

READING AREA WATER AUTHORITY

A COMPONENT UNIT OF THE CITY OF READING

FINANCIAL REPORT

DECEMBER 31, 2008

CONTENTS

	Page
INDEPENDENT AUDITOR'S REPORT	1
MANAGEMENT'S DISCUSSION AND ANALYSIS	2-5
FINANCIAL STATEMENTS	
Statement of net assets	6 and 7
Statement of revenues, expenses and changes in net assets	8 and 9
Statement of cash flows	10 and 11
Notes to financial statements	12-21

INDEPENDENT AUDITOR'S REPORT

**To the Members of the Board
Reading Area Water Authority
Reading, Pennsylvania**

We have audited the accompanying basic financial statements of the Reading Area Water Authority, a component unit of the City of Reading, Pennsylvania, as of and for the year ended December 31, 2008, as listed in the table of contents. These financial statements are the responsibility of the Reading Area Water 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. 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 Reading Area Water Authority as of December 31, 2008, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on Pages 2 through 5 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Reinsel Kuntz Lesher LLP

**Wyomissing, Pennsylvania
September 28, 2009**

READING AREA WATER AUTHORITY
A COMPONENT UNIT OF THE CITY OF READING
MANAGEMENT'S DISCUSSION AND ANALYSIS

The Management of the Reading Area Water Authority (the "Authority") offers readers of our financial statement the following narrative overview and analysis of our financial activities for the year ended December 31, 2008.

Financial Highlights

- Unrestricted current assets exceed current liabilities by \$ 7,383,330 at the close of the fiscal year. This is compared to \$ 5,110,830 at the close of the 2007 year.
- Total net assets increased by \$ 2,062,130 at the close of the fiscal year over the total net assets balance at the close of the 2007 year. This increase is largely due to contributions for capital improvements of \$ 1,460,134.
- The Authority had a net operating income of \$ 1,401,145 at the close of the fiscal year compared to a net operating income of \$ 2,739,398 at the close of the 2007 year. This decrease in net operating income is the result of a decrease in operating revenue of \$ 319,014 and an increase in operating expenses of \$ 952,984.
- The statement of cash flows, which identifies the sources and uses of cash activities for the fiscal year, indicates that cash decreased by \$ 665,979 at the close of the fiscal year compared to the cash balance at the close of the 2007 year. This decrease is largely due to the decrease in net operating income as stated above.
- The financial position of the Authority has significantly increased over the past year despite less net operating income than last year. This increase is largely due to contributions for capital improvements.

Basic Financial Statements

Our basic financial statements are prepared on the full accrual basis of accounting using an economic resources measurement focus, which is basically the same as what is used in for profit businesses in the private sector. The basic financial statements include a statement of net assets, statement of revenues, expenses and changes in net assets, statement of cash flows and notes to the financial statements.

The statement of net assets presents information on the assets and liabilities, with the difference between assets and liabilities reported as net assets. The increases and decreases in net assets over time may be a useful indicator of the finances of the Authority as to whether it is improving or deteriorating.

The statement of revenues, expenses and changes in net assets of the Authority for the fiscal year shows the detail of net income or loss being combined with the beginning net assets balance, resulting in the ending net assets for the fiscal year.

The statement of cash flows reports cash activities for the fiscal year resulting from operating activities, noncapital 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 balance at the end of the current fiscal year.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements.

Financial Information

Net Assets. The following schedule presents a summary of net assets comparison for the fiscal years ended December 31, 2008 and 2007:

	2008	2007
Unrestricted current assets	\$ 10,734,442	\$ 11,094,620
Restricted current assets	24,852,146	26,676,379
Capital assets, net	16,568,878	14,780,041
Other assets, net	<u>5,027,071</u>	<u>6,387,744</u>
 Total assets	 <u>57,182,537</u>	 <u>58,938,784</u>
Current liabilities	3,351,112	5,983,790
Long-term debt, net	<u>47,108,042</u>	<u>48,293,741</u>
 Total liabilities	 <u>50,459,154</u>	 <u>54,277,531</u>
 Net assets:		
Invested in capital assets, net	-	-
Restricted for debt service	5,442,317	4,661,253
Unrestricted assets	<u>1,281,066</u>	<u>-</u>
 Total net assets	 <u>\$ 6,723,383</u>	 <u>\$ 4,661,253</u>

A large portion of the Authority's total current assets is invested in construction funds, (e.g., cash restricted for infrastructure and improvements).

Current liabilities decreased by 44.0% compared to last year mostly because of the decrease in funds due to the City of Reading.

Revenues. The following schedule presents a summary of revenue for the fiscal years ended December 31, 2008 and 2007:

	2008	2007	Increase (Decrease)
Water billings	\$ 16,604,898	\$ 16,387,626	\$ 217,272
Interest and penalty charges	341,901	818,503	(476,602)
Tampered meter and other charges	189,553	217,273	(27,720)
Tapping and connection fees	283,575	312,514	(28,939)
Abandonment fees	<u>87,264</u>	<u>90,289</u>	<u>(3,025)</u>
 Total operating revenues	 <u>\$ 17,507,191</u>	 <u>\$ 17,826,205</u>	 <u>\$ (319,014)</u>

The fiscal year's total operating revenue decreased 1.8% compared to the 2007 year.

Expenses. The following schedule presents a summary of expenses for the fiscal years ended December 31, 2008 and 2007:

	2008	2007	Increase
Operating expenses:			
Lease payments, City of Reading	\$ 13,276,508	\$ 12,830,326	\$ 446,182
Meter reading	451,906	430,386	21,520
Other	<u>1,642,129</u>	<u>1,156,847</u>	<u>485,282</u>
Total operating expenses	<u>\$ 15,370,543</u>	<u>\$ 14,417,559</u>	<u>\$ 952,984</u>

The largest portion of the Authority's \$ 952,984 increase in expenses is the result of an increase in lease payments to the City of Reading in the amount of \$ 446,182.

Changes in Net Assets. The following schedule presents a summary of changes in net assets for the fiscal years ended December 31, 2008 and 2007:

	2008	2007
Operating revenues	\$ 17,507,191	\$ 17,826,205
Operating expenses	<u>15,370,543</u>	<u>14,417,559</u>
Operating income before depreciation and amortization	2,136,648	3,408,646
Depreciation and amortization	<u>735,503</u>	<u>669,248</u>
Operating income	1,401,145	2,739,398
Nonoperating revenues (expenses)	<u>(799,149)</u>	<u>(422,965)</u>
Income before capital contributions	601,996	2,316,433
Capital contributions	<u>1,460,134</u>	<u>-</u>
Increase in net assets	<u>\$ 2,062,130</u>	<u>\$ 2,316,433</u>

**Statement of Changes in Net Assets
Year Ended December 31, 2008**

	Beginning Balance	Increase	Ending Balance
Invested in capital assets, net	\$ -	\$ -	\$ -
Restricted	4,661,253	781,064	5,442,317
Unrestricted	<u>-</u>	<u>1,281,066</u>	<u>1,281,066</u>
Total net assets	<u>\$ 4,661,253</u>	<u>\$ 2,062,130</u>	<u>\$ 6,723,383</u>

Capital Acquisitions. The Authority's investment in capital assets includes leasehold improvements, equipment, vehicles, computers and software, and construction in process. Major additions are funded by the issuance of water revenue bonds and notes or funds held in the Authority's construction accounts.

The Authority's capital assets as of December 31, 2008 and 2007, net of accumulated depreciation, amounted to \$ 16,568,878 and \$ 14,749,041, respectively. For the year ended December 31, 2008, this amount represents a net increase (including additions, deletions and depreciation) of \$ 1,819,837 from the prior year.

**Capital Assets at December 31
(Net of Accumulated Depreciation)**

	2008	2007
Leasehold improvements	\$ 13,464,297	\$ 8,250,616
Equipment	1,313,418	561,997
Vehicles	408,689	290,889
Computers and software	64,145	25,867
Construction in process	<u>1,318,329</u>	<u>5,619,672</u>
	<u>\$ 16,568,878</u>	<u>\$ 14,749,041</u>

Debt Administration. At December 31, 2008, the Authority had \$ 48,856,586 of Guaranteed Revenue Bonds and loans payable, compared to \$ 50,013,906 at the end of the 2007 year. The proceeds from these long-term borrowings will be used for renovations and improvements to the water system. See Note 5 for additional information on the Authority's debt.

Economic Factors

The Reading Area Water Authority will continue to address the existing infrastructure by addressing the rehabilitation needs of the system, as well as pursue possible extension of the water system into new areas.

Future investments include relining of water mains throughout the existing system, replacement of water meters to increase revenue, cleaning of finished water reservoirs to uphold water quality, address PADEP requirements for the Lake Ontelaunee Dam and address sediment within Lake Ontelaunee.

Request for Information

This financial report is intended to provide an overview of the finances of the Reading Area Water Authority for those with an interest in the Authority. Questions concerning any information contained in the report may be directed to the Executive Director, Reading Area Water Authority, 815 Washington Street, Reading, PA 19601.

**READING AREA WATER AUTHORITY
A COMPONENT UNIT OF THE CITY OF READING**

**STATEMENT OF NET ASSETS
December 31, 2008**

ASSETS

UNRESTRICTED CURRENT ASSETS

Cash	\$ 7,160,432
Accounts receivable, billings, net of allowance of \$ 1,556,065	2,011,542
Accounts receivable, other	1,522,284
Accrued interest receivable	33,211
Prepaid expenses	6,973
	<u>10,734,442</u>
Total unrestricted current assets	10,734,442

RESTRICTED CURRENT ASSETS

Developer escrow deposits, cash	<u>150,552</u>
Trust accounts, cash and investments:	
Clearing Account	10,176
Construction Account	19,249,101
Debt Service Account	1,479,574
Debt Service Reserve Account	3,962,743
	<u>24,701,594</u>
Total restricted current assets	24,852,146

CAPITAL ASSETS

Capital assets not being depreciated, construction in progress	<u>1,318,329</u>
Capital assets being depreciated:	
Leasehold improvements	15,834,380
Equipment	2,150,491
Vehicles	1,168,306
Computers and software	356,334
	<u>19,509,511</u>
Less accumulated depreciation	4,258,962
	<u>15,250,549</u>
Capital assets, net	16,568,878

OTHER ASSETS

Due from City of Reading, Pennvest loan assumption	4,065,603
Unamortized bond issuance costs, net of accumulated amortization of \$ 231,270	961,468
	<u>5,027,071</u>
	\$ 57,182,537

See Notes to Financial Statements.

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES

Current maturities of long-term debt	\$ 1,748,544
Accounts payable	91,255
Accrued interest payable	110,052
Escrow deposits	147,779
Due to City of Reading	1,253,482

Total current liabilities 3,351,112

LONG-TERM DEBT, less current maturities 47,108,042

COMMITMENTS AND CONTINGENCY -

NET ASSETS

Invested in capital assets, net of related debt	-
Restricted for debt service	5,442,317
Unrestricted	1,281,066

6,723,383

\$ 57,182,537

**READING AREA WATER AUTHORITY
A COMPONENT UNIT OF THE CITY OF READING**

**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
Year Ended December 31, 2008**

Operating revenues:	
Water billings	\$ 16,604,898
Interest and penalty charges	341,901
Tampered meter and other charges	189,553
Tapping and connection fees	283,575
Abandonment fees	87,264
	<u>17,507,191</u>
Total operating revenues	
 Operating expenses:	
Lease payments, City of Reading	13,276,508
Meter reading	451,906
Engineering	79,926
Legal fees	85,105
Salaries and payroll taxes	105,097
Collections expense	193,709
Insurance	95,147
Employee benefits	7,959
Grand expenditures	54,682
Telephone	10,733
Contracted services	117,085
Repairs and maintenance	260,161
Audit and accounting	53,529
Bank charges	8,676
Advertising	2,526
Education	2,282
Supplies	2,747
Other professional services, rate study	15,000
Bad debt expense	547,765
	<u>15,370,543</u>
Total operating expenses	
Operating income before depreciation and amortization	
	<u>2,136,648</u>
Depreciation and amortization:	
Depreciation	671,116
Amortization of bond issuance costs	64,387
	<u>735,503</u>
Operating income	
	<u>1,401,145</u>

READING AREA WATER AUTHORITY
A COMPONENT UNIT OF THE CITY OF READING

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS (CONTINUED)
Year Ended December 31, 2008

Nonoperating revenues (expenses):	
Investment income	\$ 756,337
Swap income, net	421,325
Miscellaneous income	5,053
Interest expense	(1,957,754)
Miscellaneous expense	(24,110)
	<u>(799,149)</u>
Income before capital contributions	601,996
Capital contributions	<u>1,460,134</u>
Increase in net assets	<u>2,062,130</u>
Net assets, beginning, as previously reported	4,610,219
Prior period adjustments	<u>51,034</u>
Net assets, beginning, as restated	<u>4,661,253</u>
Net assets, ending	<u>\$ 6,723,383</u>

See Notes to Financial Statements.

**READING AREA WATER AUTHORITY
A COMPONENT UNIT OF THE CITY OF READING**

**STATEMENT OF CASH FLOWS
Year Ended December 31, 2008**

CASH FLOWS FROM OPERATING ACTIVITIES

Cash receipts from customers	\$ 17,962,905
Cash payments to suppliers for goods and services	(17,445,324)
Cash payments to employees for services	<u>(105,097)</u>

Net cash provided by operating activities	<u>412,484</u>
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CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

Increase in escrow liability, net	72,391
Miscellaneous income received	5,053
Miscellaneous expenses paid	(11,643)
Cash receipts from grants	<u>184,686</u>

Net cash provided by noncapital financing activities	<u>250,487</u>
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**CASH FLOWS FROM CAPITAL AND RELATED FINANCING
ACTIVITIES**

Acquisition and construction of capital assets	(2,553,103)
Principal paid on long-term debt	(423,879)
Interest paid on long-term debt	<u>(1,402,686)</u>

Net cash used in capital and related financing activities	<u>(4,379,668)</u>
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CASH FLOWS FROM INVESTING ACTIVITIES

Decrease in restricted assets, net	1,824,233
Swap income received, net	421,325
Investment income received	<u>805,160</u>

Net cash provided by investing activities	<u>3,050,718</u>
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Net decrease in cash	(665,979)
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Cash:

Beginning	<u>7,826,411</u>
Ending	<u><u>\$ 7,160,432</u></u>

**READING AREA WATER AUTHORITY
A COMPONENT UNIT OF THE CITY OF READING**

**STATEMENT OF CASH FLOWS (CONTINUED)
Year Ended December 31, 2008**

**RECONCILIATION OF OPERATING INCOME TO NET
CASH PROVIDED BY OPERATING ACTIVITIES**

Operating income	\$ 1,401,145
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	671,116
Amortization	64,387
Changes in assets and liabilities:	
Decrease in accounts receivable	1,003,479
(Increase) in prepaid expenses	(1,973)
(Decrease) in accounts payable	(177,035)
(Decrease) in due to City of Reading	<u>(2,548,635)</u>
Net cash provided by operating activities	<u>\$ 412,484</u>

NONCASH CAPITAL AND FINANCING ACTIVITIES

Payment by City of Reading, Pennvest loan assumption applied to Pennvest note payable	\$ 1,296,286
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See Notes to Financial Statements.

**READING AREA WATER AUTHORITY
A COMPONENT UNIT OF THE CITY OF READING**

NOTES TO FINANCIAL STATEMENTS

Note 1. Nature of Activity and Significant Accounting Policies

Nature of activity:

The Reading Area Water Authority (the "Authority"), a component unit of the City of Reading, was created as an operating authority in 1995 in compliance with the Pennsylvania Municipality Authorities Act. The Authority was formed to provide water services to residential, commercial and industrial users of the water system for the City of Reading and certain surrounding municipalities. The Authority is governed by a five-member board, each of whom is appointed by the City of Reading.

A summary of the Authority's significant accounting policies follows:

The accompanying financial statements conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The following is a summary of the more significant accounting policies used by the Authority.

A. THE FINANCIAL REPORTING ENTITY

Accounting principles generally accepted in the United States of America require that the reporting entity include the primary government, organizations for which the primary government is financially accountable and other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. There are no agencies or entities which should be presented with the Authority.

The Authority is a component unit of the City of Reading, Berks County, Pennsylvania.

B. MEASUREMENT FOCUS, BASIS OF ACCOUNTING AND FINANCIAL STATEMENT PRESENTATION

The preparation of 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 at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of timing of related cash flows.

Private-sector standards of accounting and financial reporting issued prior to December 31, 1989 are generally followed to the extent that these standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The Authority has elected to follow subsequent private-sector guidance, subject to the same limitation.

NOTES TO FINANCIAL STATEMENTS

Note 1. Nature of Activity and Significant Accounting Policies (Continued)

A summary of the Authority's significant accounting policies follows (continued):

B. MEASUREMENT FOCUS, BASIS OF ACCOUNTING AND FINANCIAL STATEMENT PRESENTATION (CONTINUED)

Operating revenues and expenses are distinguished from nonoperating items in the statement of revenues, expenses and changes in net assets. Operating revenues and expenses generally result from providing services in connection with the Authority's principal ongoing operations. The principal operating revenues of the Authority are charges to customers for the sale of water. Operating expenses include the cost of providing services, administrative expenses, depreciation on capital assets and amortization on bond discount and issue costs. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. The principal nonoperating revenues and expenses of the Authority are interest expense, investment income and capital contributions.

When restricted and unrestricted resources are available for its use, it is the Authority's policy to use restricted resources first.

C. ASSETS, LIABILITIES AND NET ASSETS

In accordance with the terms of the trust indenture dated September 15, 2002, the first supplemental indenture dated July 1, 2003, and the second supplemental indenture dated July 15, 2007 (hereinafter collectively referred to as the "indentures"), relating to the bonded debt, funds of the Authority are accounted for by separate trust accounts; segregated for specific use and held for the benefit of the bondholders. In accordance with the indentures, the trust accounts maintained by the independent trustee are accounted for, by the trustee, using the cash basis method of accounting. A brief description of the purposes of the several revenue bond trust restricted accounts follows:

Project accounts:

Clearing Account:

Funds are deposited herein to cover principal and interest payments due on the bonds. Transfers are made to the Debt Service Account to make these payments.

Construction Account:

The Construction Account consists of funds deposited from the Settlement Account for the purpose of paying costs of capital additions.

Debt Service Account:

Semiannual transfers from the Clearing Account were recorded herein. Current debt service and sinking fund requirements of the bond issues are paid from this Account.

NOTES TO FINANCIAL STATEMENTS

Note 1. Nature of Activity and Significant Accounting Policies (Continued)

A summary of the Authority's significant accounting policies follows (continued):

C. ASSETS, LIABILITIES AND NET ASSETS (CONTINUED)

Project accounts (continued):

Debt Service Reserve Account:

This Account was funded by the trust indentures. The aggregate balance provides additional collateral for the bondholders.

Cash:

For purposes of reporting cash flows, the Authority considers all cash accounts, which are not subject to withdrawal restrictions or penalties, and all highly-liquid debt investments purchased with a maturity of three months or less to be cash.

Accounts receivable:

Accounts receivable are shown net of an allowance for uncollectibles, as applicable. Accounts receivables are evaluated for collectibility and an allowance is established, as deemed necessary, based on the best information available and in an amount that management believes is adequate. Accounts receivable are written off when deemed uncollectible. Recoveries of accounts receivable previously written off are recorded when received.

Investments:

The Board and trustee are permitted to invest the Authority's funds as defined in the Local Government Unit Debt Act, the Municipality Authorities Act and the related trust indentures. Authorized types of investments include the following:

- a. U. S. Treasury Bills.
- b. Short-term obligations of the U. S. Government and federal agencies.
- c. Insured savings and checking accounts and certificates of deposit in banks, savings and loan associations and credit unions.
- d. General obligation bonds of the federal government, the Commonwealth of Pennsylvania or any state agency, or of any Pennsylvania political subdivision.
- e. Shares of mutual funds whose investments are restricted to the above categories.

When making investments, the Board and trustee can combine monies from more than one fund under the Authority's control for the purchase of a single investment and join with other political subdivisions and municipal authorities in the purchase of a single investment.

Investments are carried at fair value.

NOTES TO FINANCIAL STATEMENTS

Note 1. Nature of Activity and Significant Accounting Policies (Continued)

A summary of the Authority's significant accounting policies follows (continued):

C. ASSETS, LIABILITIES AND NET ASSETS (CONTINUED)

Capital assets:

Capital assets are stated at cost. Depreciation of capital assets is computed on the straight-line method over the following estimated useful lives:

	Years
Leasehold improvements	
Equipment	10-40
Vehicles	3-7
Computers and software	5-7
	3-5

Maintenance and repairs of capital assets are charged to operations and major improvements are capitalized. Upon retirement, sale or other disposition of capital assets, the cost and accumulated depreciation are eliminated from the accounts and gain or loss is included in operations. Interest costs incurred during the construction period of major projects are capitalized and amortized over the life of the asset.

Bond discounts/issuance costs:

Bond/note discount and issuance costs are deferred and amortized over the term of the bonds using the effective interest method. Bond discounts are presented as a reduction of the face amount of the revenue bonds payable, whereas issuance costs are recorded as an other asset.

Net assets:

Net assets are classified into three categories as follows:

Invested in capital assets consists of capital assets, net of accumulated depreciation and debt incurred for the acquisition of capital assets.

Restricted net assets are amounts that have externally imposed restrictions on how the funds can be spent.

Unrestricted net assets are amounts that do not meet the definitions of "invested in capital assets" or "restricted" and are available for Authority operations.

Note 2. Stewardship, Compliance and Accountability

Compliance with finance-related legal and contractual provisions:

The Authority had no material violations of finance-related legal and contractual provisions in regard to the terms, covenants, provisions or conditions contained in the trust indentures relating to the bond issues.

NOTES TO FINANCIAL STATEMENTS

Note 3. Cash and Investments

The carrying amounts of cash and investments at December 31, 2008 consist of the following:

Petty cash	\$ 2,355
Demand deposit accounts	7,308,629
Investments	<u>24,701,594</u>
	<u>\$ 32,012,578</u>
Classification per statement of net assets:	
Unrestricted current assets, cash	\$ 7,160,432
Restricted current assets:	
Developer escrow deposits, cash	150,552
Trust accounts, cash and investments	<u>24,701,594</u>
	<u>\$ 32,012,578</u>

Cash:

The Authority's available cash is invested in demand deposit accounts.

The Authority has custodial credit risk on cash deposits. This is the risk that in the event of a financial institution failure, the Authority's deposits may not be returned. The Authority has a deposit policy for custodial risk that requires depository institutions to pledge securities as collateral for deposits that exceed depository insurance.

At December 31, 2008, the carrying amounts of the Authority's bank deposits were \$ 7,308,629 and the bank balances were \$ 6,870,784, of which \$ 250,000 was covered by Federal Depository Insurance. The remaining \$ 6,620,784 of deposits were exposed to custodial risk because they were uninsured and collateralized with securities held by the pledging financial institution's trust department or agent, but not in the Authority's name. The Authority has a petty cash balance of \$ 2,355 at December 31, 2008.

Investments:

As of December 31, 2008, the Authority has the following investments and maturities with M&T Bank:

	- Investment Maturities (in Years) -	
	Fair Value	Less than One Year
Federated Treasury Obligation Funds	\$ 563,317	\$ 563,317
Morgan Stanley Institutional Liquidity Funds, Government Portfolio	20,582,676	20,582,676
Federal Home Loan Mortgage Corp Discount Note	1,055,611	1,055,611
Federal National Mortgage Association Pool	<u>2,499,990</u>	<u>2,499,990</u>
	<u>\$ 24,701,594</u>	<u>\$ 24,701,594</u>

NOTES TO FINANCIAL STATEMENTS

Note 3. Cash and Investments (Continued)

Interest rate risk:

The Authority does not have a formal investment policy that limits maturities in certain investments as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit risk:

The Authority does not have an investment policy that would limit its investment choices to certain credit ratings. However, the Authority limits the type of investments permitted as defined in the Local Government Unit Debt Act, the Municipality Authorities Act and the related trust indentures. Permitted investments are defined in Note 1.

Custodial credit risk:

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. As of December 31, 2008, \$ 24,701,594 is held by the investment's counterparty, not in the name of the Authority.

Note 4. Capital Assets

Capital asset activity for the year ended December 31, 2008 was as follows:

	Balance January 1, 2008	Additions	Deletions	Balance December 31, 2008
Capital assets not being depreciated, construction in progress	<u>\$ 5,619,672</u>	<u>\$ 1,800,037</u>	<u>\$ 6,101,380</u>	<u>\$ 1,318,329</u>
Capital assets being depreciated:				
Leasehold improvements	10,263,846	5,570,534	-	15,834,380
Equipment	1,253,805	896,686	-	2,150,491
Vehicles	907,730	260,576	-	1,168,306
Computers and software	<u>291,834</u>	<u>64,500</u>	<u>-</u>	<u>356,334</u>
Total capital assets being depreciated	<u>12,717,215</u>	<u>6,792,296</u>	<u>-</u>	<u>19,509,511</u>

NOTES TO FINANCIAL STATEMENTS

Note 4. Capital Assets (Continued)

	Balance January 1, 2008	Additions	Deletions	Balance December 31, 2008
Less accumulated depreciation for:				
Leasehold improvements	\$ 2,013,230	\$ 356,853	\$ -	\$ 2,370,083
Equipment	691,808	145,265	-	837,073
Vehicles	616,841	142,776	-	759,617
Computers and software	<u>265,967</u>	<u>26,222</u>	<u>-</u>	<u>292,189</u>
Total accumulated depreciation	<u>3,587,846</u>	<u>671,116</u>	<u>-</u>	<u>4,258,962</u>
Total capital assets being depreciated, net	<u>9,129,369</u>	<u>6,121,180</u>	<u>-</u>	<u>15,250,549</u>
Total capital assets, net	<u>\$ 14,749,041</u>	<u>\$ 7,921,217</u>	<u>\$ 6,101,380</u>	<u>\$ 16,568,878</u>

Note 5. Long-Term Debt

At December 31, 2008, long-term debt consisted of the following:

	Balance Outstanding December 31, 2007	Payments	Balance Outstanding December 31, 2008
Note payable to a bank in quarterly principal payments ranging from \$ 21,366 to \$ 23,300 plus monthly interest payments calculated at a variable rate through February 2011	\$ 284,735	\$ (82,943)	\$ 201,792
Note payable PENNVEST, due in monthly payments of \$ 18,405, including interest at 3.997% to December 2017, secured by a lien and security interest in substantially all Authority assets	1,818,132	(150,936)	1,667,196
Note payable PENNVEST, due in monthly payments of \$ 111,998, including interest at 1.000% through January 2012, guaranteed by the City of Reading	5,361,889	(1,296,286)	4,065,603
Guaranteed Water Revenue Bonds, Series of 2002, initial issue \$ 3,250,000, various interest rates ranging from 1.300% to 4.400%, maturing in amounts ranging from \$ 190,000 to \$ 265,000 through 2017	2,255,000	(190,000)	2,065,000

NOTES TO FINANCIAL STATEMENTS

Note 5. Long-Term Debt (Continued)

	Balance Outstanding December 31, 2007	Payments	Balance Outstanding December 31, 2008
Guaranteed Water Revenue Bonds, Series of 2003 (Capital Appreciation Bonds), initial issue \$ 21,080,000, various interest rates ranging from 3.600% to 4.620%, maturing in amounts ranging from \$ 610,000 to \$ 2,690,000 through 2020	\$ 21,080,000	\$ -	\$ 21,080,000
Guaranteed Water Revenue Bonds, Series of 2007, initial issue \$ 25,000,000, various interest rates ranging from 4.250% to 5.000%, maturing in amounts ranging from \$ 125,000 to \$ 3,860,000 through 2027	<u>25,000,000</u>	<u>-</u>	<u>25,000,000</u>
	<u>\$ 55,799,756</u>	<u>\$ (1,720,165)</u>	<u>\$ 54,079,591</u>

Aggregate maturities required on the long-term debt at December 31, 2008 are as follows:

	Principal	Interest	Total
2009	\$ 1,748,544	\$ 1,420,912	\$ 3,169,456
2010	1,782,478	1,393,866	3,176,344
2011	2,478,973	1,427,972	3,906,945
2012	2,560,142	1,601,730	4,161,872
2013	2,579,264	1,668,900	4,248,164
2014-2018	13,730,190	9,439,116	23,169,306
2019-2023	14,820,000	7,629,351	22,449,351
2024-2027	<u>14,380,000</u>	<u>1,841,250</u>	<u>16,221,250</u>
	<u>\$ 54,079,591</u>	<u>\$ 26,423,097</u>	<u>\$ 80,502,688</u>

Total long-term debt payable	\$ 54,079,591
Less current maturities	(1,748,544)
Plus unamortized bond premium	848,433
Less unamortized interest on capital appreciation bonds	<u>(6,071,438)</u>
	<u>\$ 47,108,042</u>

Bonds payable:

The bonds are secured under the indentures by an assignment and pledge to the trustee of receipts and revenues from the water system.

NOTES TO FINANCIAL STATEMENTS

Note 5. Long-Term Debt (Continued)

Derivative financial instrument:

Interest rate swap - In July 2005, the Authority entered into a forward interest rate swap agreement with a financial institution in conjunction with its Guaranteed Water Revenue Bonds, Series of 2003. The agreement uses an underlying index of 67% of 30-day LIBOR versus the BMA Municipal Bond Index.

The fair value liability as of December 31 is as follows:

Notional Amount	Effective Date	Maturity Date	January 1, 2008, Beginning	Decrease	December 31, 2008, Ending
\$ 21,080,000	June 1, 2005	November 1, 2020	\$ (204,339)	\$ (604,193)	\$ (808,532)

During the year ended December 31, 2008, the Authority terminated an interest rate swap and recognized a gain of \$ 421,325.

Note 6. Operating Lease

The Authority has entered into a 99-year operating lease, effective June 1, 1994, with the City of Reading for the operations of the water system. Lease payments are the sum of agreed upon administrative expenses, operating expenses, debt service expenses and financing fees of the City of Reading. In addition, the Authority must provide water service free of charge to the City. Lease payments are made monthly based on an estimate of the anticipated lease payments for the year. At the end of the year, the Authority receives an annual reconciliation statement, which reflects a credit due to the Authority or a payment due to the City. Total lease expense for the year ended December 31, 2008 was \$ 13,276,508.

Note 7. Commitments and Contingency

Commitments:

Management agreement:

The Authority has entered into an agreement with Miller Environmental, Inc. for the services of a qualified water filter plant manager, who is responsible for the management of all operational and maintenance activities of the water filter plant. The agreement is automatically renewable annually unless one of the parties gives written notice of their intent to terminate the agreement. Total expense under the agreement for the year ended December 31, 2008 was \$ 117,085.

NOTES TO FINANCIAL STATEMENTS

Note 7. Commitments and Contingency (Continued)

Commitments (continued):

Water reading services agreement:

The Authority has entered into an agreement with Miller Environmental, Inc. to perform water reading services in the Authority's service area. Under the terms of the agreement, the Authority pays a monthly operating fee of \$ 29,624 plus additional hourly charges for services performed outside the scope of the agreement. The monthly fee and hourly rates are subject to a 5% increase per year effective March 1 of each year. The agreement was extended March 1, 2006 for a three year term and is automatically renewable for three-year terms unless one of the parties gives written notice of their intent to terminate the agreement. Total expense under the agreement for the year ended December 31, 2008 was \$ 451,906.

Capital improvements:

The Authority has entered into contracts for various capital improvements of approximately \$ 885,000 as of December 31, 2008.

In January 2004, an agreement was established between the Authority, Ontelaunee Township and Ontelaunee Township Municipal Authority (OTMA) to extend water service into Ontelaunee Township and provide public water for resale. The Authority is to pay the costs associated with the extension and OTMA agreed to reimburse the Authority for 50% of the total costs no later than one year after the water extension is placed in service. As of December 31, 2008, the extension was placed in service. A receivable of \$ 1,460,134 was recorded as of December 31, 2008 for the amount owed by OTMA to the Authority for its portion of the costs which was received in April 2009.

Contingency:

The Authority has an unused letter of credit of \$ 800,000 at December 31, 2008.

Note 8. Prior Period Adjustment

The December 31, 2007 net assets were increased by \$ 51,034 to record accrued interest receivable of \$ 82,034 and to expense capital asset items of \$ 31,000.