
SEWERAGE AND WATER BOARD OF NEW ORLEANS

FINANCIAL STATEMENTS AND SCHEDULES

DECEMBER 31, 2005



Postlethwaite & Netterville

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SEWERAGE AND WATER BOARD OF NEW ORLEANS

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INDEPENDENT AUDITORS' REPORT

Members of the Board
Sewerage and Water Board of New Orleans:

We have audited the basic financial statements of the Sewerage and Water Board of New Orleans as of and for the years ended December 31, 2005 and 2004, as listed in the table of contents. These basic financial statements are the responsibility of the Board's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the Sewerage and Water Board of New Orleans as of December 31, 2005 and 2004, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis and the Schedules of Funding Progress and Employer Contributions as listed on the accompanying table of contents, are not a required part of the basic financial statements but are 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 supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report, dated May 15, 2007, on our consideration of the Board's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. 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 considering the results of our audits.

Our audits were made for the purpose of forming an opinion on the 2005 and 2004 basic financial statements of the Board taken as a whole. The accompanying information included in Schedules 1 through 6 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Postlethwaite & Netterville

New Orleans, Louisiana
May 15, 2007

SEWERAGE & WATER BOARD OF NEW ORLEANS

MANAGEMENT'S DISCUSSION AND ANALYSIS YEAR ENDED DECEMBER 31, 2005

This section of the Sewerage & Water Board of New Orleans' (the Board) annual financial report presents a discussion and analysis of the Board's financial performance during the fiscal year that ended December 31, 2005. Please read it in conjunction with the Board's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

Hurricane Katrina and the resulting flooding was the most significant event to occur during 2005. This event resulted in severe damage to assets resulting in a loss of \$49.2 million and significant decreases in the Board's revenues.

Enterprise Fund

The major highlights in the Board's enterprise fund were as follows:

2005

- The Board's additions to its major systems approximated \$124.8 million. Property damages from Hurricane Katrina resulted in property losses of \$49.2 million.
- The SELA project which is a major upgrade to the drainage system by the Corps of Engineers continued during 2005; \$1.9 million of additions to work in progress were recorded during the year.
- The Board refunded during July 2005 the \$137 million in short term bond anticipation notes originally issued in July 2004.
- Federal Emergency Management Agency (FEMA) Disaster Public Assistance grants expended totaled \$40.9 million, of which \$31.6 million were capital contributions and \$9.3 million were for operating, maintenance and debris removal expenses.

2004

- The Board's additions to its major systems approximated \$121 million.
- The SELA project which is a major upgrade to the drainage system by the Corps of Engineers continued during 2004; \$17.9 million of additions to work in progress were recorded during the year.
- The Board refunded during July 2004 the \$111,800,000 in short term bond anticipation notes originally issued in November 2003.
- The Board issued bond issues in December 2004 totaling \$58,200,000 including \$25,200,000 in short term bond anticipation notes; the proceeds of the issue are to be used to fund capital projects in the sewerage department.
- Capital contributions by others to finance construction of the Board's capital assets totaled \$22.1 million.

Pension Trust Fund

2005

The major highlight in the Board's pension trust fund was the continued improved financial performance in the convertible securities market, continued interest rate increases, and the resulting appreciation of \$3.6 million in the market value of the investments held by the plan during 2005. The plan net assets available of benefits increased to \$202 million.

2004

The major highlight in the Board's pension trust fund was the continued improved financial performance in the public securities market and the resulting appreciation of \$14.1 million in the market value of the investments held by the plan during 2004. The plan net assets available of benefits increased to \$198 million.

OVERVIEW OF THE FINANCIAL STATEMENTS

This financial report consists of five parts: management's discussion and analysis (this section), the financial statements, the notes to the financial statements, required supplementary information, and other supplementary information.

Government-wide Financial Statements – Enterprise Fund

The Board's principal activities of providing water, sewerage, and drainages services are accounted for in a single proprietary fund – the enterprise fund. Enterprise funds are used to report business activities. Since the enterprise fund is the Board's single activity, its financial statements are presented as the Board's government-wide financial statements.

The financial statements provide both long-term and short-term information about the Board's overall financial status. The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a sections of required supplementary information and other supplementary information that further explain and support the information in the financial statements.

The Board's financial statements are prepared on an accrual basis in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. Under this basis of accounting, revenues are recognized in the period in which they are earned, expenses are recognized in the period in which they are incurred, and depreciation of assets is recognized in the Statements of Revenues, Expenses, and Changes in Net Assets. All assets and liabilities associated with the operation of the Authority are included in the Statements of Net Assets.

The Statement of Net Assets reports the Board's net assets. Net assets-the difference between the Board's assets and liabilities-are one way to measure the Board's financial health or position.

Fund Financial Statements – Pension Trust Fund

The Board's fund financial statements consist of its pension trust fund. As a fiduciary fund, the pension trust fund is held for the benefit of employees and retirees of the Board. The pension trust fund is not reflected in the government wide financials because the resources are not available to the Board for its activities. The accounting for the pension trust fund is much like that used by the enterprise fund.

FINANCIAL ANALYSIS OF THE BOARD'S

ENTERPRISE FUND

2005 Net Assets

The Board's total assets at December 31, 2005 reached approximately \$1.7 billion, a 1.1% increase over December 31, 2004 (see Table A-1).

| | 2005 | 2004 | Increase (Decrease) | Increase (Decrease) |
|---|-------------------------|-------------------------|------------------------|------------------------|
| Current assets | \$ 73,067,066 | \$ 33,106,264 | \$ 39,960,802 | 120.7% |
| Restricted assets | 298,455,080 | 357,112,767 | (58,657,687) | -16.4% |
| Property, plant and equipment - net | 1,317,298,829 | 1,279,442,913 | 37,855,916 | 3.0% |
| Other assets | 5,625,101 | 6,944,092 | (1,318,991) | -19.0% |
| Total assets | \$ 1,694,446,076 | \$ 1,676,606,036 | \$ 17,840,040 | 1.1% |
| Current liabilities | \$ 273,184,938 | \$ 216,972,936 | \$ 56,212,002 | 25.9% |
| Long-term liabilities | 265,600,587 | 279,560,334 | (13,959,747) | -5.0% |
| Total liabilities | 538,785,525 | 496,533,270 | 42,252,255 | 8.5% |
| Net assets: | | | | |
| Invested in capital assets, net of related debt | 1,092,139,700 | 1,085,354,440 | 6,785,260 | 0.6% |
| Restricted | 63,520,851 | 94,718,326 | (31,197,475) | -32.9% |
| Total net assets | 1,155,660,551 | 1,180,072,766 | (24,412,215) | -2.1% |
| Total liabilities and net assets | \$ 1,694,446,076 | \$ 1,676,606,036 | \$ 17,840,040 | 1.1% |

The increase in total assets of \$17.8 million resulted primarily from an increase in property, plant and equipment of \$37.9 million in 2005 due to \$42.9 million in construction funds expended and \$35.4 million of capital contributions less property losses resulting from Hurricane Katrina of \$49.2 million and the annual provision for depreciation of \$39.2 million. Current liabilities increased by \$56.2 million and long-term liabilities decreased by \$14.0 million in 2005 as compared to 2004 due primarily to increases in accounts payable for FEMA grant-related expenditures and normal payments of bonds payable existing at the beginning of the year.

2004 Net Assets

The Board's total assets at December 31, 2004 reached approximately \$1.7 billion, a 6.0% increase over December 31, 2003 (see Table A-2).

| | 2004 | 2003 | Increase (Decrease) | Increase (Decrease) |
|---|-------------------------|-------------------------|------------------------|------------------------|
| Current assets | \$ 33,106,264 | \$ 30,779,898 | \$ 2,326,366 | 7.6% |
| Restricted assets | 357,112,767 | 350,711,343 | 6,401,424 | 1.8% |
| Property, plant and equipment - net | 1,279,442,913 | 1,192,582,354 | 86,860,559 | 7.3% |
| Other assets | 6,944,092 | 8,517,724 | (1,573,632) | -18.5% |
| Total assets | \$ 1,676,606,036 | \$ 1,582,591,319 | \$ 94,014,717 | 5.9% |
| Current liabilities | \$ 216,972,936 | \$ 184,377,170 | \$ 32,595,766 | 17.7% |
| Long-term liabilities | 279,560,334 | 260,657,353 | 18,902,981 | 7.3% |
| Total liabilities | 496,533,270 | 445,034,523 | 51,498,747 | 11.6% |
| Net assets: | | | | |
| Invested in capital assets, net of related debt | 1,085,354,440 | 1,041,213,409 | 44,141,031 | 4.2% |
| Restricted | 94,718,326 | 96,343,387 | (1,625,061) | -1.7% |
| Total net assets | 1,180,072,766 | 1,137,556,796 | 42,515,970 | 3.7% |
| Total liabilities and net assets | \$ 1,676,606,036 | \$ 1,582,591,319 | \$ 94,014,717 | 5.9% |

The increase in total assets of \$95.5 million resulted primarily from an increase in property, plant and equipment of \$86.9 million in 2004 due to \$107.6 million in construction funds expended less the annual provision for depreciation of \$38.6 million. Current liabilities increased by \$32.6 million and long-term liabilities increased by \$18.9 million in 2004 as compared to 2003 due primarily to the issuance of \$170 million in new bonds payable including \$111,800,000 of refunding bond anticipation notes less normal payments of bonds payable existing at the beginning of the year.

2005 Changes in Net Assets

The change in net assets for the year ended December 31, 2005 was approximately \$24.4 million or 42.6% less than the change in net assets for the year ended December 31, 2004. The Board's total operating revenues decreased by 23.6% to approximately \$99.4 million, and total operating expenses increased 4.9% to approximately \$162.4 million. The changes in net assets are detailed in Table A-3; operating expenses are detailed in Table A-4.

| | 2005 | 2004 | Increase (Decrease) | Increase (Decrease) |
|-------------------------------------|---------------------|--------------------|------------------------|------------------------|
| Operating revenues: | | | | |
| Charges for services | \$ 96,232,489 | \$ 126,719,406 | \$ (30,486,917) | -24.1% |
| Other | 3,171,703 | 3,343,867 | (172,164) | -5.1% |
| Total operating revenues | 99,404,192 | 130,063,273 | (30,659,081) | -23.6% |
| Operating expenses (Table A-3) | 162,369,426 | 154,833,957 | 7,535,469 | 4.9% |
| Operating loss | (62,965,234) | (24,770,684) | (38,194,550) | 154.2% |
| Non-operating revenues: | | | | |
| Property taxes | 45,851,877 | 43,064,947 | 2,786,930 | 6.5% |
| Other taxes | 631,818 | 744,322 | (112,504) | -15.1% |
| Operating and maintenance grants | 9,338,528 | - | 9,338,528 | 100.0% |
| Hurricane loss | (55,909,262) | - | (55,909,262) | -100.0% |
| Investment income (expense) | 3,288,497 | 1,352,425 | 1,936,072 | 143.2% |
| Total non-operating revenues | 3,201,458 | 45,161,694 | (41,960,236) | -92.9% |
| Income before capital contributions | (59,763,776) | 20,391,010 | (80,154,786) | -393.1% |
| Capital contributions | 35,351,561 | 22,124,960 | 13,226,601 | 59.8% |
| Change in net assets | (24,412,215) | 42,515,970 | (66,928,185) | -157.4% |
| Net assets, beginning of year | 1,180,072,766 | 1,137,556,796 | 42,515,970 | 3.7% |
| Net assets, end of year | \$ 1,155,660,551 | \$ 1,180,072,766 | \$ (24,412,215) | -2.1% |

Operating revenues decreased primarily as a result of a decline in volume due to decreases in the customer base following Hurricane Katrina. Property taxes increased by \$2.8 million in 2005 due to an increase in assessed value.

Capital revenue from federal grants and construction of Board property by other agencies increased by 59.8% to \$35.4 million. Principal capital contributions related to FEMA Disaster Public Assistance grants and the U.S. Corps of Engineers' construction of major drainage system improvements.

| | 2005 | 2004 | Increase (Decrease) | Increase (Decrease) |
|---------------------------------|-----------------------|-----------------------|------------------------|------------------------|
| Power and pumping | \$ 11,818,104 | \$ 22,334,434 | \$ (10,516,330) | -47.1% |
| Treatment | 13,736,515 | 17,131,922 | (3,395,407) | -19.8% |
| Transmission and distribution | 18,432,531 | 20,846,681 | (2,414,150) | -11.6% |
| Customer accounts | 2,413,631 | 2,625,751 | (212,120) | -8.1% |
| Customer service | 2,645,604 | 2,855,631 | (210,027) | -7.4% |
| Administration and general | 12,130,773 | 14,978,964 | (2,848,191) | -19.0% |
| Payroll related | 19,780,248 | 18,794,864 | 985,384 | 5.2% |
| Maintenance of general plant | 27,991,450 | 10,764,556 | 17,226,894 | 160.0% |
| Depreciation | 39,187,670 | 38,600,928 | 586,742 | 1.5% |
| Amortization | 360,445 | 295,156 | 65,289 | 22.1% |
| Provision for doubtful accounts | 6,582,465 | 2,718,176 | 3,864,289 | 142.2% |
| Provision for claims | 7,289,990 | 2,886,894 | 4,403,096 | 152.5% |
| Total operating expenses | \$ 162,369,426 | \$ 154,833,957 | \$ 7,535,469 | 4.9% |

The decrease of \$10.5 million or 47.1% in 2005 in power and pumping is primarily due to a decrease in operations as a result of Hurricane Katrina including a decrease in boiler operations for high pressure gas and one sewerage pumping station being down as compared to 2004. The decrease in treatment expenses in 2005 of \$3.4 million or 19.8% primarily due to the east bank wastewater treatment plant being damaged and inoperable due to Hurricane Katrina. The decrease in transmission and distribution expenses in 2005 of \$2.4 million or 11.6% is primarily due to a disruption of water service at varying levels on the east bank of New Orleans for varying periods of time and a decrease in salaries and payroll related services due to a reduction in staff, all caused by Hurricane Katrina. The decrease in administration and general expenses in 2005 of \$2.8 million or 19.0% resulted primarily from decreases in salaries and payroll related services due to a reduction in staff caused by Hurricane Katrina. The increase in maintenance of general plant in 2005 of \$17.2 million or 160% resulted primarily from increases in salaries and payroll related expenses, professional services, consulting, and equipment repairs to restore systems following Hurricane Katrina. Provisions for doubtful accounts increased by \$3.9 million or 142.2% in 2005 as compared to 2004 as a result of an increase in closed accounts which are fully reserved and additional reserves for amounts not expected to be collected following Hurricane Katrina. Provisions for claims increased by \$4.4 million or 152.5% in 2005 as compared to 2004. Claims expense varies due to the number and severity of the claims during any period. The increase is due primarily to several large judgments rendered.

2004 Changes in Net Assets

The change in net assets for the year ended December 31, 2004 was approximately \$43.0 million or 39.6% less than the change in net assets for the year ended December 31, 2003. The Board's total operating revenues increased by 8.7% to approximately \$130.1 million, and total operating expenses increased 8.2% to approximately \$154.8 million. The changes in net assets are detailed in Table A-5; operating expenses are detailed in Table A-6.

| | 2004 | 2003 | Increase (Decrease) | Increase (Decrease) |
|-------------------------------------|------------------|------------------|------------------------|------------------------|
| Operating revenues: | | | | |
| Charges for services | \$ 126,719,406 | \$ 117,542,168 | \$ 9,177,238 | 7.8% |
| Other | 3,343,867 | 2,095,805 | 1,248,062 | 59.6% |
| Total operating revenues | 130,063,273 | 119,637,973 | 10,425,300 | 8.7% |
| Operating expenses (Table A-3) | 154,833,957 | 143,095,962 | 11,737,995 | 8.2% |
| Operating loss | (24,770,684) | (23,457,989) | (1,312,695) | 5.6% |
| Non-operating revenues: | | | | |
| Property taxes | 43,064,947 | 38,943,504 | 4,121,443 | 10.6% |
| Other taxes | 744,322 | 770,663 | (26,341) | -3.4% |
| Investment income | 1,352,425 | 1,031,593 | 320,832 | 31.1% |
| Total non-operating revenues | 45,161,694 | 40,745,760 | 4,415,934 | 10.8% |
| Income before capital contributions | 20,391,010 | 17,287,771 | 3,103,239 | 18.0% |
| Capital contributions | 22,124,960 | 53,054,656 | (30,929,696) | -58.3% |
| Change in net assets | 42,515,970 | 70,342,427 | (27,826,457) | -39.6% |
| Net assets, beginning of year | 1,137,556,796 | 1,067,214,369 | 70,342,427 | 6.6% |
| Net assets, end of year | \$ 1,180,072,766 | \$ 1,137,556,796 | \$ 42,515,970 | 3.7% |

Operating revenues increased primarily as a result of an increase in charges for services due to sewerage rate increases effective July, 2004 and August, 2003. The increases in revenue due to rates in sewerage and water revenues were partially offset by a decline in volume. Property taxes increased by \$4.1 million in 2004 due to an increase in assessed value.

Capital revenue from federal grants and construction of Board property by other agencies decreased by 58.3% to \$22.1 million. Principal capital contributions relate to the U.S. Corps of Engineers' construction of major drainage system improvements.

| | 2004 | 2003 | Increase (Decrease) | Increase (Decrease) |
|---------------------------------|-----------------------|-----------------------|------------------------|------------------------|
| Power and pumping | \$ 22,334,434 | \$ 19,339,095 | \$ 2,995,339 | 15.5% |
| Treatment | 17,131,922 | 17,075,547 | 56,375 | 0.3% |
| Transmission and distribution | 20,846,681 | 20,324,308 | 522,373 | 2.6% |
| Customer accounts | 2,625,751 | 2,513,486 | 112,265 | 4.5% |
| Customer service | 2,855,631 | 2,821,025 | 34,606 | 1.2% |
| Administration and general | 14,978,964 | 12,534,252 | 2,444,712 | 19.5% |
| Payroll related | 18,794,864 | 16,697,287 | 2,097,577 | 12.6% |
| Maintenance of general plant | 10,764,556 | 10,563,936 | 200,620 | 1.9% |
| Depreciation | 38,600,928 | 35,480,955 | 3,119,973 | 8.8% |
| Amortization | 295,156 | 188,128 | 107,028 | 56.9% |
| Provision for doubtful accounts | 2,718,176 | 1,884,751 | 833,425 | 44.2% |
| Provision for claims | 2,886,894 | 3,673,192 | (786,298) | -21.4% |
| Total operating expenses | \$ 154,833,957 | \$ 143,095,962 | \$ 11,737,995 | 8.2% |

The increase of \$3.0 million or 15.5% in 2004 in power and pumping is primarily due to an increase in the price of natural gas purchased by the Board and in the price per kilowatt hour of purchased electricity as compared to 2003. The increase in administration and general expenses in 2004 of \$2.4 million or 19.5% resulted primarily from increases in non-operating, computer center, fleet and general insurance, and general superintendent expenses. Provisions for doubtful accounts increased by \$0.8 million or 44.2% in 2004 as compared to 2003 as a result of an increase in closed accounts which are fully reserved. Provisions for claims decreased by \$0.8 million or 21.4% in 2004 as compared to 2003. Claims expense varies due to the number and severity of the claims during any period. The decrease is due primarily to a several large structured settlement payments made during 2004 as compared to 2003.

PENSION TRUST FUND

2005 Plan Net Assets

The Board's total plan net assets of its pension trust fund at December 31, 2005 was approximately \$202 million, a 2.1% increase over December 31, 2004 (see table A-7). Total assets increased 1.7% to \$206.2 million.

| | 2005 | 2004 | Increase (Decrease) | Increase (Decrease) |
|--------------------------|-----------------------|-----------------------|------------------------|------------------------|
| Cash | \$ 207,806 | \$ 242,764 | \$ (34,958) | -14.4% |
| Investments | 205,248,652 | 201,549,735 | 3,698,917 | 1.8% |
| Other assets | 773,796 | 1,062,674 | (288,878) | -27.2% |
| Total assets | 206,230,254 | 202,855,173 | 3,375,081 | 1.7% |
| DROP participant payable | \$ 3,593,654 | \$ 4,571,050 | \$ (977,396) | -21.4% |
| Due to other fund | 231,509 | - | 231,509 | 100.0% |
| Total liabilities | 3,825,163 | 4,571,050 | (745,887) | -16.3% |
| Plan net assets | \$ 202,405,091 | \$ 198,284,123 | \$ 4,120,968 | 2.1% |

Plan net assets increased by \$4.1 million in 2005 primarily due to realized and unrealized gains on investments recognized in 2005.

2004 Plan Net Assets

The Board's total plan net assets of its pension trust fund at December 31, 2004 was approximately \$198 million, a 7.7% increase over December 31, 2003 (see table A-8). Total assets increased 8.2% to \$202.9 million.

| | 2004 | 2003 | Increase (Decrease) | Increase (Decrease) |
|--------------------------|-----------------------|-----------------------|------------------------|------------------------|
| Cash | \$ 242,764 | \$ 237,431 | \$ 5,333 | 2.2% |
| Investments | 201,549,735 | 186,283,692 | 15,266,043 | 8.2% |
| Other assets | 1,062,674 | 874,735 | 187,939 | 21.5% |
| Total assets | 202,855,173 | 187,395,858 | 15,459,315 | 8.2% |
| DROP participant payable | 4,571,050 | 3,279,115 | 1,291,935 | 39.4% |
| Total liabilities | 4,571,050 | 3,279,115 | 1,291,935 | 39.4% |
| Plan net assets | \$ 198,284,123 | \$ 184,116,743 | \$ 14,167,380 | 7.7% |

Plan net assets increased by \$14.2 million in 2004 primarily due to realized and unrealized gains on investments recognized in 2004.

2005 Changes in Plan Net Assets

| | 2005 | 2004 | Increase (Decrease) | Increase (Decrease) |
|------------------------------------|-----------------------|-----------------------|------------------------|------------------------|
| Additions: | | | | |
| Contributions | \$ 5,607,361 | \$ 4,841,810 | \$ 765,551 | 15.8% |
| Net income on investments | 8,890,315 | 19,415,652 | (10,525,337) | -54.2% |
| Total additions | 14,497,676 | 24,257,462 | (9,759,786) | -40.2% |
| Deductions: | | | | |
| Benefits | (8,494,829) | (7,946,658) | (548,171) | 6.9% |
| Employee refunds | (149,147) | (116,254) | (32,893) | 28.3% |
| Employee DROP contributions | (1,732,732) | (2,027,170) | 294,438 | -14.5% |
| Total deductions | (10,376,708) | (10,090,082) | (286,626) | 2.8% |
| Change in net assets | 4,120,968 | 14,167,380 | (10,046,412) | -70.9% |
| Plan net assets, beginning of year | 198,284,123 | 184,116,743 | 14,167,380 | 7.7% |
| Plan net assets, end of year | \$ 202,405,091 | \$ 198,284,123 | \$ 4,120,968 | 2.1% |

Contributions to the pension plan increased in 2005 as compared to 2004 primarily due to increased employer contributions.

The decrease in the change in plan net assets of \$10.0 million resulted primarily from a decrease in unrealized gains on investments in 2005.

2004 Changes in Plan Net Assets

| Table A-10 | | | | |
|--|---------------------|---------------------|--------------------------------|--------------------------------|
| Sewerage & Water Board of New Orleans | | | | |
| Change in Plan Net Assets | | | | |
| | 2004 | 2003 | Increase (Decrease) | Increase (Decrease) |
| Additions: | | | | |
| Contributions | \$ 4,841,810 | \$ 4,488,720 | \$ 353,090 | 7.9% |
| Net income (loss) on investments | 19,415,652 | 36,078,814 | (16,663,162) | -46.2% |
| Total additions | 24,257,462 | 40,567,534 | (16,310,072) | -40.2% |
| Deductions: | | | | |
| Benefits | (7,946,658) | (8,590,242) | 643,584 | -7.5% |
| Employee refunds | (116,254) | (202,565) | 86,311 | -42.6% |
| Employee DROP contributions | (2,027,170) | (1,475,460) | (551,710) | 37.4% |
| Total deductions | (10,090,082) | (10,268,267) | 178,185 | -1.7% |
| Change in net assets | 14,167,380 | 30,299,267 | (16,131,887) | -53.2% |
| Plan net assets, beginning of year | 184,116,743 | 153,817,476 | 30,299,267 | 19.7% |
| Plan net assets, end of year | \$ 198,284,123 | \$ 184,116,743 | \$ 14,167,380 | 7.7% |

Contributions to the pension plan increased in 2004 as compared to 2003 primarily due to increased employer contributions.

The decrease in the change in plan net assets of \$16.1 million resulted primarily from a decrease in unrealized gains on investments in 2004.

CAPITAL ASSET AND DEBT ADMINISTRATION

2005 Capital Assets

As of December 31, 2005, the Board had invested approximately \$1.9 billion in capital assets. Net of accumulated depreciation, the Board's net capital assets at December 31, 2005 totaled approximately \$1.3 billion. This amount represents a net increase (including additions and disposals, net of depreciation) of approximately \$37.9 million or 3.0% over December 31, 2004. The net book value of property damages to power and pumping stations, treatment plants, distribution systems, sewerage collection systems, other buildings and equipment, and vehicles due to the flooding caused by Hurricane Katrina was \$49.2 million.

At December 31, 2005, the Board's budget for its five year capital improvements program totaled \$1.9 billion including \$426.0 million for water, \$738.1 million for sewerage and \$736.7 million for drainage. Due to certain regulatory and legislative changes, additional capital improvements will probably be required. Future capital improvement program expenditures may require the issuance of additional debt depending on the amount and timing of expenditures. As of December 31, 2005, the Board has committed or appropriated \$81.6 million in investments for use in future capital projects and has \$182.6 million of bond proceeds remaining for construction. The capital project investments are included in restricted assets.

The capital improvements budget for 2006 is \$658.6 million, including \$81.2 million for projects, which are expected to be funded by federal grants and programs. Significant projects included in property, plant and equipment in progress as of December 31, 2005 include the following:

Restoration of Systems Damaged as a result of Hurricane Katrina
Southeast Louisiana Flood Control Program
Sewer System Sanitation Evaluation and Rehabilitation Program
Drainage Pumping Station #1
Eastbank Sewer Treatment Plant
Westbank Sewer Treatment Plant

2004 Capital Assets

As of December 31, 2004, the Board had invested approximately \$1.8 billion in capital assets. Net of accumulated depreciation, the Board's net capital assets at December 31, 2004 totaled approximately \$1.3 billion. This amount represents a net increase (including additions and disposals, net of depreciation) of approximately \$86.9 million or 7.3% over December 31, 2003.

At December 31, 2004, the Board's budget for its five year capital improvements program totaled \$1.9 billion including \$510.6 million for water, \$851.1 million for sewerage and \$614.9 million for drainage. Due to certain regulatory and legislative changes, additional capital improvements will probably be required. Future capital improvement program expenditures may require the issuance of additional debt depending on the amount and timing of expenditures. As of December 31, 2004, the Board has committed or appropriated \$85.8 million in investments for use in future capital projects and has \$225.5 million of bond proceeds remaining for construction. The capital project investments are included in restricted assets.

The capital improvements budget for 2005 is \$297.8 million, including \$42.3 million for projects, which are expected to be funded by federal grants and programs. Significant projects included in property, plant and equipment in progress as of December 31, 2004 include the following:

Southeast Louisiana Flood Control Program
Sewer System Sanitation Evaluation and Rehabilitation Program
Drainage Pumping Station #1
Eastbank Sewer Treatment Plant
Westbank Sewer Treatment Plant

2005 Debt Administration

The Board continues to make its regularly scheduled payments on its bonds. During 2005, \$137.0 million in new bonds were issued by the Board. Net proceeds of the bond issues were used to refund \$137.0 million of bond anticipation notes from 2003. During 2005, \$147.9 million in principal payments were made.

All bond debt covenants have been met.

Additional detailed information relating to capital assets and debt is presented in the financial statements and related notes.

2004 Debt Administration

The Board continues to make its regularly scheduled payments on its bonds. During 2004, \$170.0 million in new bonds were issued by the Board. Net proceeds of the bond issues are to be used for sewerage construction and to refund \$111.8 million of bond anticipation notes from 2003. During 2004, \$121.0 million in principal payments were made.

All bond debt covenants have been met.

Additional detailed information relating to capital assets and debt is presented in the financial statements and related notes.

ECONOMIC FACTORS AND RATES

In post Katrina, there are significant other revenues and expenses, which impact the Board. State and federal grants related to the disaster will have a significant impact on 2006. Total FEMA debris removal, mitigation, and capital replacement grants are expected to exceed \$160.0 million. Of these approximately \$40.9 million has been recognized in 2005. FEMA revenues will be recognized as buildings, systems, and other reimbursable assets are repaired or replaced. In 2006, the Board will recognize a significant portion of these revenues but much of the construction and replacement will not have been completed and the revenues although measurable may not be available due to the slowness of actual receipts of FEMA funds.

In July 2006, the Board and the State of Louisiana (the State) entered into a Cooperative Endeavor Agreement (the Agreement) whereby the State agreed to lend up to \$77.5 million to the Board from State funds on deposit in the Debt Service Assistance Fund, authorized by the Gulf Opportunity Zone Act of 2005 and Act 41 of the First Extraordinary Session of the Louisiana Legislature of 2006. This loan is to assist in payment of debt service requirements for 2006 to 2008 due to disruption of tax bases and revenue streams caused by Hurricanes Katrina and Rita. No principal or interest is payable during the initial five year period of the loan. After the expiration of the initial five-year period, the loan bears interest at a fixed rate of 4.64%.

The Board's authority to implement multiple year annual rate increases of 14% for 2005 and 14% in 2006 continued. The number of open accounts has decreased from approximately 145,000 at the end of 2004 to approximately 121,000 currently, a decrease of 16.7%.

CONTACTING THE BOARD'S FINANCIAL MANAGEMENT

This financial report is designed to provide our bondholders, patrons, and other interested parties with a general overview of the Board's finances and to demonstrate the Board's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Sewerage & Water Board of New Orleans at (504) 585-2356.

SEWERAGE AND WATER BOARD OF NEW ORLEANS

STATEMENTS OF NET ASSETS

December 31, 2005 and 2004

| ASSETS | 2005 | 2004 |
|--|------------------|------------------|
| Property, plant and equipment | \$ 1,851,147,896 | \$ 1,826,416,136 |
| Less: accumulated depreciation | 533,849,067 | 546,973,223 |
| Property, plant and equipment, net | 1,317,298,829 | 1,279,442,913 |
| Restricted assets: | | |
| Capital projects | 81,600,704 | 85,776,891 |
| Construction funds | 182,614,944 | 225,529,144 |
| Debt service reserve | 22,254,068 | 22,254,068 |
| Customer deposits | 5,417,248 | 5,336,338 |
| Health insurance reserve | 4,473,900 | 9,000,000 |
| Debt service | 1,882,216 | 9,004,326 |
| Other | 212,000 | 212,000 |
| Total restricted assets | 298,455,080 | 357,112,767 |
| Current assets: | | |
| Cash | 4,495,796 | 3,043,854 |
| Accounts receivable: | | |
| Customers (net of allowance for doubtful accounts) | 12,345,146 | 13,188,408 |
| Taxes | 7,409,194 | 4,737,807 |
| Interest | 894,335 | 418,576 |
| Grants | 38,596,551 | 235,091 |
| Miscellaneous | 3,313,386 | 1,542,155 |
| Due from City of New Orleans, current | 200,000 | 200,000 |
| Due from other fund | 290,778 | - |
| Inventory of supplies | 4,883,630 | 9,109,830 |
| Prepaid expenses | 638,250 | 630,543 |
| Total current assets | 73,067,066 | 33,106,264 |
| Due from City of New Orleans, less current portion | 408,614 | 546,229 |
| Other assets: | | |
| Bond issue costs | 1,446,463 | 1,666,907 |
| Deposits | 51,315 | 51,315 |
| Net pension asset | 3,718,709 | 4,679,641 |
| Total other assets | 5,216,487 | 6,397,863 |
| Total assets | \$ 1,694,446,076 | \$ 1,676,606,036 |

(Continued)

SEWERAGE AND WATER BOARD OF NEW ORLEANS

**STATEMENTS OF NET ASSETS
(Continued)**

| | 2005 | 2004 |
|--|------------------|------------------|
| NET ASSETS AND LIABILITIES | | |
| Net Assets: | | |
| Invested in capital assets - net of related debt | \$ 1,092,139,700 | \$ 1,085,354,440 |
| Restricted For: | | |
| Debt service | 21,453,647 | 28,817,876 |
| Capital projects | 42,067,204 | 65,900,450 |
| Total restricted for net assets | 63,520,851 | 94,718,326 |
| Total net assets | 1,155,660,551 | 1,180,072,766 |
| Liabilities: | | |
| Long-term liabilities: | | |
| Claims payable | 6,371,799 | 8,660,268 |
| Bonds payable (net of current maturities) | 259,228,788 | 270,900,066 |
| | 265,600,587 | 279,560,334 |
| Current liabilities (payable from current assets): | | |
| Accounts payable | 72,061,335 | 20,760,229 |
| Due to City of New Orleans | 748,746 | 259,462 |
| Retainers and estimates payable | 2,539,742 | 1,474,713 |
| Due to pension trust fund | 59,269 | 60,994 |
| Accrued salaries | 537,376 | 674,661 |
| Accrued vacation and sick pay | 9,874,395 | 9,869,659 |
| Claims payable | 27,170,348 | 22,940,327 |
| Capital lease payable | 806,172 | - |
| Other liabilities | 1,734 | 13,158 |
| | 113,799,117 | 56,053,203 |
| Current liabilities (payable from restricted assets): | | |
| Accrued interest | 2,682,637 | 2,440,517 |
| Bonds payable | 148,545,285 | 148,717,551 |
| Retainers and estimates payable | 2,740,651 | 4,425,327 |
| Customer deposits | 5,417,248 | 5,336,338 |
| | 159,385,821 | 160,919,733 |
| Total current liabilities | 273,184,938 | 216,972,936 |
| Total liabilities | 538,785,525 | 496,533,270 |
| Total net assets and liabilities | \$ 1,694,446,076 | \$ 1,676,606,036 |

See accompanying notes to financial statements.

SEWERAGE AND WATER BOARD OF NEW ORLEANS
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

For the years ended December 31, 2005 and 2004

| | 2005 | 2004 |
|--|------------------|------------------|
| Operating revenues: | | |
| Sales of water and delinquent fees | \$ 38,727,266 | \$ 54,234,144 |
| Sewerage service charges | 57,329,963 | 72,252,114 |
| Plumbing inspection and license fees | 175,260 | 233,147 |
| Other revenue | 3,171,703 | 3,343,868 |
| Total operating revenues | 99,404,192 | 130,063,273 |
| Operating Expenses: | | |
| Power and pumping | 11,818,104 | 22,334,434 |
| Treatment | 13,736,515 | 17,131,922 |
| Transmission and distribution | 18,432,531 | 20,846,681 |
| Customer accounts | 2,413,631 | 2,625,751 |
| Customer service | 2,645,604 | 2,855,631 |
| Administration and general | 12,130,773 | 14,978,964 |
| Payroll related | 19,780,248 | 18,794,864 |
| Maintenance of general plant | 27,991,450 | 10,764,556 |
| Depreciation | 39,187,670 | 38,600,928 |
| Amortization | 360,445 | 295,156 |
| Provision for doubtful accounts | 6,582,465 | 2,718,176 |
| Provision for claims | 7,289,990 | 2,886,894 |
| Total operating expenses | 162,369,426 | 154,833,957 |
| Operating loss | (62,965,234) | (24,770,684) |
| Non-operating revenues (expenses): | | |
| Two-mill tax | 1,407 | 5,192 |
| Three-mill tax | 12,990,040 | 12,199,559 |
| Six-mill tax | 13,152,643 | 12,352,092 |
| Nine-mill tax | 19,707,787 | 18,508,104 |
| Other taxes | 631,818 | 744,322 |
| Operating and maintenance grants | 9,338,528 | - |
| Investment income | 3,291,489 | 1,352,425 |
| Hurricane loss | (55,909,262) | - |
| Investment expense | (2,992) | - |
| Total non-operating revenues (expenses) | 3,201,458 | 45,161,694 |
| Income (loss) before capital contributions | (59,763,776) | 20,391,010 |
| Capital contributions | 35,351,561 | 22,124,960 |
| Change in net assets | (24,412,215) | 42,515,970 |
| Net assets: | | |
| Beginning of year | 1,180,072,766 | 1,137,556,796 |
| End of year | \$ 1,155,660,551 | \$ 1,180,072,766 |

See accompanying notes to financial statements.

SEWERAGE AND WATER BOARD OF NEW ORLEANS

STATEMENTS OF CASH FLOWS

ENTERPRISE FUND

For the years ended December 31, 2005 and 2004

| | <u>2005</u> | <u>2004</u> |
|--|----------------------|-----------------------|
| Cash flows from operating activities | | |
| Cash received from customers | \$ 90,807,310 | \$ 122,918,850 |
| Cash payments to suppliers for goods and services | (54,394,902) | (57,763,832) |
| Cash payments to employees for services | (57,786,804) | (55,562,758) |
| Other revenue | 1,575,732 | 4,378,538 |
| | <u>(19,798,664)</u> | <u>13,970,798</u> |
| Cash flows from noncapital financing activities - proceeds from property taxes | <u>43,812,308</u> | <u>43,902,698</u> |
| Cash flows from capital and related financing activities | | |
| Acquisition and construction of capital assets | (69,087,981) | (112,845,073) |
| Proceeds of bond issue | 137,189,060 | 171,402,786 |
| Bond issuance costs | (140,001) | (299,600) |
| Principal payments on bonds payable | (147,885,000) | (121,015,000) |
| Interest paid on bonds payable | (17,193,506) | (14,491,864) |
| Principal payments on capital lease | (137,201) | - |
| Interest paid on capital lease | (2,992) | - |
| Capital contributed by developers and federal grants | 6,328,629 | 22,895,714 |
| | <u>(90,928,992)</u> | <u>(54,353,037)</u> |
| Cash flows from investing activities | | |
| Payments for purchase of investments | (501,020,477) | (1,714,722,567) |
| Proceeds from maturities of investments | 527,128,807 | 1,712,625,222 |
| Investment income | 9,628,693 | 4,369,955 |
| | <u>35,737,023</u> | <u>2,272,610</u> |
| Net increase (decrease) in cash | (31,178,325) | 5,793,069 |
| Cash at the beginning of the year | <u>119,063,845</u> | <u>113,270,776</u> |
| Cash at the end of the year | <u>\$ 87,885,520</u> | <u>\$ 119,063,845</u> |
| Reconciliation of cash and restricted cash (note 2) | | |
| Current assets - cash | \$ 4,495,796 | \$ 3,043,854 |
| Restricted assets -cash | 83,389,724 | 116,019,991 |
| Total cash | <u>\$ 87,885,520</u> | <u>\$ 119,063,845</u> |

(Continued)

SEWERAGE AND WATER BOARD OF NEW ORLEANS

**STATEMENTS OF CASH FLOWS
(Continued)**

ENTERPRISE FUND

For the years ended December 31, 2005 and 2004

| | <u>2005</u> | <u>2004</u> |
|---|------------------------|----------------------|
| Reconciliation of operating loss to net cash provided by (used in) operating activities is as follows: | | |
| Operating loss | \$ (62,965,234) | \$ (24,770,684) |
| Adjustments to reconcile net operating loss to net cash provided by (used in) operating activities: | | |
| Depreciation | 39,187,670 | 38,600,928 |
| Provision for claims | 7,289,990 | 2,886,894 |
| Provision for doubtful accounts | 6,582,465 | 2,718,176 |
| Amortization | 360,445 | 295,156 |
| Change in operating assets and liabilities: | | |
| Increase in customer and other receivable | (5,739,203) | (3,620,942) |
| (Increase) decrease in inventory | (2,444,535) | (1,208,424) |
| Increase (decrease) in prepaid expenses and other receivables | (1,932,101) | 911,501 |
| Decrease in net pension asset | 960,932 | 1,451,077 |
| Increase in accounts payable | 3,905,759 | 2,437,344 |
| Increase (decrease) in accrued salaries, due to pension and accrued vacation and sick pay | (134,274) | 362,522 |
| Decrease in other liabilities | <u>(4,870,578)</u> | <u>(6,092,750)</u> |
| Net cash provided by (used in) operating activities | <u>\$ (19,798,664)</u> | <u>\$ 13,970,798</u> |

Noncash investing, capital and financing activities:

The acquisition and construction of capital assets and capital contributed by developers and federal grants do not include non-cash amounts resulting from the construction by the U.S. Corps of Engineers of \$1,943,806 and \$17,872,855 in drainage projects during the years ended December 31, 2005 and 2004, respectively.

See accompanying notes to financial statements.

SEWERAGE AND WATER BOARD OF NEW ORLEANS

STATEMENTS OF PLAN NET ASSETS

PENSION TRUST FUND

December 31, 2005 and 2004

| | <u>2005</u> | <u>2004</u> |
|--|-----------------------|-----------------------|
| Assets: | | |
| Cash | \$ 207,806 | \$ 242,764 |
| Receivables: | | |
| Investment income | 756,987 | 979,923 |
| Employee contributions receivable | 16,809 | 21,757 |
| Due from other fund | - | 60,994 |
| Investments | <u>205,248,652</u> | <u>201,549,735</u> |
| Total assets | <u>206,230,254</u> | <u>202,855,173</u> |
| Liabilities: | | |
| DROP participants payable | 3,593,654 | 4,571,050 |
| Due to other fund | <u>231,509</u> | <u>-</u> |
| Total liabilities | <u>3,825,163</u> | <u>4,571,050</u> |
| Plan net assets available for pension benefits | <u>\$ 202,405,091</u> | <u>\$ 198,284,123</u> |

See accompanying notes to financial statements.

SEWERAGE AND WATER BOARD OF NEW ORLEANS

STATEMENTS OF CHANGES IN PLAN NET ASSETS

PENSION TRUST FUND

For the years ended December 31, 2005 and 2004

| | <u>2005</u> | <u>2004</u> |
|--------------------------------------|-----------------------|-----------------------|
| Additions: | | |
| Contributions: | | |
| Employee contributions | \$ 1,176,637 | \$ 1,120,776 |
| Employer contributions | 3,716,381 | 3,103,146 |
| City annuity and other transfers in | 714,343 | 617,888 |
| Total contributions | <u>5,607,361</u> | <u>4,841,810</u> |
| Investment income: | | |
| Interest income | 3,214,087 | 3,461,162 |
| Dividend income | 2,118,541 | 1,886,416 |
| Net appreciation | 3,642,420 | 14,133,537 |
| | <u>8,975,048</u> | <u>19,481,115</u> |
| Less investment expense | <u>(84,733)</u> | <u>(65,463)</u> |
| Net investment income | <u>8,890,315</u> | <u>19,415,652</u> |
| Total additions | <u>14,497,676</u> | <u>24,257,462</u> |
| Deductions: | | |
| Benefits | (8,494,829) | (7,946,658) |
| Employee refunds | (149,147) | (116,254) |
| Employee contributions to DROP | (1,732,732) | (2,027,170) |
| Total deductions | <u>(10,376,708)</u> | <u>(10,090,082)</u> |
| Change in plan net assets | 4,120,968 | 14,167,380 |
| Plan net assets at beginning of year | <u>198,284,123</u> | <u>184,116,743</u> |
| Plan net assets at end of year | <u>\$ 202,405,091</u> | <u>\$ 198,284,123</u> |

See accompanying notes to financial statements.

SEWERAGE AND WATER BOARD OF NEW ORLEANS

NOTES TO FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies

History and Organization

The major operation of the Sewerage and Water Board of New Orleans (the Board) is providing water, sewerage and drainage services for the City of New Orleans (City). The Sewerage and Water Board of New Orleans was created by Act 6 of the Louisiana Legislature of 1899 as a special board independent of the City's government to construct, maintain and operate a water treatment and distribution system and a public sanitary sewerage system for the City. In 1903, the Legislature gave the Board control of and responsibility for the City's major drainage system and relieved the City of the duty of providing in its annual operating budget or otherwise for the maintenance and operations of the water, sewerage and drainage systems.

In accordance with the Louisiana Revised Statutes (LRS) 33:4096 and 4121, the Board has the authority to establish the water and sewerage rates to charge to its customers. The rates are based on the actual water consumed and on the costs of maintenance and operation of the water and sewerage systems, including the costs of improvements and replacements. The collections of water and sewerage revenues are to be used by the Board for the maintenance and operation of the systems, the cost of improvements, betterments, and replacements, and to provide for the payments of interest and principal on the bonds payable. The Board has also been given the authority to levy and collect various tax millages which are used for the operation and maintenance of the drainage operations. All excess revenues collected are made available for capital development of the system. The proceeds of the rate collections and tax millages are invested in such investments as authorized by the LRS. These investments are reflected in the combined statement of net assets, as "restricted assets," as they are restricted to the purposes as described above.

The Board is composed of thirteen members, including the Mayor of the City, the two Councilmembers-at-Large, and one District Councilmember selected by the City Council, two members of the Board of Liquidation and seven citizens appointed by the Mayor. The appointed members of the Board serve staggered nine year terms.

The Board's accounting policies conform to accounting principles generally accepted in the United States of America as applicable to utilities and to governmental units. The following is a summary of the more significant policies.

(A) Reporting Entity

In conformity with the Governmental Accounting Standards Board's definition of a reporting entity, the Board includes an enterprise fund and a pension trust fund for financial reporting purposes. The Board is considered a reporting entity based on the following criteria:

- (a) Responsibility for surpluses/deficits. The Board is solely responsible for its surpluses/deficits. In accordance with Louisiana Revised Statutes, no other governmental unit is responsible for the Board's deficits or has a claim to its surpluses. The Board's operations are self-sustaining; revenues are generated through charges to customers and dedicated property taxes. Other than grants, no funding is received from the State of Louisiana or the City of New Orleans.