

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT**

REPORT OF AUDIT

FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
TABLE OF CONTENTS**

	<u>Page</u>
Independent Auditor's Report	1-3
 <u>Financial Statements</u>	
Schedule A Comparative Statement of Assets, Liabilities and Net Assets	4-5
Schedule B Comparative Statement of Revenues, Expenses and Changes in Restricted and Unrestricted Net Assets	6
Schedule C Statement of Changes in Net Assets by Fund	7
Notes to Financial Statements	8-27
 <u>Supplementary Schedules</u>	
Schedule 1 Schedule of Actual Revenues and Expenditures Compared to Budget	28
Schedule 2 Schedule of Revenues, Expenditures and Changes in Restricted and Unrestricted Net Assets by Fund	29
Roster of Officials as of December 31, 2012	30
 <u>Government Auditing Standards</u>	
Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With Government Auditing Standards	31-32
Schedule of Findings and Responses	33-36
Summary Schedule of Prior Audit Findings	37

LERCH, VINCI & HIGGINS, LLP

CERTIFIED PUBLIC ACCOUNTANTS
REGISTERED MUNICIPAL ACCOUNTANTS

17 - 17 ROUTE 208
FAIR LAWN, NJ 07410
TELEPHONE (201) 791-7100
FACSIMILE (201) 791-3035
WWW.LVHCPA.COM

DIETER P. LERCH, CPA, RMA, PSA
GARY J. VINCI, CPA, RMA, PSA
GARY W. HIGGINS, CPA, RMA, PSA
JEFFREY C. BLISS, CPA, RMA, PSA
PAUL J. LERCH, CPA, RMA, PSA
DONNA L. JAPHET, CPA, PSA
JULIUS B. CONSONI, CPA, PSA

ELIZABETH A. SHICK, CPA, RMA, PSA
ANDREW PARENTE, CPA, RMA, PSA
ROBERT W. HAAG, CPA, PSA
DEBORAH K. LERCH, CPA, PSA
DEBRA GOLLE, CPA
CINDY JANACEK, CPA, RMA
RALPH M. PICONE, CPA, RMA, PSA
EDWARD N. KERE, CPA

INDEPENDENT AUDITOR'S REPORT

Honorable Chairman and Members of the Board of Commissioners
North Jersey District Water Supply Commission
Wanaque, New Jersey

Report on the Financial Statements

We have audited the accompanying statement of assets, liabilities and net assets of the North Jersey District Water Supply Commission (the "Commission") - Wanaque South Project (the "Project"), as of and for the year ended December 31, 2012, and the related statements of revenues, expenses and changes in restricted and unrestricted net assets and changes in net assets by fund for the year then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the modified accrual basis of accounting, which differs in certain respects from accounting principles generally accepted in the United States of America. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating

the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles

As described in Note 1 of the financial statements, the financial statements are prepared and presented by the North Jersey District Water Supply Commission on the modified accrual basis of accounting. This basis of accounting does not present the financial statements in accordance with accounting principles generally accepted in the United States of America.

The effects on the financial statements of the variances between the modified accrual basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinion on U.S. Generally Accepted Accounting Principles

In our opinion, because the significance of the North Jersey District Water Supply Commission preparing and presenting its financial statements on the modified accrual basis of accounting as discussed in the “Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles” paragraph above, the financial statements referred to above do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of the North Jersey District Water Supply Commission - Wanaque South Project as of December 31, 2012 or changes in financial position, or, where applicable, cash flows for the year then ended.

Opinion on Modified Accrual Basis of Accounting

In our opinion, the financial statements – modified accrual basis referred to above present fairly, in all material respects, the financial position – modified accrual basis of the North Jersey District Water Supply Commission Wanaque South Project as of December 31, 2012 and the respective changes in restricted and unrestricted net assets – modified accrual basis and changes in net assets by Fund-modified accrual basis for the year then ended in accordance with the basis of financial accounting and reporting principles and practices as described in Note 1.

Emphasis of Matter

As discussed in Note 1 (A), the financial statements-modified accrual basis of the North Jersey District Water Supply Commission Wanaque South Project, are intended to present the financial position-modified accrual basis, the changes in restricted and unrestricted net assets-modified accrual basis and the changes in net assets by fund-modified accrual basis of only that portion of the North Jersey District Water Supply Commission that is attributable to the transactions of the Wanaque South Project. They do not purport to, and do not, present fairly the financial position-modified accrual basis of the North Jersey District Water Supply Commission as of December 31, 2012, the changes in its restricted and unrestricted net assets-modified accrual basis and the changes in its net assets by fund-modified accrual basis for the year then ended in accordance with the basis for financial accounting and reporting principles and practices as described in Note 1. Our opinion on the financial statements-modified accrual basis is not modified with respect to this matter.

Other Matters

Prior Year's Financial Statements Audited by Other Auditors

The financial statements of the North Jersey District Water Supply Commission Wanaque South Project as of and for the year ended December 31, 2011 were audited by other auditors whose report dated July 12, 2012 expressed an adverse opinion on the financial statements because they were not prepared and presented in accordance with accounting principles generally accepted in the United States of America but rather the modified accrual basis of accounting. Their report also expressed an unqualified opinion on those financial statements – modified accrual basis prepared and presented in accordance with the modified accrual basis of accounting.

Required Supplementary Information

The Commission has not presented a management's discussion and analysis for the Wanaque South Project that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. A management discussion and analysis is not required by the financial accounting and reporting principles and practices utilized by the North Jersey District Water Supply Commission to supplement the modified accrual basis financial statements and therefore it has not been presented by management. Our opinion on the financial statements – modified accrual basis is not affected by this missing information.

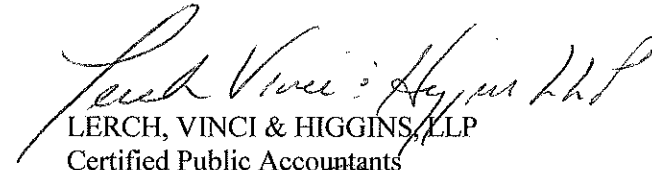
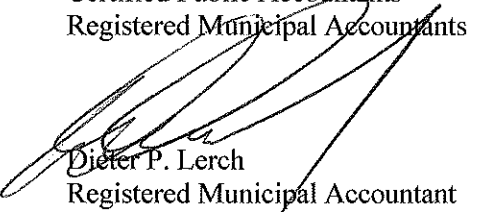
Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements of the North Jersey District Water Supply Commission - Wanaque South Project. The supplementary schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the financial statements of the North Jersey District Water Supply Commission Wanaque South Project.

The supplementary schedules listed in the table of contents are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary schedules listed in the table of contents are fairly stated, in all material respects, in relation to the financial statements as a whole on the basis of accounting described in Note 1.

Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued our report dated June 20, 2013 on our consideration of the North Jersey District Water Supply Commission - Wanaque South Project's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the North Jersey District Water Supply Commission Wanaque South Project's internal control over financial reporting and compliance.


LERCH, VINCI & HIGGINS, LLP
Certified Public Accountants
Registered Municipal Accountants

Dieter P. Lerch
Registered Municipal Accountant
RMA Number CR00398

Fair Lawn, New Jersey
June 20, 2013

FINANCIAL STATEMENTS

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
COMPARATIVE STATEMENTS OF ASSETS, LIABILITIES AND NET ASSETS
(MODIFIED ACCRUAL BASIS)
AS OF DECEMBER 31, 2012 AND 2011**

	<u>2012</u>	<u>2011</u> (Restated)
ASSETS		
Unrestricted Current Assets		
Cash and Cash Equivalents	\$ 15,361,789	\$ 14,726,977
Equity in Wanaque South, a Joint Venture	<u>2,500</u>	<u>2,500</u>
Total Unrestricted Current Assets	<u>15,364,289</u>	<u>14,729,477</u>
Restricted Current Assets		
Restricted Cash and Cash Equivalents	7,106,679	7,076,087
NJEIT Loans Receivable	<u>2,023,471</u>	<u>2,256,928</u>
Total Restricted Current Assets	<u>9,130,150</u>	<u>9,333,015</u>
Non Current Assets		
Deferred Charges		
Assessments Receivable	<u>403,677</u>	<u>424,879</u>
Capital Assets		
Investment in Dundee Water Power and Land Company	1,958,015	1,958,015
Property, Plant and Equipment	<u>122,559,379</u>	<u>121,635,479</u>
Total Capital Assets	<u>124,517,394</u>	<u>123,593,494</u>
Total NonCurrent Assets	<u>124,921,071</u>	<u>124,018,373</u>
Total Assets	<u>\$ 149,415,510</u>	<u>\$ 148,080,865</u>

The Accompanying Notes are an Integral Part of these Financial Statements

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
COMPARATIVE STATEMENTS OF ASSETS, LIABILITIES AND NET ASSETS
(MODIFIED ACCRUAL BASIS)
AS OF DECEMBER 31, 2012 AND 2011**

	<u>2012</u>	<u>2011</u> (Restated)
LIABILITIES AND NET ASSETS		
LIABILITIES		
Current Liabilities (Payable from Unrestricted Assets)		
Accounts Payable	\$ 58,395	\$ 58,395
Due to Wanaque South, a Joint Venture	261,220	796,481
Due to Wanaque North Project	<u>3,110,062</u>	<u>1,272,891</u>
Total Current Liabilities Payable from Unrestricted Assets	<u>3,429,677</u>	<u>2,127,767</u>
Current Liabilities (Payable from Restricted Assets)		
Accounts Payable	13,021	162,489
Bonds Payable	5,783,927	5,547,323
Retainage Payable	88,174	80,400
Encumbrances Payable	218,955	204,416
Unearned Revenue	<u>2,023,471</u>	<u>2,256,928</u>
Total Current Liabilities Payable from Restricted Assets	<u>8,127,548</u>	<u>8,251,556</u>
Non-Current Liabilities		
Bonds Payable	<u>23,408,294</u>	<u>29,405,284</u>
Total Liabilities	<u>34,965,519</u>	<u>39,784,607</u>
NET ASSETS		
Investment in Capital Assets, net of related debt	<u>95,325,173</u>	<u>88,640,887</u>
Restricted For:		
Operating Reserve	2,746,712	2,746,712
Debt Service	3,600,708	3,819,185
Renewal and Replacement	6,215,951	6,309,109
Unrestricted	<u>6,561,447</u>	<u>6,780,365</u>
Total Restricted and Unrestricted Net Assets	<u>19,124,818</u>	<u>19,655,371</u>
Total Net Assets	<u>114,449,991</u>	<u>108,296,258</u>
Total Liabilities and Net Assets	<u>\$ 149,415,510</u>	<u>\$ 148,080,865</u>

The Accompanying Notes are an Integral Part of these Financial Statements

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 COMPARATIVE STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN
 RESTRICTED AND UNRESTRICTED NET ASSETS
 (MODIFIED ACCRUAL BASIS)
 FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011**

	<u>2012</u>	<u>2011</u>
OPERATING REVENUES		
Charges for Services	\$ 16,049,691	\$ 16,049,690
Total Operating Revenues	<u>16,049,691</u>	<u>16,049,690</u>
OPERATING EXPENSES		
Payroll and Related Expenses	2,785,458	3,955,591
Utilities and Fuel	1,046,709	744,652
Chemicals	843,096	499,824
Pump Station and Other	94,359	135,995
Real Estate Taxes	720,639	634,846
Use Fee	277,212	277,796
Insurance	1,561,009	1,274,251
Legal and Accounting	208,323	211,248
Engineering and Consulting	63,813	23,613
Supplies and Expenses	715,236	407,119
Trustee Fees	63,504	63,970
Bond Principal	<u>5,547,323</u>	<u>5,290,623</u>
Total Operating Expenses	<u>13,926,681</u>	<u>13,519,528</u>
Operating Income	<u>2,123,010</u>	<u>2,530,162</u>
NON-OPERATING REVENUES (EXPENSES)		
Interest Income	36,971	71,653
Amortization of Assessments Receivable	(21,202)	(21,742)
Interest Expense	(1,638,904)	(1,893,838)
NJEIT Loan Proceeds	218,443	2,097,438
Capital Outlay	(1,067,256)	(2,709,899)
Bond Principal Refunded	(213,063)	-
Grants and Other Income	<u>31,448</u>	<u>51,468</u>
Total Non-Operating Revenue (Expenses)	<u>(2,653,563)</u>	<u>(2,404,920)</u>
Change in Restricted and Unrestricted Net Assets	(530,553)	125,242
Restricted and Unrestricted Net Assets - Beginning of Year	19,655,371	19,782,651
Prior Period Adjustment	<u>-</u>	<u>(252,522)</u>
Restricted and Unrestricted Net Assets - End of Year	<u>\$ 19,124,818</u>	<u>\$ 19,655,371</u>

The Accompanying Notes are an Integral Part of these Financial Statements

WANAQUE SOUTH PROJECT
STATEMENTS OF CHANGES IN NET ASSETS BY FUND
(MODIFIED ACCRUAL BASIS)
YEARS ENDED DECEMBER 31, 2012 AND 2011

		<u>Restricted</u>				<u>Total</u>		
	<u>Investment in</u>	<u>Operating</u>	<u>Debt</u>	<u>Capital</u>	<u>Restricted</u>	<u>Unrestricted</u>	<u>Total Net</u>	
	<u>Capital Assets</u>	<u>Reserve</u>	<u>Service</u>	<u>Outlay</u>			<u>Assets</u>	
Balance, January 1, 2011	\$ 79,905,549	\$ 2,746,712	\$ 3,819,185	\$ 5,319,787	\$ 11,885,684	\$ 7,896,971	\$ 99,688,204	
Prior Period Adjustment	1,325,535			1,073,009	1,073,009	(1,325,535)	1,073,009	
Additions	7,409,803			252,263	252,263	241,076	7,903,142	
Reductions				(335,950)	(335,950)	(157,389)	(493,339)	
Change in Net Assets	-	-	-	-	-	125,242	125,242	
Balance, December 31, 2011	88,640,887	2,746,712	3,819,185	6,309,109	12,875,006	6,780,365	108,296,258	
Additions	6,684,286				-	311,635	6,995,921	
Reductions			(218,477)	(93,158)	(311,635)	-	(311,635)	
Change in Net Assets	-	-	-	-	-	(530,553)	(530,553)	
Balance, December 31, 2012	\$ 95,325,173	\$ 2,746,712	\$ 3,600,708	\$ 6,215,951	\$ 12,563,371	\$ 6,561,447	\$ 114,449,991	

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The North Jersey District Water Supply Commission (the "Commission") is a public body politic and corporate established by Chapter 70 and 71, New Jersey Public Law 1916, and amended by Title 58 Chapter 5 of the Revised Statutes of 1937 (Section 58:5-1 et seq.). The law authorized the Commission to supply and distribute water to the counties of Sussex, Warren, Hunterdon, Passaic, Morris, Monmouth, Somerset, Bergen, Hudson, Essex, Union and Middlesex (the "District"). The Commission is empowered to finance, construct, and operate facilities necessary for the treatment, filtration, transmission, and distribution of potable water within the District.

The Commission is governed by a Board of Commissioners ("the Board") consisting of seven members appointed by the Governor, with the advice and consent of the Senate, to serve over-lapping four year terms. An executive director is appointed by the Board and functions chief executive officer responsible for the daily operations of the Commission.

The Commission has no stockholders and its investment in water supply facilities is jointly owned by the participating municipalities in proportion to the amount of water to be taken in the contract between each of the municipalities and the Commission.

The cost of operations of the several water supply projects is apportioned at the end of each year among the participating municipalities based on the amount of actual water consumed by each, but such amount shall not be less than the quantity contracted for. In apportioning operating costs, no participating municipality shall be charged with any item of expense or cost of operation of any water supply project, which is not used in supplying water to the respective municipality.

The Commission has the power to sell any unused water to any municipality or person for the amount of any contracting municipality or municipalities (hereinafter call the "interested municipality") having the right to use such water. The sale of unused water shall be at a price determined by the Commission, but not at a price lower than the cost of water to the interested municipality unless such municipality shall consent thereto.

The Governmental Accounting Standards Board (GASB) requires the financial reporting entity to include both the primary government and component units. Component units are legally separate organizations for which the Commission is financially accountable. The Commission is financially accountable for an organization if the Commission appoints a voting majority of the organization's governing board and (1) the Commission is able to significantly influence the programs or services performed or provided by the organization; or (2) the Commission is legally entitled to or can otherwise access the organization's resources; the Commission is legally obligated or has otherwise assumed the responsibility to finance the deficits of, or provide financial support to, the organization; or the Commission is obligated for the debt of the organization. Component units may also include organizations that are fiscally dependent on the Commission in that the Commission approves the budget, the issuance of debt or the levying of taxes. Based on such criteria, the Commission has no component units. Additionally, the Commission is not considered a component unit of any other entity.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A. Reporting Entity (Continued)

The Commission, in accordance with its authorization in R.S. 58:5-1 et seq. to supply water to interested municipalities in the North Jersey District, expanded the Ramapo Pump Station (formerly the Wanaque Ramapo Project), developed the Monksville Project and Wanaque South Pump Station. The operation of the Wanaque South Project is governed by an agreement executed on January 25, 1982 between the Commission and the participating municipalities. This report contains the financial statements of the Wanaque South Project only. The Commission does not issue entity wide financial statements and is therefore not in compliance with requirements of the Governmental Accounting Standards Board.

As a public body under existing statute, the Commission is exempt from both Federal and State taxes. The municipalities in the North Jersey District Water Supply contracting with the Commission to receive water as part of the Wanaque South Project are as follows:

<u>MUNICIPALITY</u>	<u>ALLOTMENT PER DAY (IN MILLIONS OF GALLONS)</u>
City of Newark	11.33
City of Bayonne	10.50
Town of Kearny	1.72
Township of Cedar Grove	1.20
Township of Nutley	3.00
Township of Wayne	9.00
Township of Bloomfield	<u>2.75</u>
	<u>39.50</u>

B. Measurement Focus, Basis of Accounting and Financial Statement Presentation

The accounts of the Commission are organized on the basis of funds, in accordance with the original Bond Resolution, each of which is considered a separate accounting activity. The operations of each system are accounted for with a separate set of self-balancing accounting records that comprise its assets, liabilities, net assets, revenues and expenses. Government resources are allocated and accounted for in individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled. The various activities are grouped into one generic fund type and one broad fund category, as follows:

Proprietary Fund Type

Enterprise Fund - The Enterprise Fund is used to account for governmental operations which are financed and operated in a manner similar to private enterprises, where the intent of the governing body is that the costs of providing goods or services to its participants on a continuing basis be financed or recovered primarily through participant charges.

NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Measurement Focus, Basis of Accounting and Financial Statement Presentation (Continued)

The Commission's financial transactions are recorded in accounts that are created by various resolutions adopted by the Commission to meet bond or note covenant requirements.

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the Commission are charges assessed to participants for water supply services. Operating expenses include the cost of operations and services and administrative expenses and bond principal payments. Revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. Transactions or other events that are both unusual in nature and infrequent in occurrence are reported as extraordinary items.

The Commission's financial statements are reported using the *economic resources measurement focus* and the *modified accrual basis of accounting*. Assets and liabilities associated with these operations are included on the Statement of Net Assets, with exceptions noted below. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, with exceptions noted below. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. These accounting principles differ in certain respects from accounting principles generally accepted in the United States of America (GAAP) applicable to government units. The more significant differences are noted below.

Revenues – Revenues are recognized on an accrual basis and include bond and loan proceeds as revenues. GAAP requires such revenues to be recognized in the accounting period when they become susceptible to accrual. GAAP does not recognize bond and loan proceeds as revenue for proprietary fund types.

Expenses – Expenses are recognized on the accrual basis and includes payments for bond principal and capital outlays as expenses. GAAP requires expenses to be recognized in the accounting period in which the liability is incurred, if measurable. GAAP does not recognize bond principal and capital outlay payments as expenses for proprietary fund types.

Inventories – The cost of inventories of supplies are recorded as expenditures at the time the individual items are purchased. However, there are inventories of minor plant supplies that are included on the statements of net assets.

Property, Plant and Equipment – Property, plant and equipment is recorded at cost with no recognition of depreciation. GAAP requires the recognition of depreciation of Property, Plant and Equipment for Proprietary Funds. The Wanaque North Project expenses debt principal payments in lieu of depreciation.

Loans Receivable – The Commission has participated in low cost financing through the New Jersey Environmental Infrastructure Trust ("NJEIT"). The Commission is reimbursed for allowable expenditures upon submission of a requisition evidencing actual expenditures.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Measurement Focus, Basis of Accounting and Financial Statement Presentation (Continued)

Debt Issuance – Debt issue costs and deferred charges on advance refundings are expensed when incurred. GAAP requires that these costs be capitalized and amortized over the life of the related bond issue.

Unearned Revenue – Unearned revenue consists primarily of the balance of funds available under the NJEIT loans, net of outstanding requisitions, amounts received from various sources that have not been expended and reserves for capital projects.

OPEB Liability–The Commission reports its annual other post-employment benefit (OPEB) expenses on a pay as you go basis. GAAP requires OPEB expenses be based on the annual required contribution (ARC) as determined under GASB 45 and a liability to be recorded for the net OPEB obligation at year end.

Net Assets – Net assets are reported in three components:

Investment in capital assets, net of related debt. – This category groups all capital assets, including infrastructure, into one component of net assets. The outstanding balances of debt that are attributable to the acquisition, construction or improvement of these assets reduce the balance in this category.

Restricted net assets – This category presents external restrictions imposed by creditors, grantors, contributors or laws or regulations or other governments and restrictions imposed by laws through constitution provisions or enabling legislation.

Operating Reserve – Established to provide funds to meet operational needs of the project in the event that budgeted quarterly collections are insufficient. The Reserve may not exceed 6 months of the operating budget, exclusive of debt service.

Debt Service – A cash reserve established to provide bond holders with assurance that cash will be available to meet scheduled bond payments in the event there is a shortfall in budgeted collections.

	<u>December 31, 2012</u>
Debt Service Reserve	\$3,600,708
Debt Service Requirement	<u>3,407,585</u>
	<u>\$ 193,123</u>

Debt Reserve – A Debt Service Reserve Fund is established under the South Bond Resolution for the benefit of all Bonds Outstanding from time to time thereunder. The South Bond Resolution defines the “Debt Service Reserve Fund Requirement” to mean, as of any date of computation, an amount which is equal to the lesser of (i) the greatest sum of interest and principal installments on Outstanding Bonds (which does not include the Subordinated Bonds) payable in the then current or any future calendar year, (ii) 125% of the average annual amount of interest and principal installments payable on Outstanding Bonds (which does not include the Subordinated Bonds) or (iii) 10% of the “proceeds” of Outstanding Bonds (which does not include the Subordinated Bonds). All or a portion of the Debt Service Reserve Fund Requirement may be provided in the form of a “Debt Service Reserve Credit Facility” meeting certain requirements contained in the South Bond Resolution. The Commission will satisfy the Debt Service Reserve Fund Requirement by obtaining a surety bond from the Bond Insurer in the initial face amount of \$5,031,500 with respect to the South 2003A Bonds and \$1,796,500 with respect to the South 2003B Bonds.

Renewal and Replacement – Funds which have been appropriated in the budgetary process for various purposes i.e. major plant repairs, upgrades, fleet renewal and replacement, etc.

NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Measurement Focus, Basis of Accounting and Financial Statement Presentation (Continued)

Net Assets (Continued)

Unrestricted net assets – This category represents net assets of the Wanaque South Project not restricted for any project or other purpose.

Capital Outlays – Capital projects that do not relate to infrastructure or other capitalizable assets are expensed in the period incurred. GAAP requires that these costs be capitalized and depreciated over the estimated life of the asset.

Budget - In accordance with the Commission's enabling legislation, the Commission holds public hearings and adopts an annual budget for operating expenses and capital outlays. The budget is adopted on a basis of consistent with the cash basis of accounting, including no provision for depreciation and amortization. It is monitored at various levels of classification detail within the enterprise funds. Expenses at the fund level may not exceed the total budget.

Use of Estimates – The preparation of financial statements requires management of the Commission 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 accrued revenues and expenditures during the reporting period. Accordingly, actual results could differ from those estimates.

Reclassifications - Certain reclassifications have been made to the December 31, 2011 balances to conform to the December 31, 2012 presentation.

C. Financial Statements – Modified Accrual Basis

The GASB Codification also requires the financial statements of a governmental unit to be presented in the basic financial statements in accordance with GAAP. The Commission presents the modified accrual basis financial statements listed in the table of contents which differ from the basic financial statements required by GAAP.

NOTE 2 DEPOSITS AND INVESTMENTS

The Commission considers petty cash, change funds, cash in banks, certificates of deposit and deposits with the New Jersey Cash Management Fund as cash and cash equivalents.

Deposits

The Commission's deposits are insured through either the Federal Deposit Insurance Corporation (FDIC), Securities Investor Protection Corporation (SIPC) or New Jersey's Governmental Unit Deposit Protection Act (GUDPA). The Commission is required to deposit their funds in a depository which is protecting such funds pursuant to GUDPA. The New Jersey Governmental Unit Deposit Protection Act requires all banks doing business in the State of New Jersey to pledge collateral equal to at least 5% of the average amount of its public deposits and 100% of the average amount of its public funds in excess of the lesser of 75% of its capital funds or \$200 million for all deposits not covered by the FDIC.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011**

NOTE 2 DEPOSITS AND INVESTMENTS (Continued)

Deposits (Continued)

Bank balances for interest bearing accounts are insured up to \$250,000 in the aggregate by the FDIC for each bank. Under the Dodd-Frank Wall Street Reform and Consumer Protection Act, temporary unlimited deposit insurance coverage was provided for non-interest bearing accounts from December 31, 2010 through December 31, 2012. SIPC replaces cash claims up to a maximum of \$250,000 for each failed brokerage firm. At December 31, 2012 and 2011, the book value of the Commission's deposits for the Wanaque South Project were \$15,361,789 and \$14,726,977 and bank and brokerage firm balances of the Commission's deposits for the Wanaque South Project amounted to \$15,361,789 at year end. The Commission's deposits which are displayed on the balance sheet as "cash and cash equivalents" are categorized as:

<u>Depository Account</u>	<u>Bank Balance</u> <u>2012</u>
Insured	\$ <u>15,361,789</u>

Custodial Credit Risk – Deposits – Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. The Commission does not have a formal policy for custodial credit risk. As of December 31, 2012 and 2011, the Commission's Wanaque South Project bank balances were not exposed to custodial credit risk.

Investments

The Commission is required by its Bond Resolutions to maintain each of its Wanaque South investments in the fund (account) in which the investment is made. In all accounts, except the operating accounts, the securities and the underlying collateral are held by the Bond Trustees and are within their care, custody and control. The type, quality and length of time of investment are regulated by the Bond Resolution.

Investments permitted under the Commission's Bond Resolution include the following:

- Direct obligations of the United States of America or obligations which are unconditionally guaranteed by the United States of America.
- Bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following federal agencies and provided such obligations are back by the full faith and credit of the United States of America: (1) U.S. Export-Import Bank; (2) Farmers Home Administration; (3) Federal Financing Bank; (4) Federal Housing Administration Debentures; (5) General Services Administration; (6) Government National Mortgage Association; (7) U.S. Maritime Administration; and (8) U.S. Department of Housing and Urban Development.
- Bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following non-full faith and credit U.S. government agencies: (1) Federal Home Loan Bank System; (2) Federal Home Loan Mortgage Corporation; (3) Federal National Mortgage Association; (4) Student Loan Marketing Association; (5) Resolution Funding Corp. obligations; and (6) Farm Credit System.
- Money market funds registered under the Federal Investment Company Act of 1940.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011**

NOTE 2 DEPOSITS AND INVESTMENTS (Continued)

Investments (Continued)

- Certificates of deposit secured at all times by collateral described above.
- Certificates of deposit, savings accounts, deposit accounts, or money market deposits which are fully insured by FDIC, including Bank Insurance Fund ("BIF") and Savings Association Insurance Fund ("SAIF").
- Investment Agreements, including Forward Purchase Agreements and Reserve Fund Put Agreements acceptable to Municipal Bond Insurance Association ("MBIA").
- Commercial paper rated, at the time of purchase "Prime – 1" by Moody's and "A-1" or better by Standard & Poor's ("S&P").
- Bonds or Notes issued by any state or municipality, which are rated, by Moody's and S&P in one of the two highest rating categories assigned by such agencies.
- Federal funds or bankers acceptances with a maximum term of one year of any bank which has an unsecured, uninsured and unguaranteed obligation rating of "Prime-1" or "A-3" or better by Moody's and "A-1" or "A" or better by S&P.
- The New Jersey Cash Management Fund and Repurchase Agreements for 30 days or less. Repurchase agreements, which exceed 30 days, must be acceptable to the insurer.

As of December 31, 2012 and 2011, the Commission had the following Wanaque South Project investments:

<u>Investment Type</u>	<u>Fair Value</u>	
	<u>2012</u>	<u>2011</u>
U.S. Government Security Funds		
Restricted	<u>\$ 7,106,679</u>	<u>\$ 7,076,087</u>

Custodial Credit Risk - Investments – For an investment, this is the risk, that in the event of the failure of the counterparty, the Commission will not be able to recover the value of its investments or collateral securities that are held by an outside party. The Commission does not have a policy for custodial risk. As of December 31, 2012 and 2011 \$7,106,679 and \$7,076,087, respectively of the Commission's Wanaque South Project investments were exposed to custodial credit risk as follows:

	<u>Fair Value</u>	
	<u>2012</u>	<u>2011</u>
Uninsured and Collateralized		
Collateral Held by Pledging Financial		
Institutions' Trust Department or Agent		
But Not in the Commission's Name	<u>\$ 7,106,679</u>	<u>\$ 7,076,087</u>

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011**

NOTE 2 DEPOSITS AND INVESTMENTS (Continued)

Investments (Continued)

Interest Rate Risk – The Commission does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk – The Bond Resolution limits investments as noted above. The Commission does not have an investment policy that would further limit its investment choices.

Concentration of Credit Risk – The Commission places no limit in the amount the Commission may invest in any one issuer. 100% of the Commission's Wanaque South Project investments are in U.S. Government Security Funds.

The fair value of the above-listed investments were based on market prices and values provided by the respective financial institution.

NOTE 3 RESTRICTED ASSETS

Bond covenants of the Commission require portions of the debt proceeds as well as other resources to be set aside for various purposes under the control of the Bond Trustee. These amounts are reported as restricted assets. The "Revenue Fund" account reserves all revenues received for future distribution to the various accounts of the Commission in accordance with the Bond Resolution. The "Construction Fund" account segregates cash and investments that are restricted for use in construction or capital asset acquisitions. Cash and investments restricted for debt service payment on bonds are segregated in "Bond Service Fund" and "Sinking Fund" accounts. Cash and investments reserved to meet future debt service contingencies are segregated in "Bond Reserve Fund" accounts. Cash and investments reserved for major repairs, renewals, replacements and non-routine maintenance items are segregated in "Renewal and Replacement Fund" accounts. Cash and investments reserved for funding any deficiencies under the bond resolution are segregated in the "General Fund" accounts. Cash and investments reserved to pay debt issuance costs on revenue bonds are segregated in the "Cost of Issuance" accounts.

NOTE 4 LOANS RECEIVABLE

The Commission has participated in low cost financing through the New Jersey Environmental Infrastructure Trust ("NJEIT"). The Commission is reimbursed for allowable expenditures upon submission of a requisition evidencing actual expenditures. At December 31, 2012 and 2011, the available balances are as follows:

	<u>2012</u>	<u>2011</u>
2000		\$ 216,000
2006	\$ 2,023,471	2,040,928
	<u>\$ 2,023,471</u>	<u>\$ 2,256,928</u>

NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

NOTE 5 CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2012 and 2011 was as follows:

<u>2012</u>	Balance, December 31, <u>2011</u>	<u>Increases</u>	<u>Decreases</u>	Balance, December 31, <u>2012</u>
Land	\$ 51,794			\$ 51,794
Buildings	115,409,221			115,409,221
Machinery and Equipment	1,863,954			1,863,954
Construction in Progress	<u>4,310,510</u>	<u>\$ 923,900</u>	<u>-</u>	<u>5,234,410</u>
	<u>\$ 121,635,479</u>	<u>\$ 923,900</u>	<u>\$ -</u>	<u>\$ 122,559,379</u>
<u>2011</u>	Balance, December 31, <u>2010</u>	<u>Increases</u>	<u>Decreases</u>	Balance, December 31, <u>2011</u>
Land	\$ 51,794			\$ 51,794
Buildings	115,409,221			115,409,221
Machinery and Equipment	1,863,954			1,863,954
Construction in Progress	<u>2,213,072</u>	<u>\$ 2,097,438</u>	<u>-</u>	<u>4,310,510</u>
	<u>\$ 119,538,041</u>	<u>\$ 2,097,438</u>	<u>\$ -</u>	<u>\$ 121,635,479</u>

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011**

NOTE 6 INVESTMENT IN DUNDEE WATER POWER AND LAND COMPANY

The Commission's Wanaque South Project has a 50% interest in Dundee Water Power and Land Company ("Dundee"), whose business purpose is the selling of land and water rights for power and processing. Wanaque South Project's investment includes amounts contributed for dam repairs and operating shortfalls. As of both December 31, 2012 and 2011, Wanaque South's Investment in Dundee was \$1,958,015.

NOTE 7 LONG TERM DEBT

A. Revenue Bonds

Revenue bonds outstanding as of December 31, 2012 and 2011 consist of the following:

	<u>2012</u>	<u>2011</u>
\$500,230, 1999 Project Revenue Bonds due in annual installments of \$12,785 to \$20,547 through August 1, 2019, interest at 4.75% to 5.70%. These bonds were retired in 2012		\$ 239,547
\$373,883, 2000 Project Revenue Bonds due in annual installments of \$19,735 to \$24,612 through August 1, 2020, interest at 5.05% to 5.25%	\$ 176,867	197,241
\$3,145,974, 2003 Project Revenue Refunding Bonds, due in annual installments of \$63,924 to \$99,311 through August 1, 2023	1,923,033	2,078,424

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011**

NOTE 7 LONG TERM DEBT (Continued)

A. Revenue Bonds (Continued)

	<u>2012</u>	<u>2011</u>
\$50,315,000, 2003A Project Revenue Bonds, due in annual installments of \$410,000 to \$4,820,000 through July 1, 2019, interest at 4.125%% to 5.25%	\$ 19,160,000	\$ 23,105,000
\$17,965,000 2003B Taxable Project Revenue Refunding Bonds, due in annual installments of \$150,000 to \$1,585,000 through July 1, 2019, interest at 4.79% to 5.19%	6,380,000	7,685,000
\$2,059,911, 2006 Project Revenue Bonds, due in annual installments of \$99,692 to \$122,133 through August 1, 2026, interest at 3% to 5%	<u>1,552,321</u>	<u>1,647,395</u>
	29,192,221	34,952,607
Less:		
Current Portion of Long-Term Debt	<u>(5,783,927)</u>	<u>(5,547,323)</u>
Non-Current Portion of Long-Term Debt	<u>\$ 23,408,294</u>	<u>\$ 29,405,284</u>

(a) The Series 1999 Bonds maturing on or after September 1, 2010, are subject to optional redemption prior to maturity at the option of the Commission upon the terms set forth in the respective Series 1999 Bond will not be subject to redemption prior to their respective stated maturity dates. The 1999 Bonds maturing on or after September 1, 2010 will be subject to optional redemption prior to maturity at the option of the Commission upon the terms set forth in the respective Series 1999 Bond Resolution, either in whole or in any series or any date or in part. Interest is calculated at rates ranging from 4.75% to 5.70% on \$149,538 and at various intervals through August 2019 and \$116,972 is non-interest bearing. Interest payments are due February 1st and August 1st each year.

(b) The Series I and II Bonds of 2000 shall be subject to optional redemption prior to maturity by or on behalf of the Commission in accordance with the terms and provisions set forth in the loan agreement and in accordance with the terms and provisions of Article VII of the Subordinate Bond Resolution. This obligation matures in 2020. Interest is calculated at rates ranging from 5.05% to 5.25% on \$120,000 at various intervals and \$95,476 is non-interest bearing. Interest payments are due February 1st and August 1st each year.

(c) The Series I and II Bonds of 2003 shall be subject to optional redemption prior to maturity by or on behalf of the Commission in accordance with the terms and provisions set forth in the loan agreement and in accordance with the terms and provisions of the Article IV of the General Bond Resolutions. Interest is calculated at rates ranging from 3% to 5% at various intervals through August 2023 and interest payments are due February 1st and August 1st each year.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011**

NOTE 7 LONG TERM DEBT (Continued)

A. Revenue Bonds (Continued)

(d) The Series 2003A Bonds maturing on and before July 1, 2013 are not subject to optional redemption. The Series 2003A Bonds maturing on and after July 1, 2014 are subject to redemption, at the option of the Commission prior to maturity, upon the giving of notice as provided in the South Bond Resolution, as a whole or at any time or in part on any interest payment date in such order of maturity and the Commission shall direct and by lot within any maturity, on or after July 1, 2013 at the redemption price of 100% of the principle amount of the Series 2003A Bonds to be redeemed plus accrued interest thereon to the date fixed for redemption. Interest is calculated at rates ranging from 3% to 5% at various intervals through July 2023. Interest payments are due January 1st and July 1st each year.

(e) The Series 2003B Bonds are not subject to optional redemption. The Series 2003B Term Bonds maturing July 1, 2019 are subject to mandatory redemption prior to maturity, upon the giving of notice as provided in the South Bond Resolutions, in part by lot, by operation or the sinking fund which has been established and created under the terms of the South Bond Resolutions on July 1 each year as set forth in the official statement. Interest is calculated at rates ranging from 3% to 5% on \$3,915,000 at various intervals through July 2013 and 5.19% on \$5,015,000 on term bonds maturing July 2019. Interest payments are due January 1st and July 1st each year.

(f) The Series I and II Bonds of 2006 shall be subject to optional redemption prior to maturity by or on behalf of the Commission in accordance with the terms and provisions set forth in the loan agreement and in accordance with the terms and provisions of Article IV of the General Bond Resolutions. Interest is calculated at rates ranging from 3% to 5% on \$672,600 at various intervals to August 2026 and \$1,071,538 is non-interest bearing. Interest payments are due February 1st and August 1st each year.

The Commission's schedule of principal and interest requirements for long-term debt of the Wanaque South project issued and outstanding as of December 31, 2012 is as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
<u>Year Ended December 31</u>			
2013	\$ 5,783,927	\$ 1,382,819	\$ 7,166,746
2014	6,069,509	1,103,044	7,172,553
2015	6,373,129	794,587	7,167,716
2016	6,701,047	470,864	7,171,911
2017	857,617	130,097	987,714
2018-2022	2,733,277	248,586	2,981,863
2023-2026	<u>673,715</u>	<u>28,457</u>	<u>702,172</u>
	<u>\$ 29,192,221</u>	<u>\$ 4,158,454</u>	<u>\$ 33,350,675</u>

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011**

NOTE 7 LONG TERM DEBT (Continued)

B. Changes in Long Term Liabilities

The Commission's long-term liability activity for the Wanaque South Project for the years ended December 31, 2012 and 2011 are as follows:

<u>2012</u>	Balance, December 31, <u>2011</u>	<u>Increases</u>	<u>Decreases</u>	Balance, December 31, <u>2012</u>
Revenue Bonds	\$ 34,952,607	\$ -	\$ 5,760,386	\$ 29,192,221

<u>2011</u>	Balance, December 31, <u>2010</u>	<u>Increases</u>	<u>Decreases</u>	Balance, December 31, <u>2011</u>
Revenue Bonds	\$ 40,233,230	\$ -	\$ 5,280,623	\$ 34,952,607

Unearned revenue consists of the balance of funds available under the NJEIT loans, net of outstanding requisitions, and other deferred revenue. The deferred revenue for the years ended December 31, 2012 and 2011 related to the NJEIT Loans were \$2,023,471 and \$2,256,928, respectively.

NOTE 8 RELATED COMPANY TRANSACTIONS

Inter-project payable

There are common infrastructure components ("water treatment") of the Commission shared by the participating municipalities of the Wanaque North and Wanaque South Projects. The costs associated with the maintenance of these common infrastructure components are shared by the Wanaque South Project based upon a predetermined formula for prorating water treatment costs, as well as allocation of general overhead costs. At December 31, 2012 and 2011, the amounts due to the Wanaque North Project are as follows:

	<u>2012</u>	<u>2011</u>
Operating	\$1,493,221	\$ 385,679
Loan Reallocation	283,399	424,880
Construction	<u>1,333,442</u>	<u>462,332</u>
	<u>\$3,110,062</u>	<u>\$1,272,891</u>

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011**

NOTE 8 RELATED PARTY TRANSACTIONS (Continued)

Due to Wanaque South Joint Venture

The Wanaque South Project has a 50% interest in the Wanaque South Project, a Joint Venture (the "JV"). The JV is a joint venture, formed in December 1981, between Wanaque South Project and United Water New Jersey ("UWNJ") (collectively, the "co-owners") for construction of a new pumping station, enlargement of an existing pump station, a transmission pipeline, a reservoir and the continued maintenance of the project. The co-owners have agreed to share equally, the costs of operating the JV, except for certain real estate and sales taxes, which are paid entirely by UWNJ. An annual operating budget is prepared and adopted by the Commission. As of December 31, 2012 and 2011, the amount due to the JV was \$261,220 and \$796,481, respectively. The advances are non-interest bearing, payable on demand.

The governing board and management of the joint venture consist of personnel from both partners in the venture. The personnel have the ability to approve budgets, sign contracts with exercise control over facilities and to determine the outcome or disposition of matters affecting the recipients of services provided. At December 31, 2012 and 2011, the Equity in the JV is \$2,500.

NOTE 9 EMPLOYEE RETIREMENT SYSTEMS

The State of New Jersey sponsors and administers the following contributory defined benefit public employee retirement system (retirement system) covering substantially all state and local government employees which includes those Commission employees who are eligible for pension coverage.

Public Employees' Retirement System (PERS) – established in January 1955, under the provisions of N.J.S.A. 43:15A to provide coverage, including post-retirement healthcare for those eligible employees whose local employers elected to do so, to substantially all full-time employees of the State or any county, municipality, school district, or public agency provided the employee is not a member of another State-administered retirement system. Membership is mandatory for such employees and vesting occurs after 10 years of service for pension benefits and, if applicable, 25 years for post-retirement healthcare coverage.

Other Pension Funds

The state established and administers a Supplemental Annuity Collective Trust Fund (SACT) which is available to active members of the State-administered retirement systems to purchase annuities to supplement the guaranteed benefits provided by their retirement system. The state or local governmental employers do not appropriate funds to SACT.

The cost of living increase for PERS is funded directly by the system, but is currently suspended as a result of reform legislation.

According to state law, all obligations of the retirement system will be assumed by the State of New Jersey should the retirement system be terminated.

The State of New Jersey, Department of the Treasury, Division of Pensions and Benefits, issues publicly available financial reports that include the financial statements and required supplementary information of the above systems, funds, and trust. The financial reports may be accessed via the New Jersey, Division of Pensions and Benefits website at www.state.nj.us/treasury/pensions.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011**

NOTE 9 EMPLOYEE RETIREMENT SYSTEMS (Continued)

Basis of Accounting

The financial statements of the retirement system is prepared on the accrual basis of accounting. Employer contributions are recognized when payable to the retirement systems. Benefits or refunds are recognized when due and payable in accordance with the terms of the retirement systems.

Significant Legislation

P.L. 2011, c.78, effective June 28, 2011, made various changes to the manner in which PERS operates and to the benefit provisions of the system.

This new legislation's provisions impacting employee pension and health benefits include:

- For new members of PERS hired on or after June 28, 2011 (Tier 5 members), the years of creditable service needed for early retirement benefits increased from 25 to 30 years and the early retirement age increased from 55 to 65.
- The eligibility age to qualify for a service retirement in the PERS increased from age 62 to 65 for Tier 5 members.
- It increased the active member contribution rates from 5.5 percent of annual compensation to 6.5 percent plus an additional 1 percent phased-in over 7 years. For Fiscal Year 2012, the member contribution rates increase in October 2011. The phase-in of the additional incremental member contributions for PERS members will take place in July of each subsequent fiscal year.
- The payment of automatic cost-of-living adjustment (COLA) additional increases to current and future retirees and beneficiaries was suspended. COLA increases may be reactivated at a future date as permitted by this law.
- It changed the method for amortizing the pension system's unfunded accrued liability (from a level percent of pay method to a level dollar of pay method).

Investment Valuation

Investments are reported at fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Mortgages are valued on the basis of future principal and interest payments, and are discounted at prevailing interest rates for similar instruments. The fair value of real estate investments is based on independent appraisals. Investments that do not have an established market are reported at estimated fair values.

The State of New Jersey, Department of the Treasury, Division of Investment, issues publicly available financial reports that include the financial statements of the State of New Jersey Cash Management Fund, Common Pension Fund A, Common Pension Fund B, Common Pension Fund D and Common Pension Fund E. The financial reports may be obtained by writing to the State of New Jersey, Department of the Treasury, Division of Investment, P.O. Box 290, Trenton, New Jersey 08625-0290.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011**

NOTE 9 EMPLOYEE RETIREMENT SYSTEMS (Continued)

Funded Status and Funding Progress

As of July 1, 2011, the most recent actuarial valuation date, the aggregate funded ratio for all the State administered retirement systems, including PERS is 67.5 percent with an unfunded actuarial accrued liability of \$41.7 billion. The aggregate funded ratio and unfunded accrued liability for the State-funded systems is 60.8 percent and \$30.1 billion, and the aggregate funded ratio and unfunded accrued liability for local systems, including PERS, is 77.5 percent and \$11.6 billion, respectively.

The funded status and funding progress of the retirement systems includes actuarial valuations which involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. These amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the probability of future events.

Actuarial calculations reflect a long-term perspective and are based on the benefits provided under the terms of the retirement systems in effect at the time of each valuation and also consider the pattern of the sharing of costs between the employer and members at that point in time. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and members in the future.

Actuarial Methods and Assumptions

In the July 1, 2011 actuarial valuation, the projected unit credit was used as the actuarial cost method, and the five year average of market value was used as the asset valuation method for the retirement systems. The actuarial assumptions included (a) a revised investment rate of return for all the retirement systems from 8.25 percent to 7.95 percent; and (b) revised projected salary increases which vary by fund (4.52% for PERS).

Employer and Employee Pension Contributions

The contribution policy is set by laws of the State of New Jersey and contributions are required by active members and participating employers. Plan members and employer contributions may be amended by State of New Jersey legislation, with the amount of contributions by the State of New Jersey contingent upon the annual Appropriations Act. As defined, the PERS retirement system requires employee contributions based on 6.50% of employees' annual compensation.

Annual Pension Cost (APC)

Per the requirements of GASB Statement No. 27 for the year ended June 30, 2012 for PERS, which is a cost sharing multi-employer defined benefit pension plan, annual pension cost equals contributions made.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011**

NOTE 9 EMPLOYEE RETIREMENT SYSTEMS (Continued)

Annual Pension Cost (APC) (Continued)

During the years ended December 31, 2012, 2011 and 2010, the Commission was required to contribute for normal cost pension contributions, accrued liability pension contributions, early retirement incentive program contributions, and non-contributory life insurance premiums the following amounts which equaled the required contributions for each respective year:

<u>Year Ended December 31,</u>	<u>PERS</u>	<u>Allocated to Wanaque South</u>
2012	\$1,204,173	\$274,913
2011	1,163,781	265,691
2010	915,826	209,083

NOTE 10 DEFERRED COMPENSATION PLAN

The Commission offers its employees a Deferred Compensation Plan (the "DCP Plan") created in accordance with Internal Revenue Code Section 457. The DCP plan is administered by the Nationwide Retirement Solutions and The Hartford. The DCP plan permits employees to defer a portion of their salary to future years. Individuals are one hundred percent vested. The DCP Plan, which began formal operations November 1990, is funded solely from voluntary employee deductions. Distribution is available to employees upon termination, retirement, death or unforeseeable emergency. All amounts of compensation deferred under the plan are solely property and rights of the individual contributors and are not subject to the claims of the Commission's general creditors.

NOTE 11 POST RETIREMENT MEDICAL BENEFITS

Plan Description

The Commission offers post employment medical, prescription drug, dental and vision benefits, to retirees and their eligible dependents. Medicare Part B premiums are reimbursed for Medicare eligible retirees and their spouses.

The following subsections outline the eligibility for retirement that would qualify a retiree for Commission-paid postretirement health benefits for the various groups of Commission employees.

- Age 60,
- After 25 years of service,
- After 25 years or more of service and are age 55 or older.
- After 10 years of service for disability retirement,
- Surviving spouse and dependent children under 26 are covered until spouses death or remarriage.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011**

NOTE 11 POST RETIREMENT MEDICAL BENEFITS (Continued)

Annual OPEB Cost and Net OPEB Obligation

The Commission's annual other post-employment benefit (OPEB) cost (expense) is calculated based on the *annual required contribution of the employer (ARC)*, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The following table shows the components of the Commission's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the Commission's net OPEB obligation to the plan.

	<u>District-Wide</u>
Annual Required Contribution	\$ 2,399,496
Interest on Net OPEB Obligation	285,693
Adjustment to Annual Required Contribution	<u>212,179</u>
Total (Annual OPEB Cost (Expense))	2,897,368
Contributions Made	<u>(1,296,759)</u>
Increase in Net OPEB Obligation	1,600,609
Net OPEB Obligation - Beginning of Year	<u>7,142,316</u>
Net OPEB Obligation - End of Year	<u>\$ 8,742,925</u>

The Commission's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the years 2012, 2011 and 2010 were as follows:

<u>Year Ended December 31,</u>	<u>District-Wide</u>		
	<u>Annual OPEB Cost</u>	<u>Percentage of Annual OPEB Cost Contributed</u>	<u>Net OPEB Obligations</u>
2012	\$ 2,897,368	44.75%	\$ 8,742,925
2011	2,788,824	44.49%	7,142,316
2010	2,682,981	43.15%	5,594,412

Funded Status and Funding Progress

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Actuarial Methods and Assumptions

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

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011**

NOTE 12 RISK MANAGEMENT

The Commission is exposed to various risks of loss related to general liability, automobile coverage, theft of, damage to and destruction of assets; errors and omissions; injuries to employees; termination of employees and natural disasters. The Commission has obtained commercial insurance coverage to guard against these events to minimize the exposure to the Commission should they occur.

There has been no significant reduction in insurance coverage from the previous year.

NOTE 13 CONTINGENT LIABILITIES

The Commission is a party defendant in some lawsuits, none of a kind unusual for a entity of its size and scope of operation. In the opinion of the Commission's Attorney, the potential claims against the Commission not covered by insurance policies would not materially affect the financial condition of the Commission.

The Commission is subject to various regulations promulgated by the U.S. and State of New Jersey Department of Environmental Protection (collectively, "DEP"). Laws and regulations governing DEP are complex and subject to interpretation. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines and penalties. The Commission is not aware of non-compliance of said laws and regulations.

State Awards - The Commission participates in state programs that are fully or partially funded by grants received from other governmental units. Expenditures financed by grants are subject to audit by the appropriate grantor government. If expenditures are disallowed due to noncompliance with grant program regulations, the Commission may be required to reimburse the grantor government. As of December 31, 2012 and 2011, significant amounts of grant expenditure have not been audited by the various grantor agencies but the Commission believes that disallowed expenditures, if any, based on subsequent audits will not have a material effect on the overall financial position of the Commission.

NOTE 14 FEDERAL ARBITRAGE REGULATIONS

The Commission is subject to Section 148 of the Internal Revenue Code as it pertains to the arbitrage rebate on all tax-exempt obligations, both long and short-term debt. Under the 1986 Tax Reform Act, the Internal Revenue Service (IRS) required that all excess earnings from investment proceeds be rebated to the IRS. Arbitrage, for purposes of these regulations, is defined as the difference between the yield on the investment and the yield on the obligations issued. If there are excess earnings, this amount may be required to be rebated to the IRS. At December 31, 2012 and 2011, the Commission has not estimated its estimated arbitrage earnings due to the IRS, if any, pertaining to the Wanaque South Project.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAQUE SOUTH PROJECT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011**

NOTE 15 CONSTRUCTION AND OTHER SIGNIFICANT COMMITMENTS

As of December 31, the Commission had the following commitments in the Wanaque South Project with respect to unfinished capital projects:

<u>Capital Project</u>	<u>Paid as of December 31, 2012</u>	<u>Remaining Commitment</u>	<u>Allocated to Wanaque South</u>
Water Treatment Plant Improvements	\$ 11,197,070	\$ 1,502,230	\$ 378,543

NOTE 16 PRIOR PERIOD ADJUSTMENT

The December 31, 2011 net assets have been adjusted for certain prior year assets and liabilities.

	<u>Balance Prior to Adjustment</u>	<u>Adjustment</u>	<u>Balance Subsequent to Adjustment</u>
ASSETS			
Investment in Dundee Water Power and Land Company Assessments Receivable	\$ 2,382,894	\$ (424,879)	\$ 1,958,015
		424,879	424,879
LIABILITIES			
Unearned Revenue	3,534,353	(1,277,425)	2,256,928
Encumbrances Payable		204,416	204,416
NET ASSETS			
Investment in Capital Assets	87,315,356	1,325,531	88,640,887
Restricted and Unrestricted	19,907,893	(252,522)	19,655,371

SUPPLEMENTARY SCHEDULES

NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
SCHEDULE OF ACTUAL REVENUES AND EXPENDITURES COMPARED TO BUDGET
FOR THE YEAR ENDED DECEMBER 31, 2012
(With Comparative Amounts for the Year Ended December 31, 2011)

	2012 <u>Budget</u>	2012 <u>Actual</u>	<u>Variance</u>	2011 <u>Actual</u>
Revenues:				
Assessments	\$ 16,049,691	\$ 16,049,691		\$ 16,049,690
Anticipated Income	290,000	68,419	\$ 221,581	123,121
NJEIT Loan Proceeds	<u>-</u>	<u>5,380</u>	<u>(5,380)</u>	<u>2,097,438</u>
 Total Revenues	 <u>16,339,691</u>	 <u>16,123,490</u>	 <u>216,201</u>	 <u>18,270,249</u>
Expenditures:				
Direct Expenses				
Common Facilities	388,000	391,972	(3,972)	467,847
Wanaque South Pump Station	918,758	502,483	416,275	268,810
Ramapo Pump Station	71,025	50,943	20,082	37,117
Monksville Reservoir	42,500	42,386	114	43,900
Allocated Wanaque North Operating Costs	4,984,111	4,639,582	344,529	4,370,479
Allocated Joint Venture Operating Costs	3,211,477	2,618,136	593,341	2,762,956
Use Fee	277,247	277,212	35	277,796
Amortization of Assessments Receivable	21,202	21,202	-	21,742
Debt Service	7,196,737	7,186,227	10,510	7,184,461
Capital Items	<u>437,697</u>	<u>923,900</u>	<u>(486,203)</u>	<u>2,709,899</u>
 Total Expenditures	 <u>17,548,754</u>	 <u>16,654,043</u>	 <u>894,711</u>	 <u>18,145,007</u>
 Excess of Revenue Over Expenditures	 <u>\$ (1,209,063)</u>	 <u>\$ (530,553)</u>	 <u>\$ (678,510)</u>	 <u>\$ 125,242</u>

Note: Wanaque North and Joint Venture participation is included in this schedule.

NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
 WANAEQUE SOUTH PROJECT
 SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN RESTRICTED AND UNRESTRICTED NET ASSETS BY FUND
 FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011

	Operating	Revenue	Construction	Debt Service	Total (Memo Only)	
					2012	2011
OPERATING REVENUES						
Municipal Assessments	\$ 8,394,055	-	\$ 437,697	\$ 7,217,939	\$ 16,049,691	\$ 16,049,690
TOTAL OPERATING REVENUES	8,394,055	-	437,697	7,217,939	16,049,691	16,049,690
OPERATING EXPENDITURES						
Payroll and Related Expenses	2,785,458				2,785,458	3,955,591
Utilities and Fuel	1,046,709				1,046,709	744,652
Chemicals	843,096				843,096	499,824
Pump Station and Other	94,359				94,359	135,995
Real Estate Taxes	720,639				720,639	634,846
Use Fee	277,212				277,212	277,796
Insurance	1,561,009				1,561,009	1,274,251
Legal and Accounting	208,323				208,323	211,248
Engineering and Consulting	63,813				63,813	23,613
Supplies and Expenses	715,236				715,236	407,119
Trustee Fees	56,034			7,470	63,504	63,970
Bond Principal	-	-	-	5,547,323	5,547,323	5,290,623
TOTAL OPERATING EXPENDITURES	8,371,888	-	-	5,554,793	13,926,681	13,519,528
OPERATING INCOME	22,167	-	437,697	1,663,146	2,123,010	2,530,162
NON OPERATING REVENUES (EXPENSES)						
Interest Income	33,509	\$ 412	299	2,751	36,971	71,653
Amortization of Assessments Receivable				(21,202)	(21,202)	(21,742)
Interest Expense				(1,638,904)	(1,638,904)	(1,893,838)
NJEIT Loan Proceeds			218,443		218,443	2,097,438
Capital Outlay	(143,356)		(923,900)		(1,067,256)	(2,709,899)
Bond Principal Refunded				(213,063)	(213,063)	-
Grants and Other Income	31,448				31,448	51,468
Transfer in	9,032	8,620		215,892	233,544	10,971
Transfer out	-	(9,032)	(215,892)	(8,620)	(233,544)	(10,971)
TOTAL NON OPERATING REVENUES (EXPENSES)	(69,367)	-	(921,050)	(1,663,146)	(2,653,563)	(2,404,920)
EXCESS (DEFICIENCY) OF REVENUE OVER (UNDER) EXPENDITURES	\$ (47,200)	\$ -	\$ (483,353)	\$ -	\$ (530,553)	\$ 125,242

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
ROSTER OF OFFICIALS
DECEMBER 31, 2012**

The following officials were in office at December 31, 2012:

COMMISSIONERS

Charles P. Shotmeyer, Chairman

Carmen A. Orechio, Vice-Chairman

Jerome P. Amedeo

Alan S. Ashkinaze

Donald C. Kuser

EXECUTIVE OFFICERS

Todd Caliguire

Executive Director

Joseph E. Stroin, Jr.

Chief Operating Officer

Danielle Holobinko

Chief Financial Officer

Angelo Valente

Commission Secretary

GOVERNMENT AUDITING STANDARDS

LERCH, VINCI & HIGGINS, LLP

CERTIFIED PUBLIC ACCOUNTANTS
REGISTERED MUNICIPAL ACCOUNTANTS

17 - 17 ROUTE 208
FAIR LAWN, NJ 07410
TELEPHONE (201) 791-7100
FACSIMILE (201) 791-3035
WWW.LVHCPA.COM

DIETER P. LERCH, CPA, RMA, PSA
GARY J. VINCI, CPA, RMA, PSA
GARY W. HIGGINS, CPA, RMA, PSA
JEFFREY C. BLISS, CPA, RMA, PSA
PAUL J. LERCH, CPA, RMA, PSA
DONNA L. JAPHET, CPA, PSA
JULIUS B. CONSONI, CPA, PSA

ELIZABETH A. SHICK, CPA, RMA, PSA
ANDREW PARENTE, CPA, RMA, PSA
ROBERT W. HAAG, CPA, PSA
DEBORAH K. LERCH, CPA, PSA
DEBRA GOLLE, CPA
CINDY JANACEK, CPA, RMA
RALPH M. PICONE, CPA, RMA, PSA
EDWARD N. KERE, CPA

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

INDEPENDENT AUDITOR'S REPORT

Honorable Chairman and Members of the Board of Commissioners
North Jersey District Water Supply Commission
Wanaque, New Jersey

We have audited, in accordance with the 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, the financial statements –modified accrual basis of the North Jersey District Water Supply Commission Wanaque South Project, as of and for the year ended December 31, 2012, and the related notes to the financial statements, and have issued our report thereon dated June 20, 2013. Our report on the financial statements – modified accrual basis indicated that the financial statements were not prepared and presented in accordance with accounting principles generally accepted in the United States of America but rather prepared and presented in accordance with the modified accrual basis of accounting as described in Note 1.

Internal Control over Financial Reporting

Management of the North Jersey District Water Supply Commission Wanaque South Project is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit of the financial statements, we considered the North Jersey District Water Supply Commission Wanaque South Project's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements but not for the purpose of expressing an opinion on the effectiveness of the North Jersey District Water Supply Commission Wanaque South Project's internal control. Accordingly, we do not express an opinion on the effectiveness of the North Jersey District Water Supply Commission Wanaque South Project's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Commission's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and responses as items 2012-1 through 2012-3 that we consider to be significant deficiencies in internal control over financial reporting.

Compliance and Other Matters

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

We also noted certain matters that we reported to management of the North Jersey District Water Supply Commission Wanaque South Project in a separate report of audit entitled; "Auditor's Management Report".

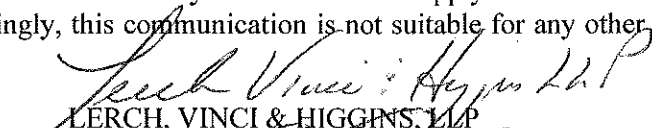
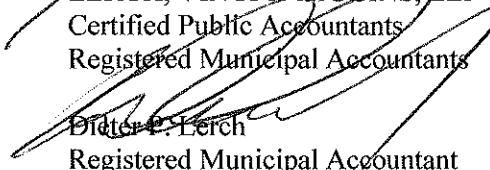
North Jersey District Water Supply Commission Wanaque South Project's Responses to Findings

The North Jersey District Water Supply Commission - Wanaque South Project's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. The North Jersey District Water Supply Commission Wanaque South Project's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the responses.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the North Jersey District Water Supply Commission Wanaque South Project's internal control or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the North Jersey District Water Supply Commission Wanaque South Project's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Fair Lawn, New Jersey
June 20, 2013


LERCH, VINCI & HIGGINS, LLP
Certified Public Accountants
Registered Municipal Accountants

Dieter P. Lerch
Registered Municipal Accountant
RMA Number CR00398

GOVERNMENT AUDITING STANDARDS

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
SCHEDULE OF FINDINGS AND RESPONSES
FOR THE YEAR ENDED DECEMBER 31, 2012**

Part I – Summary of Auditor's Results

Financial Statement Section

Type of auditor's report issued:	<u>Adverse (GAAP); Unqualified (Modified Accrual)</u>	
Internal control over financial reporting:		
1) Material weakness(es) identified?	_____ yes	<u>X</u> no
2) Were significant deficiency(ies) identified that were not considered to be material weaknesses?	<u>X</u> yes	_____ none reported
Noncompliance material to the basic financial statements noted?	_____ yes	<u>X</u> no

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
SCHEDULE OF FINDINGS AND RESPONSES
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

Part 2 – Schedule of Financial Statement Findings

This section identifies the significant deficiencies, material weaknesses, fraud, illegal acts, violations of provisions of contracts and grant agreements and abuse related to the financial statements in accordance with Government Auditing Standards.

Finding 2012-1:

Certain inventory is not being reported on the Commission's financial statements.

Criteria or specific requirement:

Generally Accepted Accounting Principles

Condition:

The Commission reports inventory only for items maintained in Administration. Various other independent inventory locations exist, but are not reported by the Commission.

Context:

An inventory system exists and is reported for items maintained in Administration. Inventory maintained at other locations are not integrated with administration and are not reported on the Commission's financial statements.

Effect:

The Commission's financial statements are misstated due to the underreporting of inventory.

Cause:

Unknown.

Recommendation:

A central warehouse and inventory control system be developed and implemented for the maintenance of inventory and all items be reported on the Commission's financial statements.

Management's Response:

A central warehouse system is being developed for implementation in 2013.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
SCHEDULE OF FINDINGS AND RESPONSES
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

Part 2 – Schedule of Financial Statement Findings

This section identifies the significant deficiencies, material weaknesses, fraud, illegal acts, violations of provisions of contracts and grant agreements and abuse related to the financial statements in accordance with Government Auditing Standards.

Finding 2012-2:

The Computer software utilized for the issuance of checks for disbursement is not integrated with the Commission's accounting software. As such, instances were noted where check numbers reported in the accounting system were not in agreement with actual check numbers issued..

Criteria or specific requirement:

Internal controls over cash disbursements

Condition:

Separate software systems are utilized for the accounting and check writing functions. These systems are not integrated.

Context:

Check numbers for disbursements reported in the accounting system were not always in agreement with actual check numbers issued for the respective disbursements.

Effect:

Check numbers in the financial reporting system do not reflect actual check numbers issued.

Cause:

Unknown.

Recommendation:

Internal controls be enhanced, whereby the computer software utilized for the issuance of checks be integrated with the Commission's accounting software.

Management's Response:

A software upgrade is being sought to integrate the systems.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
SCHEDULE OF FINDINGS AND RESPONSES
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

Part 2 – Schedule of Financial Statement Findings

This section identifies the significant deficiencies, material weaknesses, fraud, illegal acts, violations of provisions of contracts and grant agreements and abuse related to the financial statements in accordance with Government Auditing Standards.

Finding 2012-3:

The payroll clerk has the ability to revise data entered into the time management system subsequent to supervisor approval and prior to payroll processing.

Criteria or specific requirement:

Internal controls over human resources and payroll processing

Condition:

Subsequent to supervisor approval, electronically entered time management data can be accessed and revised by the payroll clerk prior to the processing of payroll.

Context:

Approved hours worked for certain time management entries were revised by the payroll clerk prior to payroll processing.

Effect:

Employees may be paid for hours worked which are not in agreement with hours approved in the time management system.

Cause:

Unknown.

Recommendation:

Internal controls be reviewed and enhanced to ensure that adequate controls are in place to prohibit the payroll clerk from unilaterally altering the time management entries.

Management's Response:

Internal controls over time management entry and approvals will be reviewed and enhanced.

**NORTH JERSEY DISTRICT WATER SUPPLY COMMISSION
WANAQUE SOUTH PROJECT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

This section identifies the status of prior year findings related to the financial statements and federal and state awards that are required to be reported in accordance with Chapter 6.12 of *Government Auditing Standards*, U.S. OMB Circular A-133 (Section .215(a)(b)) and New Jersey OMB Circular 04-04.

Finding 2011-1

The Commission did not have various account analysis supporting account balances and activity prior to the issuance of internal financial statements. However, management did provide post-closing adjustments and related support after the initial trial balance was provided.

Current Status

Corrective action has been taken.

Finding 2011-2

The Commission did not adhere to, or did not have written documentation, regarding policies and procedures with respect to payroll, related expenses and fringe benefits, such as health and life insurance benefits, pension and post-retirement benefits.

Current Status

Corrective action has been taken.

Finding 2011-3

The Commission did not adhere to the New Jersey Statutory Bidding Law, which requires that any contracts for goods and services exceeding \$17,500 be put out to bid. In addition, the Commission did not obtain quotes for goods and services below \$17,500 and above \$2,625.

Current Status

Corrective action has been taken.

Finding 2011-4

The Commission did not have in place a disaster recovery plan for the Commission's computer systems, which includes the accounting and administrative functions.

Current Status

Corrective action has been taken.