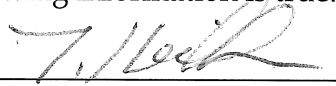


Internal Monitoring Report

Policy # EL-2D Financial Condition and Activities
Frequency: Three times a year

Date: October 23, 2012

I certify that the following information is true.

Signed , General Manager

Policy Language:

With respect to the actual, ongoing financial condition and activities of the Madison Water Utility, the General Manager shall not cause or allow the development of fiscal jeopardy or a material deviation of actual expenditures from board priorities established in Outcomes policies.

Accordingly, the General Manager shall not cause or allow conditions, procedures or decisions that:

1. Fail to ensure long-term financial health.
2. Fail to present a balanced annual operating budget and quarterly updates on actual expenditures and income.
3. Exceed total appropriations for the fiscal year, unless directed to do so by the board.
4. Use any dedicated reserves for purposes other than those for which they are designated, unless directed to do so by the board.
5. Undertake a debt without payoff schedule and identification of revenue stream.
6. Fail to establish an unrestricted reserve equal to a typical three months' operating expenses.
7. Fail to inform the board of where the utility stands with any current rate case in progress.

General Manager's interpretation and its justification:

This Executive Limitations policy requires the Utility to perform financial management without risk of jeopardy to the Utility's financial health and that ensures actual expenditures do not deviate materially from board priorities established in Outcomes policies. The Utility has the responsibility to establish, manage and plan for the necessary water rates and borrowings to fund all expenditures to meet identified capital and operational requirements, and that are budgeted and reported on accordingly.

Data directly addressing the General Manager's interpretation:

1. *Ensure the Utility's long-term financial health.*

The external report of auditor's unqualified opinion on the Utility's financial statements for the years ended December 31, 2011 and 2010, was presented to the board by a representative of Baker Tilly Virchow Krause, LLP at its August 28, 2012 meeting.

The 2013 Capital Budget of \$27,810,000 was reviewed by the City's Board of Estimates on September 11, 2012. The 2013 Operating Budget of \$33,317,468 was approved by the board at its August 28, 2012 meeting and reviewed by the Board of Estimates on October 9, 2012.

The Utility has implemented and uses a financial planning model to evaluate and project funding required to finance infrastructure and operating needs. Through the use of this model, bond sales are planned and rate increases are developed.

The General Manager is not aware of any past or present event or matter that would give rise to a future materially adverse condition affecting the long-term financial health of the Utility.

I report compliance.

2. *Present a balanced annual operating budget and quarterly updates on actual expenditures and income.*

The 2013 Operating Budget is a balanced budget as submitted. The second quarter update on 2012 actual expenditures and income is attached herewith.

I report compliance.

3. *Total appropriations for the fiscal year shall not be exceeded, unless directed to do so by the board.*

As of June 30, 2012, capital expenditures totaled \$5,624,806 compared to the budget of \$25,109,300 for the 2012 fiscal year. A report of capital expenditures compared to budget by individual project is attached herewith.

I report compliance.

4. *Dedicated reserves shall not be used for purposes other than those for which they are designated, unless directed to do so by the board.*

The Utility's restricted reserves are accessible only through the City of Madison Treasurer's office. The Utility's Fund Balance report as of June 30, 2012, is attached herewith.

I report compliance.

5. *Debt shall not be undertaken without a payoff schedule and identification of revenue stream.*

The Utility's debt repayment schedules for all debt undertaken and outstanding as of December 31, 2011, were presented to the board at its August 28, 2012 meeting. Included was the repayment schedule for the Utility's working capital loan from the City of Madison.

A Revenue Bond issue of approximately \$21.1 million is scheduled for November 27, 2012. The bond issue will fund the balance of the Utility's 2012 capital budget and part of the 2013 capital budget. The last bond issue was on December 22, 2011.

I report compliance.

6. *Establish an unrestricted reserve equal to a typical three months' operating expenses.*

The Utility currently is not funding its unrestricted reserve and likely will not do so until it completes the repayment of its loan from the City of Madison by December 31, 2019.

I report non-compliance.

7. *Inform the board of where the Utility stands with any current rate case in progress.*

The Utility plans to file a formal rate increase application - approximately 12% - with the Public Service Commission of Wisconsin in October 2012. The last rate increase of 9% was granted on May 3, 2011, and became fully effective on January 1, 2012.

I report compliance.

Attachments:

- A. Actual Operating Expenditures and Income Update as of second quarter 2012
- B. Capital Expenditures compared to Budget Update as of second quarter 2012
- C. Fund Balance Report as of June 30, 2012

MADISON WATER UTILITY

Comparative Income Statement

| | Six (6) Months Ended June 30, | |
|---------------------------------------|----------------------------------|--------------|
| | 2012 | 2011 |
| Operating Revenue | \$14,811,331 | \$14,270,114 |
| Operating Expenses: | | |
| Source of Supply | 27,421 | 14,859 |
| Pumping | 1,625,083 | 1,502,737 |
| Water Treatment | 236,723 | 243,995 |
| Transmission and Distribution | 1,708,424 | 1,639,765 |
| Customer Accounts | 188,001 | 165,959 |
| Administrative and General | 1,694,572 | 2,069,914 |
| Total Operation & Maintenance Expense | \$5,480,224 | \$5,637,229 |
| Depreciation | 2,432,113 | 2,270,810 |
| Payment in lieu of Taxes (PILOT) | 2,477,266 | 2,259,885 |
| Total Operating Expense | \$10,389,603 | \$10,167,924 |
| Operating Income | \$4,421,728 | \$4,102,190 |
| Interest Income | 83,750 | 131,993 |
| Other Income(Expense) | 9,685 | 223 |
| Interest Expense | (1,934,196) | (1,926,484) |
| Net Income | \$2,580,967 | \$2,307,922 |

**MADISON WATER UTILITY
2012 CAPITAL BUDGET EXPENDITURES
THROUGH JUNE 30, 2012**

| | CAPITAL BUDGET | JAN | FEB | MAR | APR | MAY | JUNE | EXPENDITURES TO DATE | REMAINING |
|--|-------------------|---------|---------|---------|-----------|-----------|-----------|-------------------------|------------|
| 1 METER PROGRAM | \$0 | 0 | 0 | 0 | 0 | 0 | 0 | \$0 | \$0 |
| 2 WATER MAINS - REPLACEMENTS | 7,816,000 | 283,082 | 262,663 | 155,802 | 293,583 | 709,110 | 656,839 | 2,361,079 | 5,454,921 |
| 3 WATER MAINS - NEW | 835,000 | 9,476 | 4,921 | 11,381 | 94,301 | 35,063 | 181,009 | 336,151 | 498,849 |
| 4 SCADA SYSTEM | 32,000 | 0 | 246 | 647 | 30,869 | 0 | 0 | 31,762 | 238 |
| 5 ZONE 4 FIRE FLOW SUPPLY AUGMENTATION | 1,161,000 | 47,430 | 2,875 | 7,417 | 3,225 | 5,355 | 15,644 | 81,946 | 1,079,054 |
| 6 ARBOR HILLS SUPPLEMENTAL FIRE FLOW SUPPLY | 1,000,000 | 181,615 | 86,127 | 165,664 | 265,428 | 99,326 | 69,926 | 868,086 | 131,914 |
| 7 EAST SIDE WATER SUPPLY PROJECT | 3,747,000 | 8,513 | 9,308 | 43,776 | 73,230 | 97,514 | 36,021 | 268,362 | 3,478,638 |
| 8 PRESSURE ZONE 9 STORAGE | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 9 PRESSURE ZONES 7 & 8 SUPPLEMENTAL SUPPLY | 130,000 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 130,000 |
| 10 PUMP STATION 220 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 11 LAKEVIEW RESERVOIR - RECONSTRUCTION | 263,000 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 263,000 |
| 12 BOOSTER PUMP STATION 114 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 13 NORTH END SUPPLEMENTAL SUPPLY | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 14 SECURITY UPGRADES | 100,000 | 3,580 | 2,959 | 10,750 | 9,698 | 5,951 | 4,060 | 36,998 | 63,002 |
| 15 SYSTEMWIDE MISCELLANEOUS PROJECTS | 309,300 | 8,635 | 973 | 5,648 | 559 | 1,813 | 2,752 | 20,380 | 288,920 |
| 16 PATERSON STREET BUILDING REMODEL | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 17 ADVANCED METERING INFRASTRUCTURE (PROJECT H ₂ O) | 8,400,000 | 71,648 | 82,699 | 77,542 | 347,607 | 452,555 | 408,115 | 1,440,166 | 6,959,834 |
| 18 BOOSTER STATION 106 - REBUILD | 200,000 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 200,000 |
| 19 ZONE 11 - BLACKHAWK ELEVATED STORAGE | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 20 MISCELLANEOUS PUMP STATION / PRV / FACILITY PROJECTS | 1,116,000 | 1,745 | 3,129 | 171,261 | 1,348 | 486 | 1,907 | 179,876 | 936,124 |
| 21 BOOSTER PUMP STATION 129 RECONSTRUCTION | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 22 IRON & MANGANESE FILTER @ WELL 19 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 23 IRON & MANGANESE FILTER @ WELL 30 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| 24 NEAR WEST SIDE WATER SUPPLY PROJECT | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| | 25,109,300 | 615,724 | 455,900 | 649,888 | 1,119,848 | 1,407,173 | 1,376,273 | 5,624,806 | 19,484,494 |

Fund Balance Report

| | <u>June 30, 2012</u> | <u>Dec. 31, 2011</u> |
|--|----------------------|----------------------|
| Reserves required by Bond Ordinance | | |
| Operation and Maintenance Fund | | |
| * Reserve Account (Minimum \$150,000) | \$150,000 | \$150,000 |
| Special Redemption Fund | | |
| * Principal and Interest Account | \$3,944,511 | \$4,869,877 |
| * Reserve Account (Minimum \$8,343,538) | \$8,427,692 | \$8,383,387 |
| Depreciation Fund ⁽¹⁾ | \$750,000 | \$750,000 |
| Construction Fund | \$5,574,872 | \$11,199,678 |
| Assessment Revolving Fund | \$74,753 | \$0 |
| Unrestricted Funds | | |
| PILOT Fund | \$2,460,000 | \$4,519,770 |
| Cash Flow Fund | \$350,234 | (\$349,449) |
| Unrestricted Reserve Fund | \$0 | \$0 |
| Checking Account | \$413,525 | \$251,532 |
| Debt to City of Madison | | |
| Short Term Construction Fund Loan | \$0.00 | \$0.00 |
| Short Term Loan from City | \$5,737,500 | \$6,120,000 |

(1) Transfer of funds to Construction Fund approved as needed.
Reporting special fund balances as specified in 1978 Waterworks Bond Ordinance