



Wastewater Utility Fund of the City of Norfolk, Virginia

Financial and Compliance Report
Year Ended June 30, 2008



KPMG LLP
Suite 2100
999 Waterside Drive
Norfolk, VA 23510

KPMG LLP, a U.S. limited liability partnership, is the U.S.
Member firm of KPMG International, a Swiss cooperative

Contents

Independent Auditors' Report	1 - 2
------------------------------	-------

Financial Statements	
Statement of Net Assets	3
Statement of revenues, expenses and changes in fund net assets	4
Statement of cash flows	5 - 6
Notes to financial statements	7 - 15

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i>	16 - 17
--	---------



KPMG LLP
Suite 2100
999 Waterside Drive
Norfolk, VA 23510

Independent Auditors' Report

The Honorable Members of the City Council
Wastewater Utility Fund of the City of Norfolk, Virginia:

We have audited the accompanying statement of net assets of the Wastewater Utility Fund of the City of Norfolk, Virginia (the Fund) as of June 30, 2008, and the related statement of revenues, expenses and changes in fund net assets and cash flows for the year then ended. These financial statements are the responsibility of the management of the City of Norfolk. 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; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and *Specifications or Audits of Counties, Cities and Towns* (Specifications), issued by the Auditor of Public Accounts of the Commonwealth of Virginia. Those standards and specifications 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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.

As discussed in note 1 to the financial statements, the accompanying financial statements present only the Wastewater Utility Fund and do not purport to, and do not, present fairly the financial position of the City of Norfolk, Virginia, the changes in its financial position or its cash flows, where applicable, in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Fund of the City of Norfolk, Virginia as of June 30, 2008, and the changes in its financial position and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

The Fund has not presented a Management's Discussion and Analysis that U.S. generally accepted accounting principles has determined is necessary to supplement, although not be a part of, the financial statements.



In accordance with *Government Auditing Standards*, we have also issued our report dated February 10, 2009 on our consideration of the Fund's internal control over financial reporting and 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 read in conjunction with this report in assessing the results of our audit.

KPMG LLP

February 10, 2009

Wastewater Utility Fund of the City of Norfolk, Virginia
Statement of Net Assets
June 30, 2008

	<u>2008</u>
ASSETS	
Current assets:	
Cash and cash equivalents	\$ 2,836,730
Receivables:	
Accounts (net)	3,095,876
Unbilled accounts	1,235,700
Other receivables	2,754
Inventories	46,488
Restricted cash held in escrow	156,538
Total current assets	<u>7,374,086</u>
Restricted investments	<u>28,041,294</u>
Capital Assets:	
Land and construction in progress	22,335,760
Buildings and equipment, net of accumulated depreciation	140,799,202
Total noncurrent assets	<u>163,134,962</u>
Total assets	<u>198,550,342</u>
LIABILITIES	
Current liabilities:	
Vouchers payable	1,425,964
Contract retainage	487,270
Due to Capital Project fund and Special Revenue fund	6,697,093
Accrued interest	772,900
Accrued payroll	107,073
Payable to employee retirement system	352,800
Current portion of bonds payable	6,150,117
Compensated absences	218,163
Liability for other post employment benefits (OPEB)	126,592
Other liabilities	341,059
Total current liabilities	<u>16,679,031</u>
Noncurrent liabilities:	
General obligation bonds payable	96,702,854
Revenue bonds payable	7,359,833
Compensated absences	112,137
Total noncurrent liabilities	<u>104,174,824</u>
Total liabilities	<u>120,853,855</u>
NET ASSETS	
Invested in capital assets, net of related debt	80,476,182
Unrestricted	(2,779,695)
Total net assets	<u>\$ 77,696,487</u>

See Notes to Financial Statements

Wastewater Utility Fund of the City of Norfolk, Virginia
Statement of Revenues, Expenses and Changes in Fund Net Assets
Year Ended June 30, 2008

	2008
Operating revenues:	
Charges for services	\$ 24,917,036
Miscellaneous	172,390
Total operating revenues	<u>25,089,426</u>
Operating expenses:	
Personnel services	4,479,932
Plant operations	2,059,011
Chemicals	96,869
Provision for bad debts	577,686
Depreciation	3,702,273
Retirement contribution	352,800
OPEB expense	126,592
Administrative expenses	1,568,756
Other	3,290,566
Total operating expenses	<u>16,254,485</u>
Operating income	<u>8,834,941</u>
Nonoperating revenue (expenses):	
Interest income, net of interest capitalized	558,712
Interest expense and fiscal charges, net of interest capitalized	(2,359,248)
Loss on sale or disposal of fixed assets	(534)
Total nonoperating expenses	<u>(1,801,070)</u>
Income before contributions and transfers	<u>7,033,871</u>
Capital contributions	43,240
Transfers out	(1,632,612)
Change in net assets	<u>5,444,499</u>
Total net assets - beginning	<u>72,251,988</u>
Total net assets - ending	<u>\$ 77,696,487</u>

See Notes to Financial Statements

Wastewater Utility Fund of the City of Norfolk, Virginia

Statement of Cash Flows
Year Ended June 30, 2008

	2008
CASH FLOWS FROM OPERATING ACTIVITIES:	
Receipts from customers	\$ 23,340,373
Payments to suppliers	(3,702,264)
Payments to employees	(4,920,109)
Other payments/receipts	(4,889,340)
Net cash provided by operating activities	<u>9,828,660</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:	
Internal activity, payments to other funds	(3,507,605)
Transfers out	(1,632,612)
Net cash used in noncapital financing activities	<u>(5,140,217)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:	
Proceeds from sale of debt	43,515,845
Contributed capital	43,240
Purchases of capital assets	(21,242,014)
Principal paid on capital debt	(5,031,831)
Interest paid on capital debt	(2,460,021)
Net cash provided by capital and related financing activities	<u>14,825,219</u>
CASH FLOWS FROM INVESTING ACTIVITIES:	
Purchase of investments	(43,841,836)
Proceeds from sale or maturity of investments	17,435,798
Interest and dividends	558,712
Net cash used in investing activities	<u>(25,847,326)</u>
Net decrease in cash and cash equivalents	(6,333,664)
Cash and cash equivalents - beginning of the year	<u>9,326,932</u>
Cash and cash equivalents - end of the year	<u><u>\$ 2,993,268</u></u>

(Continued)

Wastewater Utility Fund of the City of Norfolk, Virginia

Statement of Cash Flows (Continued)

Year Ended June 30, 2008

Reconciliation of Operating Income to Net Cash

Provided by Operating Activities:

Operating income	\$ 8,834,941
Adjustments to reconcile operating income to net cash provided by operating activities:	
Provision for bad debts	577,686
Depreciation expense	3,702,273
Change in assets and liabilities:	
Accounts receivable (net), billed and unbilled	(1,749,053)
Inventories	496
Vouchers payable	(1,546,880)
Accrued payroll	(87,377)
Other liabilities	96,574
Net cash provided by operating activities	<u>\$ 9,828,660</u>

Reconciliation of cash and cash equivalents to the statement of net assets:

Cash and cash equivalents	\$ 2,836,730
Restricted cash held in escrow	156,538
Total cash and cash equivalents per statement of net assets	<u>\$ 2,993,268</u>

Noncash investing, capital and financing activities:

Loss on sale or disposal of capital assets	\$ (534)
Acquisition of fixed assets through change in contract retainage	<u>\$ (248,815)</u>
Acquisition of fixed assets through vouchers payable	<u>\$ (1,175,176)</u>
Capitalized interest	<u>\$ 684,368</u>

See Notes to Financial Statements

Wastewater Utility Fund of the City of Norfolk, Virginia

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies

The Wastewater Utility Fund of the City of Norfolk, Virginia (the "Fund") was established at the direction of Norfolk City Council as an enterprise fund on July 1, 1984. The Fund accounts for the operation of the wastewater system owned by the City of Norfolk (the "City"). The costs of providing services on a continuing basis are financed or recovered through user charges to the City's residential and commercial customers. Activities necessary to provide wastewater services, including operations, maintenance, financing and related debt service, and billing and collection, are accounted for in the Fund. Although separate financial statements have been presented for the Fund, it is also included in the City of Norfolk's Comprehensive Annual Financial Report as a major Enterprise Fund.

A summary of the Fund's significant accounting policies are as follows:

Basis of accounting: The financial statements are presented on the accrual- basis of accounting, wherein revenues are recognized in the accounting period in which it is earned and expenses are recognized in the accounting period in which the related liabilities are incurred. The Fund adopted 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*. Accordingly, the Fund has elected not to apply Statements and Interpretations issued by the Financial Accounting Standards Board after November 30, 1989.

Deposits and Investments: The Fund's cash and short-term investments include cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

Investments of the Fund are stated at fair value. Short-term investments are recorded at cost, which approximates fair value. The fair value of the State Treasurer's Local Government Investment Pool (LGIP) is the same as the value of the pool shares. The LGIP is not registered with the Securities and Exchange Commission (SEC) as an investment company, but maintains a policy to operate in a manner consistent with the SEC's Rule 2a7 of the Investment Company Act of 1940. The external investment pool is administered by the Treasury Board of Virginia. Other investments are stated at their fair value; these investments are reported in the accompanying financial statements as cash and short-term investments, unless the original investment period exceeded three months, in which case they are reported as investments.

Investment income includes both realized and unrealized gain and loss components.

Accounts receivable: Accounts receivable are receivables due at the end of the fiscal year which has not been collected by year-end, net of allowance for doubtful accounts. The Fund determines past due-status of individual wastewater utility account receivables based on contractual terms and generally does not charge interest on past-due amounts. The Fund estimates its allowance for doubtful accounts based on a combination of factors, including the Fund's historical loss experience and any anticipated effects related to current economic conditions, as well as management's knowledge of the current composition of wastewater receivables. Accounts that management believes to be ultimately not collectible are written off upon such determination. Unbilled accounts, net, are estimated at each fiscal year end based on wastewater usage by customers for which billings have not been processed.

Inventories: Inventories are stated at the lower of cost (using the moving average method) or market.

Restricted assets: Certain unspent proceeds of the general obligation bonds as well as certain resources set aside for their repayment are classified as restricted assets on the statement of net assets because they are maintained in separate bank accounts and their use is limited by applicable bond covenants.

Wastewater Utility Fund of the City of Norfolk, Virginia

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Capital assets: Capital assets are recorded at cost, less accumulated depreciation. Assets acquired prior to July 1977, for which historical cost records were not available, were appraised and valued at estimated historical cost by means of accepted price indexing methodology.

Depreciation: Depreciation is computed using the straight-line method over the following estimated useful lives:

	<u>Years</u>
Buildings and improvements	40 - 75
Transmission and distribution mains	50 - 99
Service meters and meter installation	35 - 50
Pumping and other wastewater equipment	10 - 30
Furniture, fixtures and equipment	5 - 25

When an asset is retired or otherwise disposed of, the related cost and accumulated depreciation is eliminated from the accounts and any resulting gain or loss is reflected as nonoperating revenue or expense.

Interest costs incurred on funds borrowed for construction projects are capitalized, net of interest earned on the temporary investment of the unexpended portion of those funds.

The Fund evaluates prominent events or changes in circumstances affecting capital assets to determine whether impairment of a capital asset has occurred. A capital asset is generally considered impaired if both (a) the decline in service utility of the capital asset is large in magnitude and (b) the event or change in circumstance is outside the normal life cycle of the capital asset. Impaired capital assets that will no longer be used by the government are reported at the lower of carrying value or fair value. Impairment losses on capital assets that will continue to be used by the government are measured using the method that best reflects the diminished service utility of the capital asset. Any insurance recoveries received as a result of impairment events or changes in circumstances resulting in the impairment of a capital asset are netted against the impairment loss.

Compensated absences: It is the Fund's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. Vacation leave is fully vested when earned by Fund employees. Sick leave does not vest for Fund employees; however, upon retirement, Fund employees receive credit for each day of accumulated sick leave toward their pension benefit. There is no liability for unpaid accrued sick leave service since the Fund does not pay when the employee separates from service.

Net assets: Net assets in the financial statements are classified as invested in capital assets, net of related debt; restricted; and unrestricted. Restricted net assets represent constraints on resources that are either externally imposed by creditors, grants, contributions, laws and regulations of other governments or imposed by law through state statute.

Operating and nonoperating revenues: The Fund reports as operating revenues all charges for services generated through service fees and certain other miscellaneous revenues. Other revenues, including interest revenue and grants, are reported as nonoperating. When both restricted and unrestricted resources are available for use, the policy is to use restricted resources first, and then unrestricted resources as they are needed.

Due to/from other funds: The General Fund of the City provides administrative services to the Fund, which totaled \$1,500,000 for the year ended June 30, 2008. Charges for these services are treated as expenses by the Fund. In

Wastewater Utility Fund of the City of Norfolk, Virginia

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

addition the Fund recorded, as other expenses, payments to the General Fund in lieu of taxes of \$72,825 for the year ended June 30, 2008.

Bond premium or discount: Premium or discount on bonds is amortized, using the effective-interest method, over the life of the debt and is included in interest expense.

Deferred gain (loss) on advance refunding: Gain (loss) on advance refunding is amortized, using the effective-interest method, over the shorter of the life of the refunded bonds or the life of the new bonds.

Use of estimates: The preparation of financial statements 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.

Note 2. Cash and Investments

Deposits: All cash of the Fund is maintained in accounts collateralized in accordance with the Virginia Security for Public Deposits Act, Section 2.2-4400 et. seq. of the Code of Virginia or covered by federal depository insurance.

Investments: Statutes authorize the Fund to invest in obligations of the United States or agencies thereof, obligations of the Commonwealth of Virginia or political subdivisions thereof, obligations of the International Bank for Reconstruction and Development ("World Bank") and Asian Development Bank, the African Development Bank, commercial paper rated A-1 by Standard and Poor's or P-1 by Moody's Commercial Paper Record, banker's acceptances, repurchase agreements, and the State Treasurer's Local Government Investment Pool ("LGIP"), certain mutual funds, corporate notes, asset-backed securities, and savings accounts or time deposits.

The Fund has no formal policy regarding credit risk, interest rate risk, concentration of credit risk, custodial credit risk, or foreign investment risk.

The Fund has \$10,045 deposited in the State Treasurer's LGIP at June 30, 2008 which has a Standard and Poor's rating of AAAM which is included in cash and cash equivalents.

The Fund's investments are considered to be mutual fund investment types and have a maturity of less than one year.

Investment Type	2008	
	Fair Value	
	Less than 1 year	
CCRF VAIM Prime Portfolio MMF	\$	1,809,277
SNAP Money Market Mutual Funds		26,232,017
	\$	28,041,294

Wastewater Utility Fund of the City of Norfolk, Virginia

Notes to Financial Statements

Note 2. Cash and Investments (Continued)

The Fund's rated investments, other than in LGIP, as of June 30, 2008 were rated by Standard and Poor's and the ratings presented below using the Standard and Poor's rating scale.

Investment Type	Fiscal Year 2008						Total
	AAA	AAAm	A-1+	AA+	AA	AA-	
Money Market Mutual Funds							
SNAP Money Market Mutual Funds	\$ 3,567,554	\$ -	\$ 21,379,094	\$ 682,032	\$ 52,464	\$ 550,872	\$ 26,232,017
CCRF VAIM Prime Portfolio MMF	-	1,809,277	-	-	-	-	1,809,277
Total Money Market Mutual Funds	\$ 3,567,554	\$ 1,819,322	\$ 21,379,094	\$ 56,685,924	\$ 56,633,460	\$ 56,082,588	\$ 28,041,294

The City's Wastewater Utility Fund has combined amounts restricted for capital projects and amounts for which the nature of the transaction generated a related liability with amounts available for general operating use in the statements for the Wastewater Fund. These amounts are not available to meet obligations arising from the operating activities of the Fund. These amounts are restricted by covenant related to the general obligation bond issue and/or by the external source of the originating transaction.

At June 30, 2008, the Fund's cash and investments consist of the following:

Investment in LGIP	\$ 10,045
Other investments	28,041,294
Cash	2,983,223
	<u>\$ 31,034,562</u>
Cash and cash equivalents	\$ 2,836,730
Restricted cash held in escrow	156,538
Restricted investments	28,041,294
	<u>\$ 31,034,562</u>

Certain cash and investments of the Fund are combined with other City monies for investment purposes. These amounts were covered by federal depository insurance or collateralized in accordance with the Virginia Security for Public Deposits Act. Reference should be made to the Comprehensive Annual Financial Report of the City of Norfolk for further cash and investment disclosures.

Note 3. Accounts Receivable

Accounts receivable at June 30, 2008 is comprised of the following:

Wastewater maintenance fees	2008
	<u>\$ 4,124,768</u>
Less allowance for uncollectible accounts	(1,028,892)
	<u>\$ 3,095,876</u>

Wastewater Utility Fund of the City of Norfolk, Virginia

Notes to Financial Statements

Note 4. Unbilled Accounts Receivable

At June 30, 2008, the Fund recognized \$1,235,700 as unbilled accounts receivable related to unread meters. The associated revenue is included in net charges for services.

Note 5. Capital Assets

Capital assets at June 30, 2008 are comprised of the following:

	Balance June 30, 2007	Additions	Retirements	Transfers	Balance June 30, 2008
Nondepreciable assets:					
Land	\$ 85,262	\$ -	\$ -	\$ -	\$ 85,262
Construction-in-progress	25,438,978	20,875,017	(2,172,858)	(21,890,639)	22,250,498
Total nondepreciable assets	<u>25,524,240</u>	<u>20,875,017</u>	<u>(2,172,858)</u>	<u>(21,890,639)</u>	<u>22,335,760</u>
Depreciable assets:					
Buildings and equipment	159,594,040	1,115,863	(90,256)	21,890,639	182,510,287
Less accumulated depreciation	(38,098,534)	(3,702,273)	89,722	-	(41,711,085)
Total depreciable assets, net	<u>121,495,506</u>	<u>(2,586,410)</u>	<u>(534)</u>	<u>21,890,639</u>	<u>140,799,202</u>
Total capital assets, net	<u>\$ 147,019,746</u>	<u>\$ 18,288,607</u>	<u>\$ (2,173,392)</u>	<u>\$ -</u>	<u>\$ 163,134,962</u>

The Fund capitalized \$684,368 of interest expense for the fiscal year ended June 30, 2008. Total interest cost for 2008 was \$3,043,616.

Note 6. Long-Term Obligations

General obligation bonds: A summary of general obligation bond transactions for the fiscal year ended June 30, 2008 follows:

	2008
Beginning, July 1	\$ 84,483,354
Bonds retired	(6,736,471)
Bonds issued	25,360,000
Bonds outstanding at June 30	<u>103,106,883</u>
Unamortized discount/premium	(253,912)
General obligation bonds outstanding at June 30, adjusted for unamortized discount/premium	102,852,971
Less current portion	(6,150,117)
	<u>\$ 96,702,854</u>

Wastewater Utility Fund of the City of Norfolk, Virginia

Notes to Financial Statements

Note 6. Long-Term Obligations (Continued)

Wastewater utility general obligation bonds outstanding are comprised of the following individual issues:

Bond Issue/Purpose	Dated	Issue Amount	Interest Rate	2008
Series 1997 Capital Improvement	04/15/1997	43,975,000	5.25 - 5.375%	\$ -
Series 1998 Capital Improvement	06/15/1998	44,330,000	4.25 - 5.00%	998,872
Series 1998 Refunding	06/15/1998	49,190,000	4.25 - 5.00%	1,884,076
Series 2002 Capital Improvement	02/01/2002	27,000,000	2.00 - 5.00%	4,653,955
Series 2002 Refunding	02/01/2002	47,200,000	2.00 - 5.00%	844,240
Series 2002B Refunding	11/01/2002	39,890,000	5.00 - 5.25%	1,804,821
Series 2003 VRA	04/08/2003	10,000,000	3.50%	8,125,599
Series 2003 Capital Improvement	11/15/2003	57,110,000	2.00 - 5.00%	879,846
Series 2003 Refunding	11/15/2003	12,265,000	3.00 - 4.00%	502,500
Series 2004 Refunding	03/01/2004	96,395,000	2.00 - 5.00%	6,464,288
Series 2004 VRA	09/17/2004	11,100,000	3.10%	10,462,196
Series 2005 Capital Improvement	03/16/2005	59,320,000	2.50 - 5.00%	1,720,000
Series 2005 Refunding	03/16/2005	35,035,000	2.50 - 5.00%	5,652,356
Series 2005 VRA	03/14/2006	11,500,000	3.00%	10,387,393
Series 2006 VRA	09/28/2006	14,250,000	-	13,438,839
Series 2006 Capital Improvement	11/15/2006	99,225,000	4.00 - 5.00%	9,579,500
Series 2006 Refunding	11/15/2006	15,830,000	4.00 - 5.00%	348,402
Series 2008 Capital Improvement	06/30/2008	26,230,118	4.00 - 5.00%	25,360,000
Wastewater Utility General Obligation Bonds outstanding				<u>\$ 103,106,883</u>

A summary of the requirements to amortize general obligation bonds outstanding at June 30, 2008 is as follows:

Year Ending	Principal	Interest
June 30, 2008		
2009	\$ 6,150,118	\$ 3,484,863
2010	6,585,615	3,534,323
2011	6,666,060	3,298,175
2012	6,592,873	3,023,699
2013	6,366,531	2,749,988
2014-2018	26,370,701	10,517,140
2019-2023	24,221,963	6,046,152
2024-2028	20,153,022	1,920,257
	<u>\$ 103,106,883</u>	<u>\$ 34,574,597</u>

General obligation bonds are payable first from the revenue of the specific funds in which they are recorded; however, the full faith and credit of the City are pledged to the payment of the principal and interest on general obligation bonds.

Revenue bonds: A summary of revenue bond transactions for the fiscal year ended June 30, 2008 is as follows:

	2008
Beginning, July 1	\$ -
Bonds issued	<u>7,359,833</u>
Bonds outstanding at June 30	<u>\$ 7,359,833</u>

Wastewater Utility Fund of the City of Norfolk, Virginia

Notes to Financial Statements

Note 6. Long-Term Obligations (Continued)

Wastewater utility revenue bonds outstanding are comprised of the following individual issues:

Bond Issue/Purpose	Dated	Issue Amount	Interest Rate	2008
Series 2007 VRA	11/9/2007	\$ 7,359,833	-	\$ 7,359,833
Wastewater Utility Revenue Bonds outstanding				<u>\$ 7,359,833</u>

A summary of the requirements to amortize revenue bonds outstanding at June 30, 2008 is as follows:

Year Ending June 30, 2008	Principal
2009	\$ -
2010	183,996
2011	367,992
2012	367,992
2013	367,992
2014-2018	1,839,958
2019-2023	1,839,958
2024-2028	1,839,958
2029-2030	551,987
	<u>\$ 7,359,833</u>

Wastewater revenue bond, Series 2007 VRA loan, is payable solely from the revenue of the Fund. The most restrictive covenant of the wastewater revenue bond requires that the Fund's net revenue available for debt service will equal at least 115% of the amount required during the fiscal year to pay the principal of the bond, the additional payments and all other indebtedness payable from revenues.

Bonds authorized and unissued as of June 30, 2008 were \$5,535,748.

Note 7. Retirement Obligations

The Fund contributes to the Employees' Retirement System of the City of Norfolk (the "System"), a single-employer noncontributory defined benefit plan, which is accounted for as a separate Pension Trust Fund. Reference should be made to the Comprehensive Annual Financial Report of the City of Norfolk for a further description of the plan. Retirement expense was \$352,800 for the year ended June 30, 2008.

Note 8. Commitments

Commitments for completion of capital projects authorized at June 30, 2008 were \$14,019,692.

Note 9. Litigation

From time-to-time, the Fund and the City are defendants in a number of lawsuits. Although it is not possible to determine the final outcome of these matters, management and the City attorney are of the opinion that the ultimate liability will not be material and will not have a significant effect on the Fund's financial condition.

Wastewater Utility Fund of the City of Norfolk, Virginia

Notes to Financial Statements

Note 10. Risk Management

The Fund is exposed to various risks of loss related to: theft of, damage to, and destruction of assets; injuries to employees; general liability; automobile liability; crime and employee dishonesty; professional liability; and directors and officers' liability. The Fund's coverage is provided through the City of Norfolk's combination of purchased insurance policies and self-insurance plans.

Note 11. Other Postemployment Benefits (OPEB)

The Fund adopted GASB Statement No. 45, Accounting and Financial Reporting by Employers for Other Postemployment Benefits (OPEB) in FY2008.

The City of Norfolk provides post-retirement health care benefits, in accordance with state statutes which require extending access to healthcare benefits to certain retirees. General City employees are eligible to participate at the earlier of age 55 and 15 years of creditable service or 25 years of creditable service. Employees who retire on accidental disability are also eligible. Retirees that elect to participate may purchase health care coverage using the same health care plans and premium structures available to active employees. Retiree participation, plan/benefit elections and contributions are administered by the City's Retirement Bureau based on the participation guidelines established by the Norfolk City Council.

Projections of benefits for financial reporting purposes are based on the plan and include the types of benefits provided at the time of each valuation. The actuarial methods and assumptions used include techniques designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. The actuarial valuation was performed as of July 1, 2007 with results projected for the fiscal year ended June 30, 2008.

The City's annual OPEB cost (expense) is calculated based on the annual required contribution (ARC), an amount actuarially determined in accordance with GASB Statement No. 45. Under this Statement, governments report on an accrual basis, benefit costs related to the period in which benefits are earned rather than to the period of benefit distribution. The annual required contribution represents a level of funding that, if paid on an on-going basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty years.

The Fund used the pay as you go method to calculate the OPEB liability for June 30, 2008 as the City Council had not voted as June 2008 to put any OPEB money in a trust. Using the most recent OPEB Plan Valuation Date of July 1, 2007, prepared by Cheiron, the City's actuary, the City has allocated to the Fund an ARC cost of \$126,592 and total OPEB liability for 2008 of \$912,795. The allocation is based on covered payroll and does not purport to represent the OPEB liability of the Fund on a stand-alone basis. Reference should be made to the Comprehensive Annual Financial Report of the City of Norfolk for further information.

Note 12. Accounting Pronouncements Issued But Not Yet Implemented

The GASB has issued several pronouncements prior to June 30, 2008 that have effective dates that may impact future financial presentations.

Management has not currently determined what, if any, impact implementation of the following statements may have on the financial statements of the Fund.

Note 12. Accounting Pronouncements Issued But Not Yet Implemented (Continued)

- GASB Statement 49, *Accounting and Financial Reporting of Pollution Remediation Obligations*. GASB 49 identifies the circumstances under which a governmental entity would be required to report a liability related to pollution remediation. According to the standard, a government would have to estimate its expected outlays for pollution remediation if it knows a site is polluted and any of the following recognition triggers occur:
 - Pollution poses an imminent danger to the public or environment and the government has little or no discretion to avoid fixing the problem.
 - A government has violated a pollution prevention-related permit or license.
 - A regulator has identified (or evidence indicates it will identify) a government as responsible (or potentially responsible) for cleaning up pollution, or for paying all or some of the cost of the clean up.
 - A government is named (or evidence indicates that it will be named) in a lawsuit to compel it to address the pollution.
 - A government begins or legally obligates itself to begin cleanup or post-cleanup activities (limited to amounts the government is legally required to complete).

Statement 49 requires governments to disclose information about their pollution obligations associated with clean up efforts in the notes of the financial statements. Statement 49 will be effective for financial statements for periods beginning after December 15, 2007, but liabilities should be measured at the beginning of that period so that the beginning net assets can be restated.

- GASB Statement 51, *Accounting and Financial Reporting for Intangible Assets*. GASB 51 requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets. Accordingly, existing authoritative guidance related to the accounting and financial reporting for capital assets should be applied to these intangible assets, as applicable. Additionally, GASB 51 establishes a specified-conditions approach to recognizing intangible assets that are internally generated and establishes criteria for when such expenditures should be capitalized. GASB 51 is effective for periods beginning after June 15, 2009 and generally requires its provisions to be applied retroactively.
- GASB Statement 53, *Accounting and Financial Reporting for Derivative Instruments*. GASB 53 addresses the recognition, measurement and disclosure of information regarding derivative instruments entered into by state and local governments to manage specific risks or to make investments. A key provision of this statement is that derivative instruments covered in its scope with limited exception, are reported at fair value. For many derivative instruments, historical prices are zero because their terms are developed so that the instruments may be entered into without a payment being received or made. The changes in fair value of derivative instruments used for investment purposes are reported within the investment revenue classification. Alternatively, changes in fair value of derivative instruments that are classified as hedging derivative instruments are reported in the statement of net assets as deferred inflows or outflows. Effectiveness of the instruments is to be analyzed. Objectives, terms and risks of hedging derivative instruments are required disclosures. Disclosures also will include a summary of derivative instrument activity that provides an indication of the fair value amounts reported on the financial statements. The improvements under GASB 53, which becomes effective for periods beginning after June 15, 2009, should allow users of a government's financial statements to more fully understand resources available to provide services.



KPMG LLP
Suite 2100
999 Waterside Drive
Norfolk, VA 23510

**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 Audit Standards***

The Honorable Members of City Council
Wastewater Utility Fund of the City of Norfolk, Virginia:

We have audited the financial statements of the Wastewater Utility Fund of the City of Norfolk, Virginia (the Fund) as of and for the year ended June 30, 2008, and have issued our report thereon dated February 10, 2009. As discussed in note 1 to the financial statements, the accompanying financial statements present only the Wastewater Utility Fund and do not purport to, and do not, present fairly the financial position of the City of Norfolk, Virginia, the changes in its financial position or its cash flows, where applicable, in conformity with U.S. generally accepted accounting principles. Our report also discusses that the Fund has not presented a Management's Discussion and Analysis that U.S. generally accepted accounting principles has determined is necessary to supplement, although not required to be a part of, the financial statements. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

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

Our consideration of internal control over financial reporting was for the purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.

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

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



accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses.

Our consideration of the 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 the internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

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

This report is intended solely for the information and use of management, City Council, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

February 10, 2009