation's cash and cash equivalents, accounts receivable, prepaid expenses, accounts payable and note payable approximate the carrying amounts of such instruments due to their short maturity.

NOTE 8 - SUBSEQUENT EVENTS

On January 13, 2012, the Authority settled its arbitration claims with Atlantic Highlands/Highlands Regional Sewerage Authority and received \$641,230 in settlement awards.

Subsequent events were assessed through April 7, 2012, the date the financial statements were released.

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

STATEMENT OF CHANGES IN UNRESTRICTED CASH AND CASH EQUIVALENTS  
For the Year Ending December 31, 2011

	<u>Operating Account</u>	<u>Connection Fee Account</u>	<u>Total</u>
Cash and cash equivalents January 1, 2011	\$ 184,781	\$ 82,753	\$ 267,534
Cash Receipts			
Connection fees		300,468	300,468
Interest on investments	602	277	879
Interfund transfers	<u>7,078,810</u>	<u>(360,000)</u>	<u>6,718,810</u>
Total cash and cash equivalents available	7,264,193	23,498	7,287,691
Cash Disbursements			
Operations	<u>7,063,952</u>	_____	<u>7,063,952</u>
Total cash disbursements	<u>7,063,952</u>	_____	<u>7,063,952</u>
Cash and cash equivalents December 31, 2011	<u>\$ 200,241</u>	<u>\$ 23,498</u>	<u>\$ 223,739</u>

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



TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

STATEMENT OF CHANGES IN RESTRICTED CASH AND CASH EQUIVALENTS  
For the Year Ending December 31, 2011

	Construction Fund	Capital Fund	Developers' Escrow	General Fund	Revenue Account	Total
Cash and Cash Equivalents January 1, 2011	\$ 1	\$ 49,497	\$ 65,971	\$ 3,053,607	\$ 1,528,267	\$ 4,697,343
Cash Receipts						
User charges and other					9,168,507	9,168,507
Developers' escrow received			9,530		9,530	9,530
Interest on investments		257	162	16,110	2,592	19,121
Interfund transfers		3,230,689		(878,711)	(9,070,788)	(6,718,810)
Total Cash and Cash Equivalents Available	1	3,280,443	75,663	2,191,006	1,628,578	7,175,691
Cash Disbursements						
Developer's escrow returned			1,782			1,782
Operations		479,280				479,280
Capital expenditures		1,699,431				1,699,431
Bond principal payment		652,028				652,028
Interest paid on bonds		377,175				377,175
Administrative fee on bonds	1	22,775				22,776
Total Cash Disbursements	1	3,230,689	1,782			3,232,472
Cash and Cash Equivalents at December 31, 2011	\$ -	\$ 49,754	\$ 73,881	\$ 2,191,006	\$ 1,628,578	\$ 3,943,219

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

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

STATEMENT OF REVENUE AND COSTS FUNDED BY  
OPERATING REVENUES COMPARED TO BUDGET

For the Year Ended December 31, 2011

	Amended Budget Revenue/ Costs	Actual Revenue/ Costs
Sewer Billing Income		
Sewer rental income	\$8,685,945	\$9,182,609
Connection fees	348,320	300,465
Other	<u>40,735</u>	<u>56,600</u>
Total Operating Income	<u>9,075,000</u>	<u>9,539,674</u>
Operating Expenses		
Salaries		
Administrative	361,991	365,080
Treatment plant	1,793,478	1,792,182
Collection system	<u>296,619</u>	<u>303,159</u>
Total Salaries	<u>2,452,088</u>	<u>2,460,421</u>
Administration		
Insurance	57,068	57,068
Auditing	25,000	25,000
Legal	45,000	39,092
Trustee fees	2,000	2,000
Engineering	18,000	21,060
Pension	210,000	209,641
Hospitalization/dental	680,000	672,705
Payroll taxes	197,000	194,228
Payroll processing cost	15,000	13,611
Training	5,000	3,479
Safety	2,000	1,470
Travel/memberships	15,000	12,614
Recording secretary	1,800	1,950
Advertising	2,500	886
Miscellaneous	4,000	4,921
Postage	29,000	30,666
Telephone	50,000	52,853
Office supplies	8,000	9,187
Janitorial	4,000	3,948
Administrative maintenance	5,000	5,834
Printing	<u>10,500</u>	<u>6,019</u>
Total Administrative	<u>1,385,868</u>	<u>1,368,232</u>

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

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

STATEMENT OF REVENUE AND COSTS FUNDED BY  
OPERATING REVENUES COMPARED TO BUDGET (CONTINUED)

For the Year Ended December 31, 2011

	Amended Budget Revenue/ Costs	Actual Revenue/ Costs
Treatment Plant		
Electric	650,000	634,218
Gas	50,000	37,738
Water	20,000	18,700
Fuel vehicles	30,000	48,284
Chemicals	204,092	170,387
Sludge disposal/testing	621,000	613,431
Plant equipment maintenance	14,000	22,544
Vehicle maintenance	12,000	12,912
Uniforms	15,000	15,550
Insurance	<u>114,135</u>	<u>114,135</u>
Total Treatment Plant	<u>1,730,227</u>	<u>1,687,899</u>
Collection System		
Maintenance supplies	2,000	
Equipment maintenance	2,000	931
Chemicals	<u>8,000</u>	
Total Collection System	<u>12,000</u>	<u>931</u>
Monmouth County Outfall	838,000	837,775
Plant Maintenance	270,000	713,245
Post retirement medical expense net of payments of \$120,885 included under Hospitalization/Dental		615,972
Bond Administration Fee		22,772
Township of Middletown Appropriation	<u>368,146</u>	<u>368,146</u>
Total Operating Expense	<u>7,056,329</u>	<u>8,075,393</u>
Net Operating Revenue	2,018,671	1,464,281
Add: Interest on Investments	<u>30,000</u>	<u>19,838</u>
Net Operating Revenue Before Debt		
Service Payments	<u>2,048,671</u>	<u>1,484,119</u>
Less: Debt Service Payments		
Interest expense	399,881	372,100
Principal Payments	<u>652,028</u>	<u>652,028</u>
Total Debt service	<u>1,051,909</u>	<u>1,024,128</u>
Excess Revenues Over Costs		
Funded by Operating Revenues	<u>\$ 996,792</u>	<u>\$ 459,991</u>

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

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*

Board of Directors  
Township of Middletown Sewerage Authority  
Belford, NJ

We have audited the financial statements of the Township of Middletown Sewerage Authority as of and for the year ended December 31, 2011, and have issued our report thereon dated April 7, 2012. 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 Township of Middletown Sewerage Authority is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Township of Middletown Sewerage Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Township of Middletown Sewerage Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Township of Middletown Sewerage Authority'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 and correct 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 Township of Middletown Sewerage Authority'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 was not designed to identify all

deficiencies in internal control over financial reporting 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.

#### Compliance and Other Matters

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

This report is intended for the information of the Members of the Board and Management of the Township of Middletown Sewerage Authority and trustee banks, and for filing with the Division of Local Government Services, Department of Community Affairs, State of New Jersey. However, this report is a matter of public record and its distribution is not limited.

*Meyler & Company LLC*  
Meyler & Company, LLC

April 7, 2012

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
DECEMBER 31, 2011 (CONTINUED)

SECTION II FINANCIAL STATEMENT FINDINGS AND QUESTIONED COSTS

None

TOWNSHIP OF MIDDLETOWN SEWERAGE AUTHORITY

DECEMBER 31, 2011

ROSTER OF OFFICIALS

<u>Authority Members</u>	<u>Position</u>	<u>Term Expires</u>	<u>Amount of Surety Bond</u>
Chantal N. Bouw	Chairperson	February 1, 2013	\$50,000
James L. Hinckley	Vice Chairperson	February 1, 2014	50,000
Joan Smith	Treasurer/Secretary	February 1, 2015	50,000
Charles W. Rogers III		February 1, 2017	50,000
Thomas Stokes		February 1, 2013	50,000
 <u>Alternate Members</u>			
Emil F. Wrede		February 1, 2013	50,000
 <u>All Other</u>			
Office Staff			50,000
Plant Employees			50,000
 <u>Surety Company</u>			
New Jersey Utility Authorities Joint Insurance Fund			
Trenton, New Jersey			