

**Cape Fear Public Utility Authority
Wilmington, North Carolina**

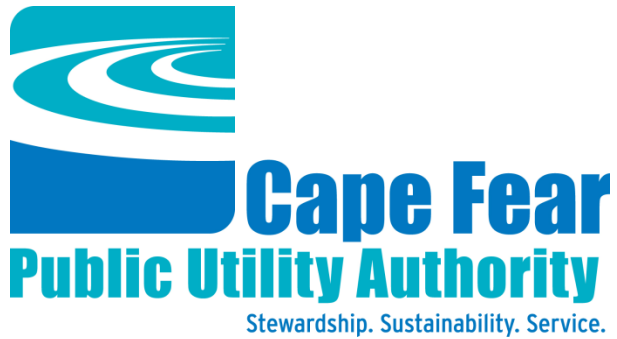
COMPREHENSIVE ANNUAL FINANCIAL REPORT

For the fiscal year ended June 30, 2011



**Cape Fear
Public Utility Authority**

Stewardship. Sustainability. Service.



COMPREHENSIVE ANNUAL FINANCIAL REPORT

**CAPE FEAR PUBLIC UTILITY AUTHORITY
WILMINGTON, NORTH CAROLINA
For The Fiscal Year Ended June 30, 2011**

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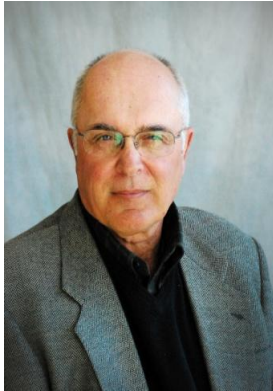
Introductory Section

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**Cape Fear Public Utility Authority Board
For the fiscal year ended June 30, 2011**



Gene Renzaglia
Chairman



J. C. Hearne II
Vice Chairman



Michael C. Brown III
Secretary



Burrows Smith
Treasurer



Brian Berger
Commissioner



Rick Catlin
Commissioner



Patricia O. Kusek
Member



Jim Quinn
Member



Charlie Rivenbark
Councilman



Ronald Sparks
Councilman

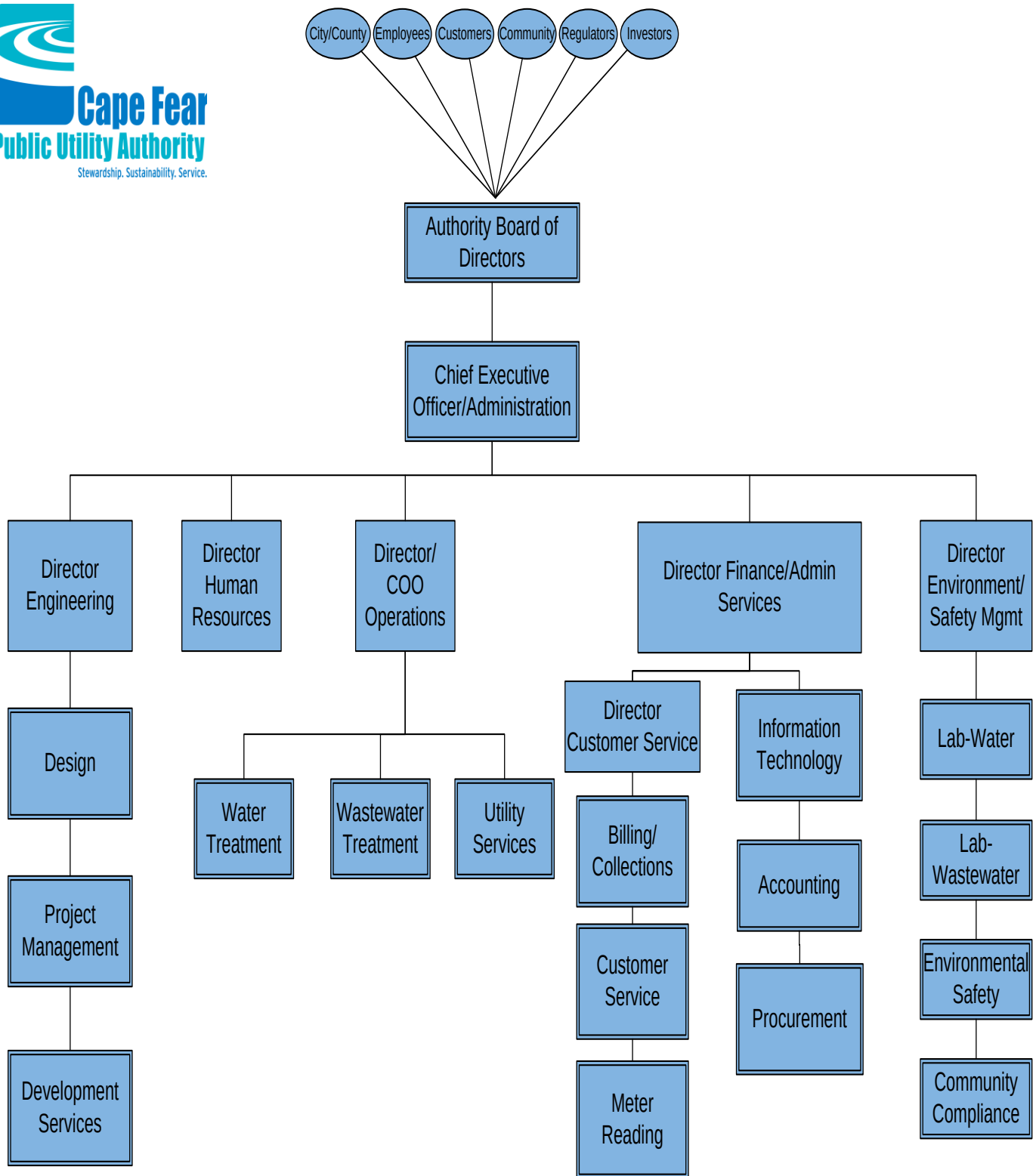


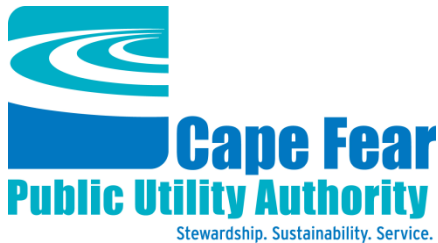
Cindee Wolf
Member

Other Principal Officers

Matthew W. Jordan, PE
Chief Executive Officer

Cheryl J. Spivey, CPA
Chief Financial Officer





October 28, 2011

To the Cape Fear Public Utility Authority Board, Customers, and Bondholders:

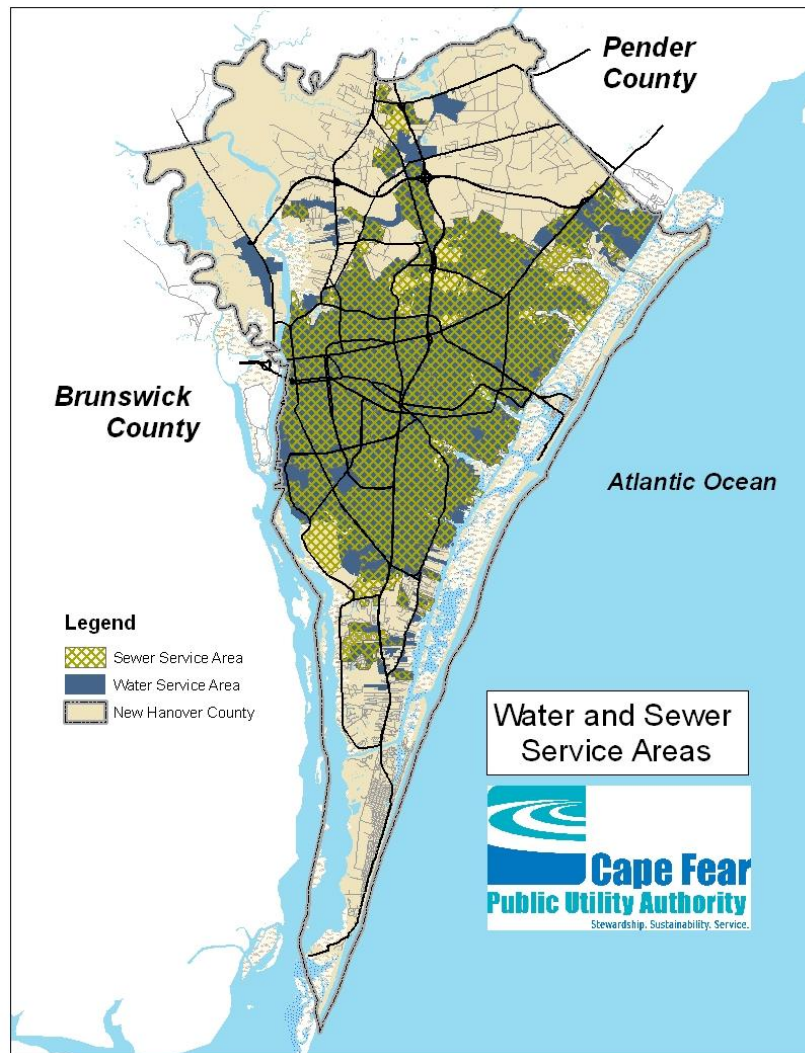
We are pleased to submit the Comprehensive Annual Report (CAFR) of the Cape Fear Public Utility Authority (CFPUA or Authority) for the fiscal year ended June 30, 2011. This report conforms to the reporting and accounting standards of the Governmental Accounting Standards Board (GASB), the Financial Accounting Standards Board (FASB), and the Government Finance Officers Association (GFOA).

The Authority's management is responsible for the accounting system and for establishing and maintaining internal financial controls. The internal control system is designed to provide reasonable assurance regarding (1) the safeguarding of assets against loss from unauthorized use or disposition and (2) the reliability of financial records for preparing financial statements in conformity with accounting principles generally accepted in the United States of America and maintaining accountability for assets. The concept of reasonable assurance recognizes that the cost of a control should not exceed its likely benefits and the evaluation of costs and benefits requires estimates and judgments by management.

Management assumes full responsibility for both the accuracy of the data presented and the completeness and fairness of the presentation, including all disclosures. To the best of our knowledge and belief, the enclosed financial data is accurate in all material aspects and fairly presents the financial position of the Authority. All disclosures necessary to enable the reader to gain an understanding of the Authority's financial activities have been included.

Please refer to the Management's Discussion and Analysis (MD&A) and the basic financial statements for detailed information on The Authority's financial performance in FY 2011. The basic financial statements have been audited by our independent auditors, McGladrey & Pullen, LLP, who issued an unqualified opinion on the financial statements of the Authority for the year ended June 30, 2011. Their audit was performed in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards, and accordingly, included such tests of the accounting records and other such auditing procedures as they considered necessary. The independent auditor's report is presented as the first component of the financial section of this report.

The Authority was formed by the City of Wilmington and New Hanover County to combine the water and sewer operations, and began operations on July 1, 2008. The Cape Fear Public Utility Authority was established pursuant to the Chapter 162A, Article 1 of the North Carolina General Statutes, known as the North Carolina Water and Sewer Authorities Act. The Authority's service area consists of the City of Wilmington and areas of New Hanover County served by the New Hanover County Water and Sewer District (District). It does not include the municipalities of Carolina Beach, Kure Beach, and Wrightsville Beach. New Hanover County's population is approximately 202,700 in an area encompassing approximately 220 square miles. New Hanover County is the second smallest county in North Carolina by land area and is also the second most densely populated of the 100 counties.



An eleven-member board governs the Authority. The City and County appoint five members each, with two of those appointments coming from their respective governing boards. The eleventh member is jointly appointed. The Authority board is responsible for the adoption of the annual budget, setting water and sewer rates, making policy decisions; and appointing the Executive Director, Clerk to the Board, and Authority's General Counsel.

The annual budget serves as the foundation for the Authority's financial planning and control. The annual operating budget is adopted by the Authority board at a functional level with capital project ordinances adopted on a multi-year basis. The Authority's operations are accounted for and reported as an enterprise fund, as provided services are funded by user fees and charges. Budget-to-actual comparisons are provided in this report for the annually appropriated operating fund. Multi-year capital projects are presented on a separate schedule with year to date and project to date information.

System Description

The Water System

The water system is comprised of a surface water system and a groundwater system. There are currently few interconnects between the two systems; however, the Capital Improvement Program (CIP) includes several interconnect projects. There are a total of 67,500 water connections with 65,000 active customer accounts and 1,070 miles of distribution lines at June 30, 2011. The Authority also keeps six wells on standby to supplement the water supply during peak demand periods.

The Authority has a needs contract to purchase up to 23.0 MGD of raw water from the Lower Cape Fear Water and Sewer Authority (LCFWSA) with a term ending in 2030. Raw surface water is either drawn from the Cape Fear River through the Authority's 15.0 million gallon per day (MGD) raw water intake at King's Bluff or purchased through a connection with the

LCFWSA at U.S. Highway 421. The raw surface water is pumped to the Sweeney Water Treatment Plant (SWTP), which provides potable water to the majority of the Authority's service area. The SWTP utilizes upflow clarification with ozonation as the primary disinfection method, followed by filtration and chlorine disinfection, fluoridation, corrosion control, and pH adjustment. The SWTP has a rated capacity of 27.5 MGD, and average production during the fiscal year ended June 30, 2011 of 13.7 MGD. The SWTP is being expanded to have the capability of processing up to 35 MGD. The expansion includes demolition of the old abandoned portion of the water treatment plant that predates 1910 and demolition of the older section of the current water treatment plant that predates 1958. These aging facilities will be replaced with new facilities incorporating the latest, more innovative water treatment technologies currently being used in the newer part of the plant, and the addition of a UV disinfection facility. The SWTP has stayed online, processed and distributed clean water throughout construction. This project is expected to be complete in summer 2012. The surface water distribution system has been providing water service for more than 50 years and includes 16.0 million gallons of covered ground storage of finished water and 5 million gallons of storage in three elevated tanks.

In October 2009, the Authority placed a Nano-Filtration Groundwater Membrane Plant (the Nano Plant) into operation to serve the northeast section of the distribution system. The source of raw water is from 25 wells located in two different aquifers. The plant softens the groundwater and removes many organic and inorganic contaminants to produce a blended groundwater that is followed by disinfection, fluoridation, corrosion control and pH adjustment. The Nano Plant has a rated capacity of 6.0 MGD. The Nano Plant had a daily average production during the fiscal year ended June 30, 2011 of 3.24 MGD. The distribution system provides water service to customers and includes 2.0 million gallons of covered ground storage and 2.75 million gallons of elevated storage in six elevated tanks. In addition, the Authority operates two smaller groundwater systems providing groundwater directly to customers from seven wells and two elevated storage tanks. The groundwater receives disinfection and pH adjustment before being pumped to the distribution system and the storage tanks.

The Wastewater System

The Authority currently serves approximately 65,000 wastewater connections with 63,000 active customers in and around the Authority's service area and provides wholesale wastewater treatment services to the Town of Wrightsville Beach. The Authority's collection system consists of approximately 840 miles of gravity lines, 20,300 manholes, 141 pump stations and 104 miles of pressurized sewage force main.

The Authority currently owns and operates the James Loughlin, or Northside Wastewater Treatment Plant (NSWWTP), the M'Kean Maffitt, or Southside Wastewater Treatment Plant (SSWWTP) and the Walnut Hills Wastewater Treatment Plant (the Walnut Hills Plant). Although the NSWWTP is currently permitted to treat up to 10.0 MGD, the completion of an expansion to the NSWWTP by the end of calendar year 2011 will increase the permitted limit to 16.0 MGD. The SSWWTP is permitted to treat up to 12.0 MGD. The Walnut Hills Plant is a smaller facility permitted to treat up to 0.1 MGD. For the fiscal year ended June 30, 2011, the combined average daily flows were 15.83 MGD of the combined 22.1 MGD permitted. The NSWWTP and the SSWWTP use physical, chemical and biological processes to clean the wastewater. Screening and settling processes help remove most suspended materials. Biological processes, utilizing bacteria, aid with removing the remainder of the suspended materials and the dissolved substances. Organic material left over from the treatment process undergoes further treatment at each plant. These solids are nutrient rich and are utilized locally for farming operations. After the wastewater flows are collected and treated, the treated effluent is discharged back into the Cape Fear River.

The Authority has a sewer use ordinance in place that is administered under the Authority's pretreatment program. The pretreatment program monitors and regulates significant wastewater dischargers connected to the Authority's wastewater collection system. Currently, six significant industrial users are permitted under the program and have discharge limits for Biochemical Oxygen Demand (BOD), Total Suspended Solids (TSS), Chemical Oxygen Demand (COD), oil and grease, chlorides, ammonia, Total Kjeldahl Nitrogen (TKN), fluoride, certain metals, and organics, as applicable. Most of these significant users pre-treat their wastewater prior to discharging such waste to the Authority, and all submit monthly monitoring reports. The Authority conducts semi-annual monitoring. Surcharges apply to waste that exceeds sewer use ordinance limits. An enforcement response plan is also in place to address any permit violations.

Economic Condition and Outlook

The service area of the Authority, comprising most of New Hanover County, continues to be the economic, medical, and educational hub for the surrounding counties that comprise southeastern North Carolina. The area has been one of the fastest growing in the nation with a population increase of over 26% since 2000. Tourism is the area's largest economic component in terms of employment and revenues. New Hanover County was ranked nine out of 100 counties in the state with over \$400 million

in travel-related revenues in calendar year 2010, a 6.9% increase over revised 2009 revenues. Tourism provided over 5,000 jobs with an annual payroll of almost \$92 million in New Hanover County.

Major employers in New Hanover County include New Hanover Regional Medical Center, New Hanover County Board of Education, GE Wilmington, University of North Carolina at Wilmington, New Hanover County, PPD Inc, Corning Incorporated, Wal-Mart, City of Wilmington, and Cape Fear Community College.

Although the area has been significantly affected by the recent economic crisis, the fiscal year ended June 30, 2011 showed signs of recovery. Water consumption increased 5.3%, compared to a 10.7% decrease the previous year. Wastewater consumption increased 5.5%. Taxable sales receipts in New Hanover County were up 11.7%. Room occupancy tax receipts increased 8.7%. New Hanover County reported a 16% increase in the number of building permits and a 30% increase in project costs compared to the prior year. However, the County's unemployment rate at June 30, 2011 of 10.1% is slightly higher than the 9.8% at June 30, 2011. It is lower than North Carolina's 10.4% and higher than the United States' 9.3%.

Long-Term Financial Planning

The Authority utilizes a 10-year model to forecast revenue requirements based on anticipated operating expenditures, debt service, and capital needs.

Relevant Financial Policies

The Authority has established a comprehensive set of financial policies including the following:

Finance and Accounting Policy	Consistency of Budgeting and Financial Reporting Policy
Investment Policy	Revenue Policy
Budget Policy	Budget Amendment and Transfer Policy
Reserve Policy	Contract Approval Policy
Debt Management Policy	Capital Improvements Program Policy
Corporate Governance Policy	Travel Policy

Major Initiatives and Accomplishments for FY 2011

In the Authority's third year of operations a number of initiatives were undertaken. These initiatives embrace the Authority's guiding principles of Stewardship, Sustainability, and Service.

Capital Projects: During the year ended June 30, 2011, the Authority had over 100 active capital projects in process and approximately \$43 million in expenditures. A number of the projects were underway by the City and County when the Authority began operations. The Capital Improvement Plan (CIP) for the ten-year period from FY 2012 to FY 2021 totals over \$353 million. The largest capital expenditures during the year were for the following projects:

- Sweeney Water Treatment – \$73.8 million project to increase the SWTP treatment capacity from 27.5 mgd to 35 mgd, with an ultimate plant capacity of 44 mgd. Process upgrades and improvements are included. Ongoing.
- Ogden Interceptor Replacement - \$5.8 million project to replace approximately 1.5 miles of 30-inch and 36-inch gravity interceptor located in a remote area that was failing. This project removed the existing pipe and installed new ductile iron pipe. Completed 2011.
- Southside Wastewater Treatment Plant Rehab & Upgrade (Design) – \$8.6 million design and upgrade of treatment processes and capacity expansion. This project will upgrade the existing plant processes and increase capacity from 12 mgd to 16 mgd. Ongoing.

- Northeast Interceptor Rehabilitation (NEI) Project, including Pump Stations 34 & 35 - \$9.4 million project to increase wastewater conveyance capacity and upgrade aging infrastructure associated with the critical NEI force main and two regional pump stations (PS 34 & PS 35). Among other things, larger pumps and an emergency generator were installed at PS 35, and a new bar screen was installed at PS 34. Phase 1 Complete.
- Middle Sound Sewer - Prior to formation of the Authority, a New Hanover County project to provide sewer to a significant portion of the Middle Sound area was underway. This \$2.6 million project resurfaced streets that were affected by construction. Substantially Complete.
- Northern Route Force Main – \$17.3 million force main project that will direct flows to the Northside Wastewater treatment plant and away from the NEI and the Southside Wastewater treatment plant. This project constructs approximately 4.4 miles of 24-inch force main. Ongoing.
- Asset Management - \$2.5 million project which includes a Computer Maintenance Management System. Asset Management will enable the Authority to manage infrastructure capital assets while minimizing the total cost of ownership and operation. As part of this program, the Authority is building a Geographic Information System based on real time data, which will be used for a variety of general asset collection projects and enhance the Authority's ability to link Customer Service, Operations, Engineering, Environmental Service Management and other joint services. The system will define where/when maintenance activities should occur, and develop strategies for deploying resources in the most efficient ways. The program includes Maximo software. Phase 1 Complete.
- Northside Wastewater Treatment Plant Force Main - \$5.8 million project to construct approximately 2.2 miles of 30-inch force main to convey treated effluent to its discharge. Part of the Northside plant expansion. Ongoing.
- System-Wide Odor Corrosion Control Program - \$2.2 million project to install 23 chemical dosing stations and 20 monitoring units in the wastewater conveyance system to reduce odor and control corrosive gas. Ongoing.

Environmental Management System (EMS) - EMS has been developed and is being implemented within the Authority. The Authority's EMS will ultimately include all areas of the organization. During the fiscal year ended June 30, 2011, the Utility Services Collection System section was the first group to be incorporated into EMS. This group consists of preventative maintenance, video assessment, pump station maintenance and operations and outfall maintenance.

Other Accomplishments – The Authority also accomplished the following during the year:

- Continued to improve relationships with federal, state and local regulatory agencies;
- Reduced sewer odors within the community;
- Reduced spillage from the sewer system;
- Improved water quality for consumption;
- Quickly and aggressively responded to infrastructure failures;
- Continued a septage receiving program;
- Continued increased educational outreach;
- Proactively worked as environmental stewards to minimize and/or prevent environmental impacts.

Certificate of Achievement for Excellence in Financial Reporting

The Government Finance Officers Association of the United States and Canada (GFOA) awarded the Certificate of Achievement for Excellence in financial Reporting to the Authority for its comprehensive annual financial report for the fiscal year ended June 30, 2010. This was the second consecutive year that the Authority has achieved this prestigious award. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

Acknowledgements

We appreciate the support of Authority members for their policy guidance in financial matters. Preparation of this report was accomplished through the dedicated efforts of the entire staff of the Finance department.

Respectfully submitted,



Matthew W. Jordan, P.E.
Chief Executive Officer



Cheryl J. Spivey, CPA
Chief Financial Officer

Certificate of Achievement for Excellence in Financial Reporting

Presented to
Cape Fear Public Utility Authority
North Carolina

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2010

A Certificate of Achievement for Excellence in Financial
Reporting is presented by the Government Finance Officers
Association of the United States and Canada to
government units and public employee retirement
systems whose comprehensive annual financial
reports (CAFRs) achieve the highest
standards in government accounting
and financial reporting.



President

Executive Director

Financial Section

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Independent Auditor's Report

To the Board of Directors
Cape Fear Public Utility Authority
Wilmington, North Carolina

We have audited the accompanying basic financial statements of Cape Fear Public Utility Authority (the "Authority"), as of and for the year ended June 30, 2011, as listed in the table of contents. These financial statements are the responsibility of the Cape Fear Public Utility Authority's management. Our responsibility is to express 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 includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Cape Fear Public Utility Authority as of June 30, 2011, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 25, 2011 on our consideration of the Cape Fear Public Utility Authority'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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management's Discussion and Analysis on pages 15 through 21 and the Other Post-Employment Benefits Schedule of Funding Progress and Schedule of Employer Contributions on page 49 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of Cape Fear Public Utility Authority as a whole. The supplementary schedules listed in the table of contents on pages 50 through 54 and pages 75 through 82 are not a required part of the basic financial statements. The accompanying schedule of expenditures of Federal and State awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and the State Single Audit Implementation Act, and is not a required part of the basic financial statements. The supplementary schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

The accompanying introductory and statistical sections, as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements. This information has not been subjected to the auditing procedures applied in the audit of the basis financial statements and, accordingly, we express no opinion on them.

McGladrey & Pullen, LLP

Wilmington, North Carolina
October 25, 2011

Management's Discussion and Analysis (Unaudited)

The management of Cape Fear Public Utility Authority, (the "Authority"), offers readers of our financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal year ended June 30, 2011. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal, which can be found on pages 1 through 6 of this report.

Financial Highlights

- The overall financial condition of the Authority remained stable during the year ended June 30, 2011. Assets of the Authority exceeded its liabilities at the close of the fiscal year by \$359.6 million (net assets) which is about the same as the previous year. Of this amount, \$72.0 million is unrestricted net assets that may be used to meet the Authority's ongoing obligations to customers and creditors.
- Unrestricted net assets increased \$7.8 million.
- Total operating revenues were \$59.8 million, an increase of \$9.9 million or 19.9% over the prior year. The increase in revenues reflects increases in water and sewer charges effective May 1, 2010 and May 1, 2011, as well as an increase in demand for service.
- Total operating expenses (including depreciation and amortization) were approximately \$43.8 million, an increase of approximately \$.3 million, or less than 1%, from fiscal 2010.
- Operating income increased to \$16.0 million from \$6.4 million in the prior year.
- Overall debt coverage increased to 1.65 for fiscal year 2011 from 1.44 the previous year, remaining above the 1.0 ratio required by bond covenants. Coverage on revenue bond debt was 2.80, also remaining above the 1.2 ratio required by revenue bond covenants.
- The Authority maintained a credit rating of AA from Standard & Poor's and AA2 from Moody's.

Overview of the Financial Statements

The Authority's primary mission is to provide water and sewer services to the City of Wilmington and the unincorporated areas of New Hanover County. The Authority does not provide other general purpose government services or programs. The Authority's operations, capital expansion program and debt payments are funded almost entirely through rates, fees and other charges for these water and sewer services. As such, the Authority is considered to be, and therefore presents the Authority's financial report, as a stand-alone enterprise fund.

Enterprise fund financial statements. As a stand-alone enterprise fund, the Authority's basic financial statements consist of a *Statement of Net Assets*, a *Statement of Revenues, Expenses and Changes in Net Assets* (Equity) and a *Statement of Cash Flows*. These statements, together with the *Management's Discussion and Analysis*, provide both short-term and long-term financial information about, and implications for the Authority's financial position. To provide a better understanding of the information contained in these statements, *Notes to the Financial Statements* and a *Statement of Revenues and Expenditures – Budget and Actual*, appear immediately following the basic financial statements. In addition to this discussion and analysis, other required supplementary information, generally statistical and demographic in nature, is presented.

The *Statement of Net Assets* presents information on the Authority's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating.

The *Statement of Revenues, Expenses and Changes in Net Assets* presents information showing how the Authority's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The basic enterprise fund financial statements can be found on pages 23 through 26 of this report.

Management's Discussion and Analysis (Unaudited)

Notes to Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes to the financial statements can be found on pages 27 through 48 of this report.

Financial Analysis

Table A presents the Condensed Statement of Net Assets for the years ended June 30, 2011 and June 30, 2010.

The Cape Fear Public Utility Authority's Condensed Statement of Net Assets

Table A

	June 30, 2011	June 30, 2010
Current assets	\$ 115,004,763	\$ 104,898,714
Noncurrent assets-restricted and other	17,466,875	62,599,620
Noncurrent assets-capital	559,699,622	534,154,033
Total assets	692,171,260	701,652,367
Current liabilities	36,297,085	32,293,356
Noncurrent liabilities	296,288,570	309,770,739
Total liabilities	332,585,655	342,064,095
Net Assets		
Invested in capital assets, net of related debt	287,538,728	295,307,938
Unrestricted	72,046,877	64,280,334
Total net assets	\$ 359,585,605	\$ 359,588,272

As noted earlier, net assets may serve over time as a useful indicator of an Authority's financial position. In the case of the Authority, assets exceeded liabilities by \$359.6 million at June 30, 2011, which is about the same as the previous year. Capital assets net of related debt comprised 80.0% of total net assets at June 30, 2011. These capital assets are essential in providing water and sewer services to our customers and consequently, these assets are not available for future spending. The resources needed to repay the associated debt must be provided by other sources. At June 30, 2011, these other resources totaled \$72.0 million, an increase of 12.1%, or \$7.8 million over the prior year. As mentioned earlier, the increase in operating revenues with minimal increase in operating expenditures (including depreciation and amortization) was primarily responsible for the increase in unrestricted assets in the current year.

Management's Discussion and Analysis (Unaudited)

Table B presents for the reader the Condensed Statement of Revenues, Expenses and Changes in Net Fund Assets for the years ended June 30, 2011 and June 30, 2010.

Condensed Statement of Revenues, Expenses and Change in Net Assets

Table B

	Year Ended June 30, 2011	Year Ended June 30, 2010
Revenue		
Operating revenue		
Charges for services	\$ 57,086,229	\$ 47,524,673
Other operating revenue	2,671,784	2,313,214
Nonoperating revenue		
Investment earnings	738,453	4,105,897
Contributions from New Hanover County	1,900,000	1,900,000
Total revenue	62,396,466	55,843,784
Expenses		
Operating expenses	29,495,995	30,357,906
Depreciation and amortization	14,283,401	13,096,230
Nonoperating expense		
Interest expense	13,011,609	10,909,406
Amortization	230,087	235,208
Total expenses	57,021,092	54,598,750
Increase in net assets before capital contributions, special items and extraordinary items	5,375,374	1,245,034
Capital contributions-other	2,813,350	7,982,758
Special impairment of capital assets	(8,191,391)	(2,275,200)
Extraordinary impairment of capital assets	-	(1,292,068)
Increase (decrease) in net assets	(2,667)	5,660,524
Net assets, July 1	359,588,272	353,927,748
Net assets, June 30	\$ 359,585,605	\$ 359,588,272

Management's Discussion and Analysis (Unaudited)

The condensed two-year comparison of Revenues, Expenses and Changes in Net Assets, combined with the following discussion provides insight as to the causes affecting net assets.

- **Operating Revenues:** The Authority is not empowered to levy or collect taxes. The Authority did receive a contribution of \$1.9 million from New Hanover County in fiscal year 2011. This contribution will continue at the \$1.9 million level through fiscal year 2013 and then gradually reduce over the next five years with a final contribution of \$.3 million in fiscal year 2018. Except for this contribution, which accounted for 3% of total revenues in fiscal year 2011, the Authority's operations, capital expansion program, and debt service are funded almost entirely from fees charged to our customers. As such, the Authority's revenue stream is impacted by fluctuations in demand for our services and other economic factors.
- **Charges for services:** Charges for services revenue increased by \$9.6 million from the prior fiscal as a result of rate changes implemented in May 2010 and May 2011, as well as an increase in demand for services. The May 2011 and May 2010 rate changes increased both fixed and volumetric charges by 13% and 14%, respectfully.
- **Increased demand:** Overall water volumes consumed increased by 5.3% from the prior year. Residential demand, which constituted 70.9% of water demand in the prior year increased 6.4% while non-residential demand was up 2.7%. Billed volumes for sewer service increased by 5.5% from fiscal year 2010. Residential sewer volumes were up 5.0% from the prior fiscal year while non-residential increased 6.6%
- **Operating expenses:** Operating expenses, mainly depreciation and amortization increased less than 1% from the prior year. Increases in operations, environmental compliance, safety, and non-departmental expenses were mostly offset by decreases in administration and customer service expenses.
- **Other revenues:** Investment earnings decreased from \$4.1 million to \$.7 million as yields declined and bond proceeds were drawn down for capital project expenditures. Capital contributions from developers declined from \$8.0 million to \$2.8 million. Cash contributions included in this category in the form of impact fees were \$2.0 million in fiscal year 2011, down from \$2.3 million collected in 2010.

Management's Discussion and Analysis (Unaudited)

Capital Assets and Debt Administration

Capital Assets. The Authority's investment in capital assets totals \$559.7 million (net of accumulated depreciation and amortization) at June 30, 2011. Table C presents the Changes in Net Capital Assets for the year ended June 30, 2011. The major assets include water plants, wastewater treatment plants, pump stations, water distribution systems, and the wastewater collection system.

Cape Fear Public Utility Authority's Capital Assets Net of Depreciation and Amortization

Table C

	Beginning Balances July 1, 2010	Increases	Retirements	Transfers	Ending Balances June 30, 2011
Capital assets not being depreciated:					
Land	\$ 7,182,245	\$ -	\$ -	\$ -	\$ 7,182,245
Intangible Asset-Easements	1,096,042	140,188	-	60,060	1,296,290
Construction in progress	59,740,035	46,705,119	-	(17,314,497)	89,130,657
Total capital assets not being depreciated or amortized	68,018,322	46,845,307	-	(17,254,437)	97,609,192
Capital assets being depreciated or amortized:					
Plant, Structures and Improvements	202,581,231	61,103	(8,256,366)	242,552	194,628,520
Water and Sewer Lines	280,367,777	432,603	-	14,306,876	295,107,256
Furniture, Fixtures and Machinery	6,186,396	681,368	(1,488)	302,753	7,169,029
Intangible Asset-Computer Software	511,675	-	-	2,402,256	2,913,931
Intangible Asset-Water Availability Rights	1,988,116	-	-	-	1,988,116
Total capital assets being depreciated or amortized	491,635,195	1,175,074	(8,257,854)	17,254,437	501,806,852
Less:					
Accumulated depreciation	(25,098,657)	(13,839,693)	66,463	-	(38,871,887)
Accumulated amortization	(400,827)	(443,708)	-	-	(844,535)
Net depreciable assets	(25,499,484)	(14,283,401)	66,463	-	(39,716,422)
Total capital assets, net	<u>\$ 534,154,033</u>				<u>\$ 559,699,622</u>

Management's Discussion and Analysis (Unaudited)

Major capital asset events during the current fiscal year included the following:

- Construction in progress increased by \$29.4 million with \$18.2 million related to the Sweeney water treatment plant expansion and \$3.4 million related to Southside wastewater treatment plant rehab & upgrade design.
- Projects completed during the year included the \$5.6 million phase 1 NEI rehab project, including pump stations 34 & 35; the \$5.6 million Ogden Interceptor replacement, the \$2.2 million phase 1 of an asset management system, and the \$1.7 million street repaving phase of the Middle Sound sewer project.
- Retirements of \$8.2 million were related to the impairment of two capital assets. Outdated portions of the Sweeney water treatment plant were demolished as part of the expansion project. As a result, the carrying value was reduced by \$7.5 million. Also, certain existing facilities at the Northside Wastewater Treatment Plant are not being fully utilized with the upgrade in the treatment process and were reduced in carrying value by \$.7 million as a result.

Additional information on the Authority's capital assets can be found in Note 4 on page 35 of this report.

Debt Administration The Authority's long term debt, presented in Table D below, totaled \$307.7 million at June 30, 2011, net of applicable premiums, discounts and deferred refunding charges. \$.3 million of a \$1.5 million loan from the State of North Carolina has been drawn as of June 30, 2011. The Authority's overall debt coverage for fiscal year 2011 was 1.65 for fiscal year 2011, remaining above the 1.0 ratio required by bond covenants. Coverage on revenue bond debt was 2.80, remaining above the 1.2 ratio required by revenue bond covenants.

Cape Fear Public Utility Authority's Outstanding Long-Term Debt

Table D

	2011	2010
Revenue Bonds	\$ 255,556,814	\$ 259,225,928
General Obligation Bonds:		
Locality compensation payment	11,712,630	16,371,000
Installment Obligations:		
Locality compensation payment	39,918,647	42,475,207
ARRA revolving loan	330,545	-
Capitalized Leases	179,315	413,381
Totals	<u>\$ 307,697,951</u>	<u>\$ 318,485,516</u>

The Authority assumed the long term obligations of the City of Wilmington and New Hanover County on July 1, 2008 for water and sewer related debt. At that time, the total debt assumed was \$184.6 million with \$67.2 million of that amount in outstanding revenue bonds.

The Authority issued \$187,765,000 in revenue bonds in August 2008 to pay for water and sewer capital improvements and to refund \$42 million in New Hanover County Certificates of Participation that the Authority had assumed on July 1, 2008. The capital improvements funded by this debt issuance included the Sweeney plant expansion, NANO water treatment facility, and improvements to the Northeast Interceptor sewer force main. The City and County had either started construction or were in final design on these projects when the Authority began operations on July 1, 2008.

Management's Discussion and Analysis (Unaudited)

Subsequent to year-end, the Authority issued \$44.1 million of revenue bonds on September 28, 2011, primarily to fund replacement and rehabilitation of wastewater and water lines, construction and installation of new water and wastewater lines, pump station and force main improvements, and programs expected to be required by the Environmental Protection Agency.

Additional information on the Authority's long term debt can be found in Note 8, Long-Term Obligations beginning on page 40 and Note 13, Subsequent Event on page 48 of this report.

Budget Highlights for the Fiscal Year Ending June 30, 2011

The Authority's adopted FY 2012 budget for operations is \$37.0 million as compared to \$37.6 million in FY 2011.

Revenues are projected to increase to \$68.4 million in FY 2012 from \$58.6 million in the adopted FY 2011 budget. Water and wastewater rates were increased in May 2011 to produce 13.1% additional revenues from charges for services. The rate increase was primarily required to fund increased debt service. Debt service increases in FY 2012 since this is the first year that revenues with no capitalized interest will be needed to pay principal and interest on the 2008 revenue bonds. FY 2012 net debt service is \$25.5 million compared to \$19.8 million in FY 2011.

The Authority will continue to closely monitor revenues and consumption patterns in FY 2012 and will make adjustments to expenditure levels as needed.

Requests for Information

This report is designed to provide an overview of the Authority's finances for those with an interest in this area. Questions concerning any of the information found in this report or requests for additional information should be addressed to the Cape Fear Public Utility Authority, Finance Department, 235 Government Center Drive, Wilmington, NC 28403.

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Cape Fear Public Utility Authority

Statement of Net Assets

June 30, 2011

ASSETS

Current assets	
Cash and cash equivalents	\$ 71,071,980
Receivables, net	16,241,308
Due from other governments	3,108,270
Restricted cash and cash equivalents	8,568,406
Restricted receivables	256,022
Prepays	49,101
Inventories	1,420,237
Deferred outflow of resources	833,249
Total current assets	101,548,573
Noncurrent assets	
Restricted cash and cash equivalents	13,512,461
Restricted investments	13,456,190
Unamortized bond issuance costs	3,954,414
Capital assets:	
Land, easements and construction in progress	97,609,192
Other capital assets, net	462,090,430
Total capital assets	559,699,622
Total noncurrent assets	590,622,687
Total assets	692,171,260

LIABILITIES

Current liabilities	
Current maturities of long-term obligations	13,974,566
Accrued interest payable	4,503,082
Customer and escrow deposits	767,859
Due to other governments	3,694,900
Accounts payable and accrued liabilities	3,211,094
Compensated absences	696,062
Unearned revenue	47,867
Accounts payable from restricted assets	8,568,406
Derivative instrument - interest rate swap	833,249
Total current liabilities	36,297,085
Noncurrent Liabilities	
Compensated absences	361,083
Other postemployment benefits (OPEB)	2,204,102
Long-term obligations, net of current maturities	293,723,385
Total noncurrent liabilities	296,288,570
Total liabilities	332,585,655

NET ASSETS

Invested in capital assets, net of related debt	287,538,728
Unrestricted	72,046,877
Total net assets	\$ 359,585,605

See Notes to Financial Statements.

Cape Fear Public Utility Authority

**Statement of Revenues, Expenses and Changes in Net Assets
For the Year Ended June 30, 2011**

Operating revenues	
Charges for services	\$ 57,086,229
Other operating revenues	2,671,784
Total operating revenues	<u>59,758,013</u>
Operating expenses	
Personnel and benefits	15,176,175
Services and utilities	10,689,144
Materials	3,630,676
Depreciation and amortization	14,283,401
Total operating expenses	<u>43,779,396</u>
Operating income	<u>15,978,617</u>
Nonoperating revenues (expenses)	
Investment earnings	738,453
Interest expense	(13,011,609)
Amortization	(230,087)
Contributions from New Hanover County	1,900,000
Total nonoperating (expenses)	<u>(10,603,243)</u>
Income before capital contributions and special item	<u>5,375,374</u>
Capital contributions	
Capital contributions	2,813,350
Special impairment of capital assets	(8,191,391)
Total capital contributions and special item	<u>(5,378,041)</u>
Decrease in net assets	<u>(2,667)</u>
Net assets	
Beginning of year	359,588,272
End of year	<u><u>\$ 359,585,605</u></u>

See Notes to Financial Statements.

Cape Fear Public Utility Authority

Statement of Cash Flows
For the Year Ended June 30, 2011

Cash Flows From Operating Activities

Cash received from customers	\$ 56,118,088
Cash paid to suppliers	(13,739,597)
Cash paid to or on behalf of employees	(15,025,005)
Other operating income	2,670,181
Net cash provided by operating activities	30,023,667

Cash Flows From Capital and Related Financing Activities

Acquisition and construction of capital assets	(44,344,318)
Principal paid on long-term obligations	(9,147,645)
Proceeds from long-term obligations	
Principal	330,545
Interest paid on long-term obligations	(14,663,063)
Capital contributions	2,216,391
Net cash used for capital and related financing activities	(65,608,090)

Cash Flows From Investing Activities

Investment earnings	296,389
Net cash provided by investing activities	296,389
Net decrease in cash and cash equivalents	(35,288,034)

Cash and cash equivalents, beginning of year	128,440,881
Cash and cash equivalents, end of year	\$ 93,152,847

Reconciliation to statement of net assets:

Cash and cash equivalents	\$ 71,071,980
Restricted cash and cash equivalents (current and noncurrent)	22,080,867
Total cash, cash equivalents and investments	\$ 93,152,847

(Continued)

Cape Fear Public Utility Authority

**Statement of Cash Flows (Continued)
For the Year Ended June 30, 2011**

Reconciliation of Operating Income to Net Cash

Provided by Operating Activities

Operating income	\$ 15,978,617
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Adjustments to reconcile operating income to net cash

provided by operating activities:

Depreciation and amortization	14,283,401
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Changes in assets and liabilities:

(Increase) in receivables and due from other governments	(1,170,163)
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Decrease in inventories	42,648
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(Increase) in prepaids	(3,903)
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Increase in accounts payable and accrued liabilities	533,207
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Increase in customer and escrow deposits	208,690
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Increase in compensated absences and OPEB	151,170
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Total adjustments	14,045,050
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Net cash provided by operating activities	\$ 30,023,667
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Supplemental Schedule of Noncash Activities

Contributions of capital assets from developers	\$ 572,791
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Debt payment reduction from New Hanover County	\$ 1,900,000
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See Notes to Financial Statements.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies

The accounting policies and financial statements of the Cape Fear Public Utility Authority ("Authority") have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to governmental units. The Governmental Accounting Standards Board ("GASB") is the accepted standard-setting body for establishing accounting and financial reporting principles. The more significant of the Authority's accounting policies are described below.

Reporting Entity:

Cape Fear Public Utility Authority was created in 2007 pursuant to Chapter 162A of the North Carolina General Statutes, by the governing bodies of New Hanover County (County) and the City of Wilmington (City), for the purpose of providing water and sewer services to residents of New Hanover County. The assets and related liabilities of the City of Wilmington and New Hanover County water and sewer systems were transferred to the Authority on July 1, 2008. The Authority is empowered to set rates, fees and charges without oversight, supervision, or direction from any other state or local entity or agency, but has no taxing authority. The Governing Board consists of eleven directors who hold office for staggered terms. The directors are appointed by the governing bodies of New Hanover County and the City of Wilmington. Each of the governing bodies appoints five members and they jointly appoint the eleventh member. The five appointed members from each governing body include two current members from those governing bodies.

Accounting principles generally accepted in the United States require that the reporting entity include (1) the primary government, (2) organizations for which the primary government is financially accountable and (3) other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. The criteria provided in Government Accounting Standards Board Codification Section 2100 have been considered and the Authority has identified two blended component units, described below, which are in substance part of the Authority's operations, and so data from these units is combined with data of the Authority. Also, the Authority is not included in any other reporting entity. The Authority is a jointly governed organization, i.e. an entity governed primarily by representatives from other governments. The participants do not retain any ongoing financial interest in or financial responsibility for the Authority.

Blended Component Units:

Cape Fear Utilities, Inc. and Quality Water Supplies, Inc., North Carolina nonprofit corporations, exist to provide and maintain a ground water utility system for citizens of Wilmington, North Carolina and the surrounding community. The Authority is the sole shareholder of each corporation and each of the corporations is governed by a board comprised of members of the Authority Board. The corporations have no other operations except for services provided to the Authority and are exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. The rates for user charges and the annual budget of the ground water utility system are approved by the Authority Board. Therefore the operations of these corporations are combined and reported as a part of the Authority's operations. The corporations do not issue separate financial statements.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Basis of Presentation:

All activities of the Authority and its blended component units are accounted for within a single business-type activity and within a single proprietary (enterprise) fund. Enterprise Funds are used to account for operations that are financed and operated in a manner similar to private business enterprises where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges. An Enterprise Fund is required to be used when an activity is financed with debt that is secured solely by pledges of the net revenues from fees and charges of the activity.

Measurement Focus and Basis of Accounting:

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. Concurrent with the commencement of providing water/sewer services on July 1, 2008, the Authority elected to be treated as a "special-purpose government engaged only in business-type activities" as described in accounting principles generally accepted in the United States of America. Enterprise activities are accounted for on the flow of economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenue is recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Non-exchange transactions, in which the Authority gives (or receives) value without directly receiving (or giving) equal value in exchange, include grants and donations. Revenue from grants and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

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 Authority's funds are charges to customers for sales and services. The Authority also recognizes as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the water and sewer system. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

As permitted by accounting principles generally accepted in the United States, the Authority has elected to apply only applicable Financial Accounting Standards Board ("FASB") statements and interpretations issued before November 30, 1989 in its accounting and reporting practices, to the extent that those standards do not conflict with or contradict guidance of the GASB.

Budgets

Budgets are adopted utilizing the modified accrual basis of accounting as required by State statute. An annual budget ordinance is adopted for the operating sub-funds. All annual appropriations lapse at fiscal year end. Project ordinances are adopted for capital projects sub-funds, which are consolidated with the operating funds for reporting purposes.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Expenditures may not legally exceed appropriations at the functional level for the operating sub-fund and at the project level for the capital projects sub-funds. The budget may be amended as necessary by the governing board. A budget calendar is included in the North Carolina General Statutes which prescribes the last day on which certain steps of the budget procedure are to be performed. The following schedule lists the tasks to be performed and the date by which each is required to be completed.

April 30	Each department head will transmit to the budget officer the budget requests as estimates for their department for the budget year.
June 1	The budget and the budget message shall be submitted to the governing board. The public hearing on the budget should be scheduled at this time.
July 1	The budget ordinance shall be adopted by the governing board.

Assets, Liabilities, and Net Assets

Deposits and Investments

All deposits of the Authority are made in board-designated official depositories and are collateralized as required by State law (G.S. 159-31). The Authority may designate, as an official depository, any bank or savings and loan association whose principal office is located in North Carolina. Also, the Authority may establish time deposit accounts such as NOW and SuperNOW accounts, money market accounts and certificates of deposit.

State law [G.S. 159-30(c)] authorizes the Authority to invest in obligations of the United States or obligations fully guaranteed both as to principal and interest by the United States; obligations of the State of North Carolina; bonds and notes of any North Carolina local government or public authority; obligations of certain non-guaranteed federal agencies; certain high quality issues of commercial paper and bankers' acceptances; and the North Carolina Capital Management Trust ("NCCMT"), an SEC registered (2a-7) money market mutual fund. The securities of the NCCMT cash portfolio are valued at fair value, which is the NCCMT's share price.

Cash and Cash Equivalents

The Authority pools moneys from several sub-funds to facilitate disbursement and investment and to maximize investment earnings. The Authority considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash and cash equivalents.

Restricted Assets

The unexpended bond proceeds of revenue bonds, certificates of participation and other long-term obligations issued by the Authority are classified as restricted assets under Restricted cash, cash equivalents and investments because their use is restricted to the purpose for which the bonds were originally issued.

Allowance for Doubtful Accounts

All receivables that historically experience uncollectible accounts are shown net of an allowance for doubtful accounts. This amount is estimated by analyzing the aging of account balances.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Inventories

Inventories consist of materials and supplies maintained for major items used by the Authority. Inventories are valued at cost (first-in, first-out method), which approximates market. Inventories are recorded as an asset and materials and supplies are not recorded as an expense until consumed.

Capital Assets

Capital assets are defined by the Authority as assets with an initial, individual cost of more than \$5,000 and estimated useful life in excess of one year. Purchased capital assets are valued at original cost at the time of acquisition. The cost of normal repairs and maintenance which do not add to the value of the asset or materially extend assets' lives are not capitalized. Donated capital assets are recorded at their estimated fair value at the time of donation.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets is included as part of the capitalized value of the assets constructed. The construction interest capitalized during the year ended June 30, 2011 totaled \$1,961,676.

Capital assets, which include buildings, plant, furniture, fixtures, equipment and infrastructure assets, are depreciated using the straight-line method by groups or classes of property over the following expected service lives:

	Years
Plant, Structures and Improvements	20-40
Water and Sewer Lines	50
Furniture, Fixtures and Machinery	5

The Authority may consider capital assets impaired if both: (a) the decline in service utility of the capital asset is large in magnitude and (b) the event or change in circumstances is outside the normal life cycle of the capital asset. Impaired assets will be appropriately reduced in value or discarded if idle.

During the year ended June 30, 2011, the Authority recorded special impairment charges of \$8,191,391 for certain assets that were removed from service when a treatment plant expansion was completed at the discretion of management.

Intangible assets consist of water availability rights, easements, and software. The water availability rights are available under an agreement the City of Wilmington entered into with a regional public authority. The agreement makes available fifteen million gallons per day of raw water. The availability rights are being amortized over forty years, the life of the agreement. Easements are recorded at fair value and are not amortized. In accordance with GASB Codification Section 1400, computer software is capitalized with a minimum capitalization cost of \$25,000 and is amortized over a period of 3 to 8 years.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates to the financial statements include the unbilled receivables, allowance for doubtful accounts, the estimated useful lives of capital assets, compensated absences, other post employment benefits, medical IBNR reserve, workers' compensation self-insurance, unamortized bond issuance costs, and the valuation of interest rate swaps.

Long-Term Obligations

Long-term debt is reported as a liability in the statement of net assets, net of applicable bond charges, premiums or discounts. Bond charges, premiums and discounts are deferred and amortized over the life of the bonds using the effective interest method. Bond issuance costs are reported as noncurrent assets and amortized over the life of the bonds using the straight-line method.

Compensated Absences

The vacation policy of the Authority provides for the accumulation of up to 320 hours earned vacation leave with such leave being fully vested when earned. Accrued vacation at year end totaled \$1,057,145 and is included as compensated absences.

The Authority has adopted a first-in first-out method of using accumulated compensated time. An expense and a liability for compensated absences and the salary related payments are recorded as the personal leave is earned. The portion of the accumulated vacation pay which is expected to be liquidated during the next fiscal year is recorded as a current liability on the statement of net assets.

The Authority's sick leave policy provides for an unlimited accumulation of earned sick leave. Sick leave does not vest, but any unused sick leave accumulated at the time of retirement may be used in the determination of length of service for retirement benefit purposes. Since the Authority does not have any obligation for the accumulated sick leave until it is actually taken, no accrual for sick leave has been made.

Medical Self-Insurance

The Authority is self-insured for group medical insurance and has contracted with Blue Cross and Blue Shield of North Carolina to administer the program. The Authority's program provides for individual stop-loss coverage for claims above a specific amount. The individual stop-loss insurance provides reimbursement to the group plan of all eligible claims paid above \$85,000 on behalf of any participant during the contract period. The stop-loss insurance policy is underwritten by Blue Cross and Blue Shield of North Carolina. A provision of \$437,091 for estimated claims incurred but not reported as of June 30, 2011 has been accrued.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Workers' Compensation Self-Insurance

The Authority is self-insured for workers' compensation and employers' liability insurance, and purchases Specific and Aggregate Excess Workers Compensation and Employers Liability Indemnity insurance. The Authority contracted with PMA, Inc., a provider of claims administrative services, to administer the program. The program provides that the Authority is responsible for the first \$400,000 of cost and/or benefits payable to employees resulting from any one accident or event, regardless of the number of persons injured.

Specific and Aggregate Excess Workers Compensation and Employers Liability Indemnity insurance provides protection against compensable claims during the policy year above the self insured specific retention of \$400,000, up to the maximum limits provided under the North Carolina Workers' Compensation Act and up to \$1,000,000 each accident or disease for Employer's Liability. In addition, the insurance would provide protection against cumulative retained losses after the Authority's aggregate costs reach a minimum of \$1,077,213 for claims occurring during the policy period and would then provide an additional \$1,000,000 of coverage, with any losses beyond the \$1,000,000 limit being retained by the Authority.

A provision of \$115,000 for estimated claims incurred as of June 30, 2011 has been accrued.

Net Assets

Net assets are classified as invested in capital assets, net of related debt, restricted, or unrestricted. Invested in capital assets, net of related debt represents the amounts invested in capital asset less any outstanding debt used in the acquisition of those assets. Restricted net assets represent constraints on resources that are either externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or imposed by law through state statute. Unrestricted net assets consist of net assets that do not meet the definition of "invested in capital assets" or "restricted". Unrestricted net assets of \$4,257,434 is designated for post-employment benefits and represents the amount that has been designated by the governing board to fund a trust to be established for future costs of post-employment benefits.

Special Item

During the year ended June 30, 2011, the Authority recorded a special impairment of \$8.2 million for the impairment of two capital assets. Outdated portions of the Sweeney water treatment plant were demolished as part of the expansion project. As a result, the carrying value was reduced by \$7.5 million. Also, certain existing facilities at the Northside Wastewater Treatment Plant are not being fully utilized with the upgrade in the treatment process and were reduced in carrying value by \$.7 million as a result.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 2. Cash, Cash Equivalents, Deposits and Investments

Deposits

Custodial credit risk for deposits is the risk that in the event of bank failure, a government's deposit may not be returned to it. The Authority has no policy on custodial credit risk, but all of the Authority's deposits are to be either insured or collateralized by using one of two methods. Under the Dedicated Method, all deposits that exceed the federal depository insurance coverage level are separately collateralized with securities held by the governments' agents in the governments' names. Under the Pooling Method, which is a statewide collateral pool, all uninsured deposits are collateralized with securities held by the State Treasurer's agent in the name of the State Treasurer. Since the State Treasurer is acting in a fiduciary capacity for the governments, these deposits are considered to be held by the governments' agents in their name. The amount of the pledged collateral is based on an approved averaging method for non-interest bearing deposits and the actual current balance for interest-bearing deposits. Depositories using the Pooling Method report to the State Treasurer the adequacy of their pooled collateral covering uninsured deposits. The State Treasurer does not confirm this information with the governments or the escrow agents. Because of the inability to measure the exact amounts of collateral pledged for governments under the Pooling Method, the potential exists for under-collateralization, and this risk may increase in periods of high cash flows. However, the State Treasurer of North Carolina enforces strict standards of financial stability for each depository that collateralizes public deposits under the Pooling method. The State Treasurer enforces standards of minimum capitalization for all pooling method financial institutions.

At June 30, 2011, the carrying amount of the Authority deposits was \$86,654,178 and the bank balance was \$86,814,696. Of the bank balance, \$250,000 was covered by FDIC insurance and \$86,564,696 was collateralized using the Pooling Method. Cash on hand at June 30, 2011 was \$2,200.

During the year ended June 30, 2011, it was determined that the revenue bond trustee overstated investment earnings by \$816,192 on the 2008 Revenue bonds Construction Fund account for the year ended June 30, 2010. Correction of the investment earnings has been recorded in the fiscal year ended June 30, 2011.

Investments

At June 30, 2011, the Authority had the following investments:

	Fair Value	Maturity Less Than One Year
Restricted investments - US Government Agencies	\$ 13,456,190	\$ 13,456,190
Restricted cash and cash equivalents -NC Capital Management Trust - Cash Portfolio	6,496,469	N/A
	<u>\$ 19,952,659</u>	<u>\$ 13,456,190</u>

Interest Rate Risk

As a means of limiting its exposure to fair value losses arising from rising interest rates, the Authority's investment policy limits the weighted average maturity of the investment portfolio to no more than one year. Also, the investment policy requires purchases of securities to have staggered maturities and limits all securities to a final maturity of no more than five years.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 2. Cash, Cash Equivalents, Deposits and Investments (Continued)

Credit Risk and Concentration of Credit Risk

The Authority has no formal policy on managing credit risk. The Authority's investment policy limits investments to the provisions of North Carolina G.S. 159-30(c) and requires the investment security types to be no more than 25% of the total portfolio in a single security type. As of June 30, 2011 the Authority's investments in the NCCMT Cash Portfolio carried a credit rating of AAAm by Standard & Poor's.

The Authority's investments in U.S. Government Agencies (Federal National Mortgage Association) are rated AA+ by Standard & Poor's and Aaa by Moody's Investor's Service.

Custodial Credit Risk

The Authority has no policy on custodial credit risk. However, the Authority contracts with the trust department of a financial institution, as escrow agent to hold its investments in the Authority's name.

The Authority has no policy on foreign currency risk.

Note 3. Receivables

The Authority estimates the revenue value of water consumed by its customers at year end but not billed by the last day of the fiscal year. This is done by multiplying the estimated unbilled water usage by the approximate number of days unbilled at June 30. As of June 30, 2011, the Authority had approximately \$7,122,393 of unbilled receivables included in Accounts receivable – customers, below.

The amounts presented in the Statement of Net Assets are as follows:

Accounts receivable - customers	\$ 19,145,696
Allowance for doubtful accounts	(2,904,388)
Total receivables, net of allowance	<u>\$ 16,241,308</u>

The amounts due from other governments consist of the following:

Refund of sales and use tax paid	\$ 1,432,469
New Hanover County	1,000,000
Other grants and reimbursements	675,801
Total due from other governments	<u>\$ 3,108,270</u>

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 4. Capital Assets

Capital assets activity consists of the following for the year ended June 30, 2011. Current depreciation and amortization expense was \$13,839,693 and \$443,708, respectively.

	Beginning Balances July 1, 2010	Increases	Decreases	Transfers	Beginning Balances June 30, 2011
Capital assets not being depreciated:					
Land	\$ 7,182,245	\$ -	\$ -	\$ -	\$ 7,182,245
Intangible Asset-Easements	1,096,042	140,188	-	60,060	1,296,290
Construction in progress	59,740,035	46,705,119	-	(17,314,497)	89,130,657
Total capital assets not being depreciated or amortized	68,018,322	46,845,307	-	(17,254,437)	97,609,192
Capital assets being depreciated or amortized:					
Plant, Structures and Improvements	202,581,231	61,103	(8,256,366)	242,552	194,628,520
Water and Sewer Lines	280,367,777	432,603	-	14,306,876	295,107,256
Furniture, Fixtures and Machinery	6,186,396	681,368	(1,488)	302,753	7,169,029
Intangible Asset-Computer Software	511,675	-	-	2,402,256	2,913,931
Intangible Asset-Water Availability Rights	1,988,116	-	-	-	1,988,116
Total capital assets being depreciated or amortized	491,635,195	1,175,074	(8,257,854)	17,254,437	501,806,852
Less accumulated depreciation or amortization for:					
Plant, Structures and Improvements	7,234,787	5,437,699	(64,975)	-	12,607,511
Water and Sewer Lines	15,660,063	7,100,931	-	-	22,760,994
Furniture, Fixtures and Machinery	2,203,807	1,301,063	(1,488)	-	3,503,382
Intangible Asset-Computer Software	227,947	357,268	-	-	585,215
Intangible Asset-Water Availability Rights	172,880	86,440	-	-	259,320
Total accumulated depreciation and amortization	25,499,484	14,283,401	(66,463)	-	39,716,422
Total capital assets being depreciated or amortized, net	466,135,711				462,090,430
Capital assets, net	\$ 534,154,033				\$ 559,699,622

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 5. Operating Leases

The Authority leases building, office facilities and land under two operating lease arrangements. A lease for the Administration Building commenced on June 1, 2008 and covers a period of 120 months, with the option to extend the lease for two additional five year periods. A new lease for the Operations Center commences August 1, 2011 and covers a period of 60 months, with the option to extend the lease for one additional two year period. Total lease costs of \$849,585 for the year ended June 30, 2011, included the Administration Building and a separate lease for the Operations Center at a different location that ended August 31, 2011. The future minimum lease payments as of June 30, 2011 are as follows:

Year Ending June 30	Amount
2012	\$ 783,701
2013	819,296
2014	843,875
2015	869,191
2016	895,267
Thereafter	1,478,577
Total	<u>\$ 5,689,907</u>

Note 6. Benefit Plan Obligations

Local Governmental Employees' Retirement System

Plan description: The Authority contributes to the statewide Local Governmental Employees' Retirement System ("LGERS"), a cost sharing multiple-employer defined benefit pension plan administered by the State of North Carolina. LGERS provides retirement and disability benefits to plan members and beneficiaries. Article 3 of G.S. Chapter 128 assigns the Authority to establish and amend benefit provisions to the North Carolina General Assembly. The Local Governmental Employees' Retirement System is included in the Comprehensive Annual Financial Report ("CAFR") for the State of North Carolina. The State's CAFR includes financial statements and required supplementary information for LGERS. That report may be obtained by writing to the Office of the State Controller, 1410 Mail Center Service, Raleigh, North Carolina 27699 - 1410, or by calling (919) 981-5454.

Funding policy: Plan members are required to contribute 6% of their annual covered salary. The Authority is required to contribute at an actuarially determined rate. For the Authority, the current rate is 6.35% of annual covered payroll. The contribution requirements of members and the Authority are established and may be amended by the North Carolina General Assembly. The Authority's contributions to LGERS for the years ended June 30, 2011, 2010 and 2009 were \$799,850, \$630,628 and \$627,104, respectively. The contributions made by the Authority equaled the required contributions for the year.

Supplemental Retirement Income Plan and Deferred Compensation Plan

Plan Descriptions. The Authority offers its employees to participate in the Supplemental Retirement Income Plan, a defined contribution pension plan administered by the Department of State Treasurer and a Board of Trustees. The plan provides retirement benefits to employees of the Authority. Article 5 of G.S. Chapter 135 assigns the authority to establish and amend benefit provisions to the North Carolina General Assembly.

The Authority also offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all Authority employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency. All assets of the plan are held in trust for the exclusive benefit of the participants and their beneficiaries.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 6. Benefit Plan Obligations (Continued)

Funding Policy. The Authority has elected to make contributions on behalf of all employees to the Supplemental Retirement Income Plan or the 457 Deferred Compensation Plan. The Authority's contribution is 2% of covered payroll and contributions are made to the plan selected by the employee. The Authority also matches the contributions made by employees up to 2% of covered payroll. If the employee does not elect either plan, the Authority's contribution is placed into the Supplemental Retirement Income Plan on behalf of the employee.

Employer contributions to the Supplemental Retirement Income Plan totaled \$342,269 and employee contributions and loan repayments were \$352,010 for the year ended June 30, 2011.

Employer contributions to the 457 Deferred Compensation Plan totaled \$128,298 and employee contributions and loan repayments were \$147,039 for the year ended June 30, 2011.

Other Post-employment Benefits

Plan Description. According to the Authority's personnel policy, the Authority provides post-employment health care benefits to retirees of the Authority as a single-employer defined benefit plan, provided they participate in the North Carolina Local Government Employees' Retirement System and were employed by the City or County prior to July 1, 2008 as the years of service were transferred from participating member governments during the initial transition phase of the Authority. Employees transferred from the City of Wilmington must have at least five years of creditable service. Employees transferred from New Hanover County must have at least fifteen years of creditable service. The Authority shares the cost of coverage for these benefits through private insurers with the retiree by paying claims under its medical self-insurance program and charging participants a co-payment amount. Also, the Authority's retirees can purchase coverage for their dependents at the Authority's group rates. A separate report was not issued for the plan.

Membership consisted of 234 active plan members and 2 retirees receiving benefits at December 31, 2010, the date of the latest actuarial valuation.

Funding Policy. The Authority's contribution towards the plan is based on a set amount or percentage of the cost of the individual insurance coverage. The Authority is not required to fully fund the annual required contribution (ARC); however, the Authority is required to disclose the unfunded ARC, which must be amortized over future periods. To date, the Authority has chosen to fund these benefits on a pay-as-you-go basis.

The current ARC is 1.22% of annual covered payroll. Contributions of \$7,491 (.06% of annual covered payroll) were made by the Authority for the current year. There were no contributions made by employees of the Authority.

Summary of Significant Accounting Policies. Postemployment benefits are paid as they come due from the Authority's operating fund. Assets have been accumulated for OPEB purposes but have not yet been placed in an irrevocable trust fund.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 6. Benefit Plan Obligations (Continued)

Annual OPEB Cost and Net OPEB Obligation. The Authority's annual OPEB cost 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 Authority's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the Authority's net OPEB obligation for the healthcare benefits:

Annual required contribution (ARC)	\$ 157,186
Interest on net OPEB obligation	83,479
Adjustment to annual required contribution	(116,048)
Annual OPEB cost	124,617
Contributions made	(7,491)
Increase in net OPEB obligation	117,126
Net OPEB obligation, beginning of year	2,086,976
Net OPEB obligation, end of year	\$ 2,204,102

The Authority's trend information for the annual OPEB cost, the percentage of annual OPEB cost contributed, and the net OPEB obligation is as follows:

For The Year Ended June 30	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2011	\$ 124,617	6.011%	\$ 2,204,102
2010	1,043,781	0.056%	2,086,976
2009	1,043,781	0.000%	1,043,781

Funded Status and Funding Progress. As of December 31, 2010, the most recent actuarial valuation date, the plan was not funded. The actuarial accrued liability for benefits and, thus, the unfunded actuarial accrued liability (UAAL) was \$2,351,870. The covered payroll (annual payroll of active employees covered by the plan) was \$12,895,415, and the ratio of the UAAL to the covered payroll was 18.2%.

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 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. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents information about the actuarial value of plan assets and the actuarial accrued liabilities for benefits.

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

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 6. Benefit Plan Obligations (Continued)

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.

In the December 31, 2010 actuarial valuation, the entry age normal actuarial cost method was used. The actuarial assumptions included a 4.0% discount rate, salary increases of 2.5%, medical trend rates between 9.0% and 4.5%, and a 2.50% inflation assumption. The UAAL is being amortized on a level dollar amount. The remaining amortization period at December 31, 2010 was 30 years.

Note 7. Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Authority has chosen to establish a risk financing fund for risks associated with the employee's health insurance program and workers' compensation coverage. The Authority carries commercial coverage for all other risks of loss including property and general liability coverage. Claims did not exceed coverage for any category for the fiscal years ended June 30, 2011, 2010 or 2009.

The Authority also carries flood insurance coverage for its facilities with a blanket limit of \$1,000,000 and a deductible of \$100,000 on properties not located within a 100-year flood plain.

The Authority's Chief Financial Officer is individually bonded for \$250,000. The remaining employees that have access to funds are bonded under a blanket bond for \$1,000,000.

Liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported (IBNR). Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends including the frequency and amount of payouts.

Claims liabilities are reported as Accounts payable and accrued liabilities. Changes in claims liability for the years ended June 30, 2011 and 2010 are as follows:

	2011	2010
Medical Self-Insurance Program		
Unpaid claims, beginning of year	\$ 343,533	\$ 202,884
Incurred claims (including IBNR)	1,995,826	2,648,456
Claim payments (including fees)	(1,902,268)	(2,507,807)
Unpaid claims, end of year	<u>\$ 437,091</u>	<u>\$ 343,533</u>
Workers' Compensation Self-Insurance Program		
Unpaid claims, beginning of year	\$ 201,000	\$ 20,768
Incurred claims (including IBNR)	85,248	262,347
Claim payments	(171,248)	(82,115)
Unpaid claims, end of year	<u>\$ 115,000</u>	<u>\$ 201,000</u>

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 8. Long-Term Obligations

Capital Lease

The Authority has entered into an agreement to lease certain equipment. The lease agreement qualifies as a capital lease for accounting purposes and, therefore, has been recorded at the present value of the future minimum lease payments as of the date of its inception.

The agreement was executed on April 23, 2008 for the lease of computer equipment for a period of 48 months and requiring a monthly payment of \$14,236. At June 30, 2011 the Authority's leased equipment was valued at \$612,731, net of accumulated depreciation of \$446,783, for a net carrying value of \$165,948. The equipment is recorded as Furniture, Fixtures and Machinery.

The future minimum lease obligations and the net present value of these minimum lease payments as of June 30, 2011 are as follows:

Year Ending June 30,	
2012	\$ 170,832
2013	14,236
Total minimum lease payments	185,068
Less: amount representing interest	5,753
Present value of the minimum lease payments	<u>\$ 179,315</u>

Changes in Long-Term Obligations

	July 1, 2010 (1)	Additions	Retirements	(Charges) Premiums (Discounts) Unamortized	Balance June 30, 2011	Current Portion of Balance
Revenue Bonds	\$ 250,421,083	\$ -	\$ 3,329,579	\$ 8,465,310	\$ 255,556,814	\$ 6,919,113
General Obligation Bonds:						
Locality compensation payment	17,140,000	-	4,830,000	(597,370)	11,712,630	4,110,000
Installment Obligations:						
Locality compensation payment	42,564,000	-	2,654,000	8,647	39,918,647	2,712,400
ARRA Revolving Loan	-	330,545	-	-	330,545	67,909
Capital lease/installment agreement	413,381	-	234,066	-	179,315	165,144
Compensated absences	1,023,101	34,044	-	-	1,057,145	696,062
Other postemployment benefits	2,086,976	124,617	7,491	-	2,204,102	-
Totals	<u>\$ 313,648,541</u>	<u>\$ 489,206</u>	<u>\$ 11,055,136</u>	<u>\$ 7,876,587</u>	<u>\$ 310,959,198</u>	<u>\$ 14,670,628</u>

(1) Balance at July 1, 2010 is not net of unamortized charges, premiums, and discounts of \$7,947,052.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 8. Long-Term Obligations (Continued)

The payments of the Authority's outstanding long-term obligations for the future years are as follows:

Year Ending June, 30	Parity Bonded Debt		Subordinated Bonded & Installment Debt		Total	
	Principal	Interest	Principal	Interest	Principal (1)	Interest
2012	\$6,919,113	\$11,937,386	\$6,822,400	\$2,270,434	\$13,741,513	\$14,207,820
2013	7,179,182	11,674,792	5,726,000	2,014,340	12,905,182	13,689,132
2014	6,249,806	11,389,518	5,747,000	1,798,598	11,996,806	13,188,116
2015	5,476,005	11,146,632	5,275,600	1,560,818	10,751,605	12,707,450
2016	4,372,801	10,948,085	2,994,200	1,334,669	7,367,001	12,282,754
2017-2021	41,224,597	49,112,254	13,434,800	4,629,233	54,659,397	53,741,487
2022-2026	46,685,000	38,420,378	10,000,000	1,676,554	56,685,000	40,096,932
2027-2031	59,735,000	25,388,075	2,220,000	154,013	61,955,000	25,542,088
2032-2036	69,250,000	8,726,375	-	-	69,250,000	8,726,375
Total	247,091,504	\$178,743,495	52,220,000	\$15,438,659	299,311,504	\$194,182,154
Unamortized charges	(607,429)		(1,492,832)		(2,100,261)	
Unamortized premiums	9,072,739		904,109		9,976,848	
Net carrying value	\$255,556,814		\$51,631,277		\$307,188,091	

(1) Principal balances do not reflect reduction of debt payments to New Hanover County, as described in the following paragraph.

Pursuant to the inter-local agreement transferring the City's and the County's water and sewer system to the Authority, the Authority assumed responsibility for all of the related debt. However, certain debt instruments could not be transferred to the Authority or refinanced due to the nature of the agreements. Accordingly, the City and the County have retained and are servicing those obligations with the Authority making payments to the City and the County equal to the principal and interest payments required under those debt instruments. Debt service payments made to the City and County for the year ended June 30, 2010 were \$5,185,767 and \$4,831,061, respectively. Under Section 2.10 of the inter-local agreement, the County agreed to a reduction in the amount of the debt service payments made by the Authority to the County (debt payments reduction amounts) for a period of 10 years, starting with the year ended June 30, 2009. The debt payment reduction amount which reduces the debt service payments to be paid to the County by the Authority was \$1.9 million in the prior two years and the current year and will be an additional \$1.9 million each year for the next two years. Beginning in the sixth year (2014), the debt payment reduction amounts will consist of \$1.577 million for the sixth year, \$1.254 million for the seventh year, \$950,000 for the eighth year, \$627,000 for the ninth year, and \$304,000 for the tenth year. If at any time the debt payments reduction amounts in a given year are greater than the amounts required to be paid by the Authority to the County, the County will pay the Authority the difference.

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 8. Long-Term Obligations (Continued)

Details of the Authority's outstanding long-term obligations at June 30, 2011 are as follows:

Revenue Bonds

\$6,508,316 Refunding Water and Sewer Revenue Bonds, Series 2003 issued to refund Water and Sewer Revenue bonds, the proceeds of which were used for water and sewer system improvements; principal installments due semiannually on June 1 and December 1 in varying amounts from \$202,707 to \$261,107 plus interest through December 1, 2018; interest at a fixed rate of 3.65% .

\$ 3,461,504

\$62,400,000 Water and Sewer Revenue and Refunding Revenue Bonds, Series 2005 issued for a wastewater plant expansion, other water and sewer system improvements and to refund \$9,235,000 of Water and Sewer Revenue Bonds, the proceeds of which were used for like improvements; principal installments due annually on June 1 in varying amounts of \$1,725,000 to \$2,875,000 plus interest through June 1, 2034; interest at fixed rates from 3.75% to 5.0% .

56,785,000

\$187,765,000 Water and Sewer Revenue bonds, Series 2008 issued for water and sewer improvements and to refund \$42 million of New Hanover County Certificates of Participation; principal payments due annually on August 1 in varying amounts of \$1,410,000 to \$13,125,000 plus interest through August 1, 2035; interest at rates ranging from 3.5% to 5.0% .

186,845,000

Total Revenue Bonds

247,091,504

General Obligation Bonds

Locality compensation payment payable to City of Wilmington due in annual principal payments on June 1 in varying amounts from \$2,355,000 to \$2,985,000 through June 1, 2015; variable rate semiannual interest payments due June 1 and December 1 .

11,185,000

Locality compensation payment payable to New Hanover County due in one remaining annual principal payment of \$1,125,000 on June 1, 2012; semiannual interest payments due June 1 and December 1 at 3% .

1,125,000

Total General Obligation Bonds

12,310,000

Installment Obligations

Locality compensation payable to City of Wilmington due in annual principal payments on June 1 ranging from \$925,000 to \$1,550,000 through June 1, 2024; semiannual interest payments due June 1 and December 1 at rates ranging from 4.0% to 5.0% .

15,415,000

Locality compensation payable to New Hanover County due in annual principal payments on February 23 ranging from \$1,110,000 to \$1,115,000 through February 23, 2028; semi-annual interest payments due August 26 and February 23 at rates ranging from 3.25% to 5.0% .

18,905,000

Locality compensation payable to New Hanover County due in annual principal payments on August 26 ranging from \$712,400 to \$891,800 through August 26, 2017; semiannual interest payments due August 26 and February 23 at rates ranging from 3.5% to 4.0% .

5,590,000

Total Installment Obligations

39,910,000

Total Long-Term Obligations

299,311,504

Plus Unamortized Charges, Premiums and Discounts

7,876,587

Net Carrying Value of Long-Term Obligations

\$ 307,188,091

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 8. Long-Term Obligations (Continued)

Unexpended proceeds from the issuance of revenue bonds and certificates of participation are currently held by an escrow agent in the name of the Authority. The proceeds held in the escrow account have been classified as restricted assets because their use is restricted to the purpose for which they were originally issued. The unexpended proceeds will be used for various water and sewer improvement capital projects.

Certain covenants are contained in the revenue bond orders, among the most restrictive of which provides that the Authority maintain a long-term debt service coverage ratio, as defined, of not less than 1.20. The Authority was in compliance with the covenants during the fiscal year ended June 30, 2011.

ARRA Loan

During the year ended June 30, 2010, the Authority was approved for a loan from the State of North Carolina, Department of Environment and Natural Resources (DENR). The loan will be drawn down as expenditures are paid on a certain capital project, to a maximum of \$2,716,357. Half of the loan amount is subject to immediate principal forgiveness under an American Recovery and Reinvestment Act of 2009 (ARRA) program awarded by the Environmental Protection Agency (EPA) through the State Revolving Fund program administered by DENR. The remaining \$1,358,179 will be due in twenty equal, annual installments of \$67,909, commencing on May 1 immediately following the completion of the project. The loan does not bear interest. At June 30, 2011, \$661,089 of this loan had been drawn down of which \$330,545 is recorded as an outstanding loan as of June 30, 2011.

Interest Rate Swap Agreement

The Interlocal Transition and Operating Agreement established the terms and conditions of the transfer of water and sewer assets of the City and County to the Authority on July 1, 2008. Under that Agreement, the Authority is responsible for reimbursement of payments on water and sewer-related long-term debt that could not be assumed by the Authority. Included in those long-term debt obligations retained by the City was the outstanding balance on Variable Rate General Obligation Bonds, Series 2002, for which the City entered into an interest rate swap agreement (the "swap agreement"). Based on the agreement with the City, after July 1, 2008, the Authority is responsible for payments made and received under this swap agreement. Details on the swap agreement are presented below.

Objective of the interest rate swap. As a means to lower its borrowing costs and increase its savings, when compared against fixed-rate refunding bonds at the time of issuance in February 2002; the City entered into a pay-fixed, receive variable interest rate swap in connection with its \$28,825,000 Variable Rate General Obligation Refunding Bonds, Series 2002. The intention of the swap agreement was to effectively change the interest rate on the bonds to a synthetic fixed rate of 3.815%. The swap is accounted for as a cash flow hedge and is determined to be effective using the synthetic instrument method.

Terms. The bonds and the related swap agreement mature on June 1, 2015 and the swap's June 30, 2011 notional amount of \$11,185,000 matches the face amount of the variable-rate bonds. The swap was entered into at the same time the bonds were issued (February 2002). The notional value of the swap declines with the principal amount of the associated debt. Under the swap the City (as assumed by the Authority) pays the counterparty a fixed payment of 3.815% and receives a variable payment computed at 67% of the LIBOR. Conversely, the bonds' variable-rate coupons are based on the actual float rate coupons marketed weekly.

Cape Fear Public Utility Authority

Notes to Financial Statements

8. Long-Term Obligations (Continued)

Interest Rate Swap Agreement

Fair value. Because interest rates have declined since execution of the swap, the swap has a negative fair value of \$833,249 as of June 30, 2011 which is reported on the Statement of Net Assets as a derivative liability offset by a deferred outflow of resources. The swap's negative fair value may be countered by a reduction in total interest payments required under the variable rate bonds, creating a lower synthetic interest rate. Because the coupons on the variable-rate bonds are adjusted every seven days to changing interest rates, the bonds do not have a corresponding fair value increase. The mark-to-market valuations were established by market quotations from the counterparty representing estimates of the amounts that would be paid for replacement transactions.

Credit risk. As of June 30, 2011 the Authority was not exposed to credit risk because the swap had a negative fair value. However, should interest rates change and the fair value of the swap become positive, the Authority would be exposed to credit risk in the amount of the derivative's fair value. The swap counterparty was rated A3 by Moody's Investors Service (Moody's), A by Standard and Poor's (S&P) and A+ by Fitch Ratings (Fitch). To mitigate the potential for credit risk, if the counterparty's credit quality falls to A1 by Moody's or A+ by either S&P or Fitch and their exposure exceeds \$5,000,000 the fair value of the swap will be fully collateralized by the counterparty with U.S. government securities. Collateral would be posted with a third party custodian.

Basis risk. The swap agreement exposes the Authority to basis risk should the relationship between LIBOR and the average rate paid on the floating rate coupon converge, changing the synthetic rate on the bonds. The effect of this difference in basis is indicated by the difference between the intended synthetic rates of 3.815% and the synthetic rate as of June 30, 2011 of 3.77%. As of June 30, 2011, the rate on the variable rate Bonds was .08% whereas 67% of LIBOR was .124%.

Termination risk. The City or the counterparty may terminate the swap if the other party fails to perform under the terms of the contract. An additional termination event occurs if the counterparty's credit rating falls below Baa1 (Moody's) or BBB+ (S&P and Fitch) by at least two of the rating agencies. The swap may be terminated by the City with 30 days notice and the counterparty can only terminate the swap if the City falls below BBB- with any of the three major rating services. Also, if at the time of termination the swap has a negative fair value, the Authority would be liable to the counterparty for a payment equal to the swap's fair value.

Swap payments and associated debt. Using rates as of June 30, 2011, debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same for the term of the bonds, were as follows. As rates vary, variable-rate bond interest payments and net swap payments will vary.

Fiscal Year	Interest Rate			
Ending June 30,	Principal	Interest	Swap, Net	Total
2012	\$ 2,985,000	\$ 8,948	\$ 412,805	\$ 3,406,753
2013	2,945,000	6,560	302,637	3,254,197
2014	2,900,000	4,204	193,946	3,098,150
2015	2,355,000	1,884	86,916	2,443,800
Total	\$ 11,185,000	\$ 21,596	\$ 996,304	\$ 12,202,900

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 8. Long-Term Obligations (Continued)

In connection with the creation of the Authority on July 1, 2008, the interest rate swap agreement continues to be an obligation of the City and all payments required to be made by the City under the agreement are reimbursed to the City by the Authority.

The following sets forth a summary of the Authority's derivative instrument as of June 30, 2011: The pay-fixed, receive variable interest rate swap is a cash flow hedge with a notional amount of \$11,185,000 and a negative fair value of \$833,249 at June 30, 2011. The negative fair value at June 30, 2011 represents a \$322,824 increase from the prior year and is reported on the Statement of Net Assets as a derivative liability offset by a deferred outflow of resources.

Debt Service Coverage

The Authority has been in compliance with the covenants as to the rates, fees, rentals, and charges in Article VI, Section 6.6 of the General Trust Indenture, authorizing the issuance of the Water and Sewer Revenue Bonds, Series 1998. The General Trust Indenture dated as of December 1, 1998 and four series indentures under which the City of Wilmington had issued revenue bonds were assigned to the Authority on July 1, 2008 as provided for in Section 6.11(a) of the General Trust Indenture. Section 6.6 of the General Trust Indenture requires the debt service coverage to be no less than 120% or 1.20 times on revenue bond indebtedness and to be no less than 100% or 1.00 times on total long-term indebtedness. The debt service coverage ratio calculation for the year ended June 30, 2011, is as follows:

Revenues

Operating revenues (1)	\$ 59,758,013
System development fees	2,035,607
Investment earnings	1,027,308
	<u>62,820,928</u>

Expenses

Operating expenses (2)	43,779,396
Less depreciation and amortization	(14,283,401)
Less increase in net OPEB obligation	(117,126)
	<u>29,378,869</u>

Net Revenues Available for Debt Service	<u>\$ 33,442,059</u>
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Debt Service on Parity Indebtedness	\$ 11,942,460
Debt Service on Subordinate Indebtedness	\$ 8,365,323
Total Debt Service on All Indebtedness (3)	<u>\$ 20,307,783</u>

Debt Service Coverage Ratio for Parity Indebtedness	2.80
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Debt Service Coverage Ratio for All Indebtedness	1.65
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Cape Fear Public Utility Authority

Notes to Financial Statements

Note 8. Long-Term Obligations (Continued)

(1)"Operating Revenues" from the Statement of Revenue, Expenses, and Changes in Net Assets on page 20 of this report.

(2)"Operating Expenses" from Statement of Revenue, Expenses, and Changes in Net Assets on page 20 of this report.

(3)Total long term debt includes revenue bonds (parity indebtedness), and locality compensation payables for general obligation bonds and installment obligations (subordinate indebtedness).

Note 9. Contributions From Other Governments

Contributions from other governments consist of the following contributions from New Hanover County at June 30, 2011:

Noncapital contributions:

Reduction in debt service payments	\$ 1,900,000
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Total contributions from other governments	<u>\$ 1,900,000</u>
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Note 10. Other Related Party Transactions

The Authority provides water and sewer services to the County which generated water revenues of approximately \$196,000 and sewer revenues of approximately \$173,000 for the fiscal year ended June 31, 2011 making the County one of the top 10 principal customers of the Authority. The County has a receivable to the Authority of \$48,063 as of June 30, 2011 which is included in Receivables, net on the Statement of Net Assets.

Refer to Notes 1, 8 and 9 for further disclosures on the relationship between the Authority and the County and City.

Note 11. Pending GASB Statements

The GASB has issued several pronouncements prior to June 30, 2011 that has effective dates that may impact future financial presentations.

Statement No. 57 OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans will be effective for the Authority beginning with its year ending June 30, 2012.

Statement No. 60 Accounting and Financial Reporting for Service Concession Arrangements will be effective for the Authority beginning with its year ending June 30, 2013.

Statement No. 61 The Financial reporting Entity: Omnibus-an amendment of GASB Statements No. 14 and No. 34 will be effective for the Authority with its year ending June 30, 2013.

Statement No. 62 Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements will be effective for the Authority with its year ending June 30, 2013.

Statement No. 63 Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position will be effective for the Authority with its year ending June 30, 2013.

Statement No. 64 Derivative Instruments: Application of Hedge Accounting Termination Provisions-an amendment of GASB Statement No. 53 will be effective for the Authority with its year ending June 30, 2012.

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

Cape Fear Public Utility Authority

Notes to Financial Statements

Note 12. Litigation

The Authority is a party to a number of civil lawsuits and other legal actions. There are also several claims for damages that have not yet resulted in litigation. In the opinion of the Authority attorney and management, the ultimate outcome of these claims is not expected to have a significant impact on the Authority's financial position.

Prior to the transfer of assets to the Authority on July 1, 2008, the City and the County were notified by the Environmental Protection Agency (EPA) that the City and County were in violation of the Clean Water Act. The EPA contends that the City and County experienced numerous sanitary sewer overflows that violated State and federal regulations. As the owner and operator of the wastewater system formerly operated by the City and County, the Authority has been included in the EPA action. The Authority is in negotiations with EPA and working toward a consent decree. Since the Authority began operations, it has had ongoing projects to repair and upgrade the Northeast Interceptor. In addition, the Authority has implemented comprehensive programs to control inflow and infiltration and other contributors to potential spills. Such significant progress has been made that, on September 25, 2009, the Director of the DENR Division of Water Quality notified the EPA that the State of North Carolina believes that actions taken by the Authority address most elements of the proposed consent decree with the EPA.

No admission of violation has been made by the City, the County or the Authority. The City and the County have retained a total of \$3 million for payment of any fine that may eventually be levied. In the opinion of the Authority's attorney, any fine that may be levied will be substantially less than the amount retained, and the final agreement with the EPA will not have a material effect on the Authority's financial position.

Note 13. Commitments and Contingencies

The Authority has active water and sewer capital projects as of June 30, 2011. The Authority's remaining commitments with contractors, developer and professional firms related to these projects is approximately \$41 million. The remaining commitments will be funded from the proceeds of revenue bonds and funds generated from operations.

The Authority and the City of Wilmington entered into an interlocal agreement on May 6, 2009 to share jointly in the cost of providing water and sewer services to an area that the City is annexing pursuant to North Carolina General Statutes. The agreement calls for the City to install water distribution lines and sewer collection lines to properties in the annexation area that are not served. The City and the Authority are going to share in the upgrade of water distribution mains and sewer pump stations that serve the area. The City's share is estimated at \$9.9 million with the Authority's share estimated at \$7.7 million. The City will transfer ownership for all installed improvements to the Authority upon completion. In addition the City has agreed to the payment of \$393,500 in impact fees for the 88 water and sewer connections. All water and sewer improvements are to be completed by April 2012. The Authority's share of the cost is included in the total construction commitments disclosed above.

Federal and State Assisted Programs

The Authority has been approved to receive proceeds from federal grants under the American Recovery and Reinvestment Act of 2009 (ARRA). Periodic audits of these grants are required and certain costs may be questioned as not being appropriate expenditures under the grant agreements. Such audits could result in the refund of grant moneys to the grantor agencies. Management believes that any required refunds will be immaterial. No provision has been made in the accompanying financial statements for the refund of grant moneys.

Cape Fear Public Utility Authority

Notes to Financial Statements

Billing and Collection Procedures

Each bill of the Authority includes charges levied on behalf of the City for stormwater and solid waste collection. In the event of partial payments of current charges, payments are applied to stormwater charges first, solid waste charges second, wastewater charges third and then to water charges. The Authority enforces collection procedures, including shutting off water service, on delinquent accounts. In compliance with the Interlocal Agreement, the Authority uses these same collection methods for delinquent stormwater and solid waste accounts. Payments are applied to the most delinquent billing period first with the proceeds satisfying the entire outstanding amount for that billing period to stormwater charges first, solid waste charges second, wastewater charges third and then to water charges. It is unclear whether the Authority has the legal authority to collect delinquent solid waste accounts on behalf of the City.

Note 14. Subsequent Event

On September 28, 2011, the Authority issued \$44,100,000 of Water and Sewer System Revenue Bonds, Series 2011. The 2011 Bonds are being issued for the purpose of providing funds, together with any other available funds, to (a) pay the costs of certain improvements to the Authority's water and sanitary sewer system, (b) refund the Authority's outstanding Water and Sewer System Refunding Revenue Bond, Series 2003, (c) pay interest on a portion of the 2011 Bonds until February 1, 2012, and (d) pay other costs incurred in connection with the issuance and sale of the 2011 Bonds. The interest rates on the bonds range from 2% to 5% with final maturity on August 1, 2036. Annual principal payments range from \$1,330,000-\$2,615,000.

Cape Fear Public Utility Authority

**Required Supplementary Information
Other Post-Employment Benefits
Schedule of Funding Progress
2009-2011**

Actuarial Valuation Date	Actuarial Value of Assets a	Actuarial Accrued Liability (AAL) b	Unfunded AAL (UAAL) b-a	Funded Ratio a/b	Covered Payroll for Year Ending on Valuation c	UAAL as a Percentage of Covered Payroll (b-a)/c
12/31/08	\$0	\$7,167,107	\$7,167,107	0.00%	\$11,551,913	62.04%
12/31/10	\$0	\$2,351,870	\$2,351,870	0.00%	\$12,895,415	18.24%

**Required Supplementary Information
Schedule of Employer Contributions
2009-2011**

Fiscal Years Ended	Annual Required Contribution	Percentage Contributed
2009	\$1,043,781	0.000%
2010	\$1,043,781	0.056%
2011	\$157,186	6.011%

Notes to the Required Schedules:

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

Valuation date	12/31/10
Actuarial cost method (1)	Entry Age Normal
Amortization method	Level dollar amount
Remaining amortization period	30 years
Asset valuation method	Market value
Actuarial assumptions:	
Discount rate	4.0%
Salary increases	2.5%
Medical trend rate *	4.5% -9.0%
* Includes inflation at	2.5%

(1) Projected Unit Credit method was used in the 12/31/08 valuation

Cape Fear Public Utility Authority

**Schedule of Revenues and Expenditures - Budget and Actual (Modified Accrual Basis) -
Operating Fund
For Year Ended June 30, 2011**

	Final Budget	Actual	Variance Positive (Negative)
Operating revenues			
Water charges	\$ 27,094,650	\$ 28,537,770	\$ 1,443,120
Sewer charges	26,443,873	28,548,459	2,104,586
Connection fees	489,600	400,718	(88,882)
Miscellaneous revenue	1,318,600	2,276,018	957,418
Total operating revenues	55,346,723	59,762,965	4,416,242
Nonoperating revenues			
System development charges	2,340,000	2,035,607	(304,393)
Investment earnings	928,000	896,197	(31,803)
Total nonoperating revenues	3,268,000	2,931,804	(336,196)
Total revenues	58,614,723	62,694,769	4,080,046
Operating expenditures			
General - administrative	5,651,506	4,856,774	794,732
Operations - water and sewer	21,287,534	18,635,956	2,651,578
Environment & safety management	2,229,836	1,982,762	247,074
Customer service	2,855,618	2,538,905	316,713
Nondepartmental	1,881,330	1,759,162	122,168
Debt service	23,601,879	23,562,214	39,665
Repairs and maintenance	2,126,189	1,575,397	550,792
Capital outlay	973,475	742,472	231,003
Contingency	800,000	-	800,000
Total operating expenditures	61,407,367	55,653,642	5,753,725

(Continued)

Cape Fear Public Utility Authority

**Schedule of Revenues and Expenditures - Budget and Actual (Modified Accrual Basis) -
Operating Fund (Continued)
For Year Ended June 30, 2011**

	Final Budget	Actual	Variance Positive (Negative)
Other financing sources (uses)			
Capital contributions	\$ -	\$ 2,868	\$ 2,868
Transfers out - Capital Projects Funds	(2,888,500)	(2,888,500)	-
Appropriated fund balance	5,681,144	-	(5,681,144)
Total financing sources (uses)	2,792,644	(2,885,632)	(5,678,276)
 Revenue and other financing sources over (under) expenditures	 \$ -	 4,155,495	 \$ 4,155,495

Reconciliation of modified accrual basis

to full accrual basis:

Revenue and other financing sources (under)	
expenditures - capital projects funds water and sewer	(39,996,365)
Capital contributions	67,157
Depreciation and amortization on capital assets	(14,283,401)
Amortization on bond issue costs	(230,087)
Capital and intangible assets	39,256,201
Long-term obligations:	
Unamortized charge-interest expense	(371,652)
Unamortized bond discount/premium-interest income	442,117
Accrued interest income	(37)
Accrued interest expense	61,430
Other postemployment benefits (OPEB)	(117,126)
Compensated absences accrual	(34,044)
Principal payment on long-term debt	11,047,645
Decrease in net assets	\$ (2,667)

Cape Fear Public Utility Authority

**Schedule of Revenue and Expenditures - Budget and Actual (Modified Accrual Basis) -
Capital Projects Funds - Water and Sewer
From Inception and For the Fiscal Year Ended June 30, 2011**

	Project Ordinance	Prior Years	Actual Current Year	Total to Date
Revenue				
Investment earnings	\$ 4,567,230	\$ 6,432,901	\$ (599,824)	\$ 5,833,077
Total revenue	4,567,230	6,432,901	(599,824)	5,833,077
Expenditures				
Northern School Site	5,170,671	4,471,901	241,602	4,713,503
Barnards Creek Outfall	72,000	59,349	7,077	66,426
Hydraulic Model/Cap Study	431,934	391,249	39,032	430,281
Burnt Mill Creek Outfall	6,895,078	3,372,936	81,077	3,454,013
Infiltration Inflow I&E	1,008,216	307,835	368,551	676,386
GIS Asbuilt Entry/Mapping	147,845	47,845	-	47,845
NSWWTP Force Main	5,843,410	155,736	1,506,521	1,662,257
Northern Route Force Main	17,257,861	3,232,688	1,728,871	4,961,559
SSWWTP Rehab & Upgrade	8,597,828	2,418,925	3,400,012	5,818,937
GIS & CMMS Updates	94,231	76,546	4,223	80,769
Asset Mgmt Implementation Study	2,534,774	611,688	1,591,884	2,203,572
Sewer Emergency Repair	3,902,293	1,437,386	-	1,437,386
Downtown Sewer Rehab/Assessment	981,037	740,731	-	740,731
General W&S Projects-NHC	881,017	791,997	-	791,997
Middle Sound Sewer-NHC	2,621,540	33,483	1,620,024	1,653,507
Relocate Utility Lines Per DOT	2,650,039	1,389,508	123,985	1,513,493
Annex 98-Sewer Extensions	1,380,835	74,613	7,244	81,857
NSWWTP Expansion//Upgrade	5,861,855	5,802,265	52,399	5,854,664
NEI Rehab Project-PS 34-35	9,374,565	2,213,834	3,398,744	5,612,578
River Road Force Main	1,218,469	243,768	168,500	412,268
System Wide OCCP Facility	2,247,345	588,810	1,374,356	1,963,166
Country Haven PS Upgrade	2,322,435	135,183	77,094	212,277
PS 34 Barscreen Replacement	1,428,451	140,720	67,520	208,240
PS 10-12	113,200	113,200	-	113,200
N Front St Streetscape - Sewer	633,403	340,784	24,132	364,916
Downtown Water Line Rehab	1,187,015	1,157,387	25,800	1,183,187
Water Valve Replacement	200,000	-	13,690	13,690
Water Laterals & Services	75,000	-	-	-
Phase I CB Rd Trans Main	650,500	94,558	-	94,558

(Continued)

Cape Fear Public Utility Authority

**Schedule of Revenue and Expenditures - Budget and Actual (Modified Accrual Basis) -
Capital Projects Funds - Water and Sewer (Continued)
From Inception and For the Fiscal Year Ended June 30, 2011**

		Actual		
	Project Ordinance	Prior Years	Current Year	Total to Date
COW-NHC Water System Study	\$ 234,860	\$ 199,222	\$ -	\$ 199,222
GIS Asbuilt Integration	141,211	45,085	-	45,085
Kerr Ave Waterline	616,882	76,912	-	76,912
Heritage Park Water	771,362	16,765	-	16,765
Northern School Site	1,800,390	1,763,562	36,827	1,800,389
Water Emergency Repair	2,535,462	65,837	-	65,837
Annex 95 & 98 Water Lines	206,574	5,286	-	5,286
Water System Enhancements-NHC	990,630	958,009	-	958,009
Wellfield & Water Treatment Plant-NHC	28,342,999	27,879,187	84,350	27,963,537
Sweeney WTP Exp To 40 MGD	73,832,722	36,550,134	18,161,673	54,711,807
Environmental Services Building	4,596,830	4,155,127	234,871	4,389,998
30" Raw Water Main Rehab	6,152,127	5,185,171	24,887	5,210,058
Meter Replacement Program	245,000	99,616	-	99,616
Aquifer Storage Retrieval	3,007,515	415,105	587,155	1,002,260
Annex 1195 Area Water System	136,202	55,910	-	55,910
N Front St Streetscape - Water	633,411	340,973	192,825	533,798
N Third St Streetscape - Sewer	1,208,418	173,078	20,618	193,696
Heritage Park Pump Station	410,000	-	-	-
Find It/Fix it Repairs	34,471	-	34,470	34,470
Scada Telemetry Enhancement	430,705	29,150	-	29,150
US 421 Regional WWTP	788,742	547,241	198,659	745,900
Vactor Bay Building	450,000	-	11,063	11,063
Manhole Rehab	592,250	-	406	406
ARV Replacement	100,000	-	-	-
Pump Station-Bernards & Motts Creek	4,155,208	120,032	131,964	251,996
Myrtle Landing Subdivision	327,000	-	-	-
Ogden Interceptor	5,811,924	1,723,505	3,866,579	5,590,084
Riverside Subdivision Project	160,055	-	-	-
Barclay Hills & Princess Place	238,992	954	228,364	229,318
Wrightsville Avenue	237,602	-	227,946	227,946
N. Third St. Streetscape - Water	1,200,727	-	-	-
System Interconnects	838,900	75	4,803	4,878
Aquifer Sustain & Monitor	30,636	15,000	15,000	30,000
Porters Neck Water System	1,078,000	695,056	338,570	1,033,626
Raw Water Pump Station	1,214,884	111,019	475,743	586,762
Toomers Creek Water Line	291,355	31,144	187,191	218,335
30th & Princess Place Dr	114,720	-	114,720	114,720
Gleason & McCelland Sewer	77,606	-	77,605	77,605
Arboretum/Wild Turkey	38,000	-	38,000	38,000
Dawson & Surry Emergency	83,636	-	83,635	83,635
Mimosa St Area Outfall	44,538	-	44,538	44,538
Marstellar St. Sewer Project	292,389	-	287,447	287,447

(Continued)

Cape Fear Public Utility Authority

**Schedule of Revenue and Expenditures - Budget and Actual (Modified Accrual Basis) -
Capital Projects Funds - Water and Sewer (Continued)
From Inception and For the Fiscal Year Ended June 30, 2011**

	Project Ordinance	Prior Years	Actual Current Year	Total to Date
39th St. Sewer Repair	\$ 44,209	\$ -	\$ 44,208	\$ 44,208
Walden Dr/Lake Shore	38,755	-	38,755	38,755
Collection System Rehab	725,529	-	-	-
Gum Branch Outfall Repair	36,117	-	36,116	36,116
E. Shore Dr. Sewer Repair	37,762	-	37,761	37,761
Marsh Oaks FM Repair	75,000	-	26,454	26,454
W.Lake Shore Dr. Sewer	106,542	-	106,542	106,542
NSWWTP Bypass Emergency Repair	56,224	-	56,223	56,223
6th St. Sewer Repair	143,870	-	135,897	135,897
S. Kerr Ave. Sewer Repair	30,653	-	30,653	30,653
Airport Entrance Sewer Emergency	21,954	-	21,954	21,954
Sheffield Dr. Manhole	38,936	-	38,936	38,936
Airport Sewer Main Replacement	114,898	-	150,548	150,548
Campbell St. Sewer Repair	52,450	-	2,450	2,450
Kerr & McCelland Sewer	144,629	-	153,082	153,082
11th & Hanover Sewer Repair	305,608	-	104,890	104,890
Gleason Sewer Cave-In	237,070	-	225,712	225,712
Grace St. 900 Block	1,850	-	1,850	1,850
Between the Creeks	7,750	-	-	-
Nano Generator Repairs	128,325	-	115,726	115,726
23rd Street	250,000	-	-	-
Grathwol-Kings Grant Interconnect	50,000	-	17,885	17,885
Foxwood lane Interconnect	36,000	-	-	-
Groppo Cove & Haymarket	125,000	-	-	-
S. College Hardess Interconnect	35,000	-	-	-
Nano Market St. Feeder	64,100	-	14,870	14,870
Completed Projects-Prior Years	6,020,783	6,020,780	-	6,020,780
Total expenditures	239,206,796	117,723,860	42,992,759	160,716,619
Revenue (under) expenditures	(234,639,566)	(111,290,959)	(43,592,583)	(154,883,542)
Other financing sources				
Long-term obligations issued	174,781,484	152,024,732	-	152,024,732
Capital contributions revenue	2,246,413	1,025,567	707,718	1,733,285
Transfers in - Operating Fund	11,245,172	7,900,000	2,888,500	10,788,500
Appropriated fund balance	46,366,497	-	-	-
Total other financing sources	234,639,566	160,950,299	3,596,218	164,546,517
Revenue and other financing sources over (under) expenditures	\$ -	\$ 49,659,340	\$ (39,996,365)	\$ 9,662,975

Statistical Section

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Statistical Section Overview

Financial Trends:

These charts and schedules identify the trends in changes over time of Cape Fear Public Utility Authority's financial functional effectiveness and financial strength.

- Net Assets by Component
- Change in Net Assets

Revenue Capacity:

These schedules contain information to help the reader assess the Authority's revenue sources.

- Schedule of User Rates
- Principal Employers
- Principal Customers
- Consumption by Customer Group
- Schedule of New Connections

Debt Capacity:

The schedule represents the ratio of debt to revenue.

- Pledged-Revenue Coverage
- Ratios of Outstanding Debt by Type

Demographic and Economic Information:

These schedules show the demographic and economic picture of the environment in which Cape Fear Public Utility Authority provides its services.

- Demographic Statistics
- Full Time Equivalent Employees

Operating Information:

These schedules contain operating and capital asset data to show how operations and assets have changed as the Authority grows.

- Water Production and Wastewater Treatment
- Operating Statistics

Sources:

Unless otherwise noted, the information included in these schedules and charts is derived from the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2011 and is provided for additional analysis purposes only and has not been verified by audit as presented.

Cape Fear Public Utility Authority

**Net Assets By Component
Last Three Fiscal Years
(Accrual Basis of Accounting)**

	Fiscal Year 2011	Fiscal Year 2010	Fiscal Year 2009, Restated (1)
Invested in capital assets, net of related debt	\$ 287,538,728	\$ 295,307,938	\$ 293,467,066
Unrestricted	72,046,877	64,280,334	60,460,682
Total net assets	<u>\$ 359,585,605</u>	<u>\$ 359,588,272</u>	<u>\$ 353,927,748</u>

Source: Cape Fear Public Utility Authority's Accounting Records.

Note: Fiscal year 2009 was the first year of operations for the Authority.

(1) Statement of Net Assets was restated in fiscal year 2009 to reflect a change in accounting principle.

Cape Fear Public Utility Authority

**Change in Net Assets
Last Three Fiscal Years
(Accrual Basis of Accounting)**

	Fiscal Year 2011	Fiscal Year 2010	Fiscal Year 2009, Restated (1)
Operating revenues			
Charges for services	\$ 57,086,229	\$ 47,524,673	\$ 42,726,268
Other operating revenues	2,671,784	2,313,214	139,595
Total operating revenues	59,758,013	49,837,887	42,865,863
Operating expenses			
Personnel and benefits	15,176,175	17,038,778	17,714,505
Services and utilities	10,689,144	10,888,068	11,475,219
Materials	3,630,676	2,431,060	3,264,294
Depreciation and amortization	14,283,401	13,096,230	12,400,153
Total operating expenses	43,779,396	43,454,136	44,854,171
Operating income (loss)	15,978,617	6,383,751	(1,988,308)
Nonoperating revenues (expenses)			
Investment earnings	738,453	4,105,897	5,970,732
Interest expense	(13,011,609)	(10,909,406)	(9,674,421)
Amortization	(230,087)	(235,208)	(432,912)
Contributions from the City of Wilmington and New Hanover County	1,900,000	1,900,000	64,627,498
Total nonoperating (expenses)	(10,603,243)	(5,138,717)	60,490,897
Income before capital contributions, special items and extraordinary items	5,375,374	1,245,034	58,502,589
Capital contributions from the City of Wilmington and New Hanover County	-	-	285,873,980
Capital contributions - other	2,813,350	7,982,758	9,551,179
Special impairment of capital assets	(8,191,391)	(2,275,200)	-
Extraordinary impairment of capital assets	-	(1,292,068)	-
Total capital contributions, special and extraordinary items	(5,378,041)	4,415,490	295,425,159
Increase (decrease) in net assets	(2,667)	5,660,524	353,927,748
Net assets			
Beginning of year	359,588,272	353,927,748	-
End of year	\$ 359,585,605	\$ 359,588,272	\$ 353,927,748

Source: CFPWA Water and Sewer Authority's Accounting Records.

Note: Fiscal year 2009 was the first year of operations for the Authority.

(1) Statement of Revenues, Expenses and Changes in Net Assets was restated in fiscal year 2009 to reflect a change in accounting principle.

Cape Fear Public Utility Authority

Schedule of User Rates Last Three Fiscal Years

	Fiscal Year		
	2011 (1)	2010 (1)	2009
Water Rates			
Water Fixed Rate (bi-monthly)	\$ 24.99	\$ 21.89	\$ 15.20
Water Variable Rate:			
0 - 9,000 gallons	N/A	\$ 2.22	\$ 1.95
9,001 - 18,000 gallons	N/A	\$ 3.36	\$ 2.95
18,001+ gallons	N/A	\$ 4.50	\$ 3.95
0 - 12,000 gallons	\$ 2.64	N/A	N/A
12,001 - 24,000 gallons	\$ 3.96	N/A	N/A
Over 24,000 gallons	\$ 5.28	N/A	N/A
Irrigation (5)	\$ 2.64	N/A	N/A
Non-Residential	\$ 3.96	\$ 3.36	\$ 2.95
Average bi-monthly residential bill (4)	\$ 51.39	\$ 45.23	\$ 35.70
Sewer Rates			
Sewer Fixed Rate (bi-monthly)	\$ 26.68	\$ 23.37	\$ 16.50
Sewer Variable Rate (2)	\$ 3.59	\$ 3.14	\$ 2.75
Sewer Flat Rate (3)	\$ 112.84	\$ 98.73	\$ 82.50
Average bi-monthly residential bill (4)	\$ 62.58	\$ 54.77	\$ 44.00

Note: Fiscal year 2009 was the first year of operations for the Authority.

- (1) Rates effective May 1 of respective fiscal year.
- (2) Sewer volume charges are capped at 30,000 gallons for residential customers.
- (3) Sewer flat rate charge when Authority water is not available.
- (4) Average bi-monthly bill calculated at usage of 10,000 gallons.
- (5) Board adopted lower irrigation rate to discourage irrigation wells.

Cape Fear Public Utility Authority

**Principal Employers
Current Fiscal Year and Two Years Ago**

Employer	2011		
	Employees (1)	Rank	Percentage of Total County Employment
New Hanover Regional Medical Center	4,738	1	5.04%
New Hanover County Schools	3,666	2	3.90%
Wal-Mart Stores	2,592	3	2.76%
GE Wilmington	2,100	4	2.23%
The University of North Carolina at Wilmington	1,898	5	2.02%
PPD, Inc.	1,500	6	1.60%
New Hanover County	1,480	7	1.57%
Corning, Inc.	1,000	8	1.06%
City of Wilmington	981	9	1.04%
Cape Fear Community College	541	10	0.58%
			21.80%

Total # Employed June 30 of the respective FY (2) 94,030

Employer	2009		
	Employees (3)	Rank	Percentage of Total County Employment
New Hanover Regional Medical Center	4,890	1	5.10%
New Hanover County Schools	4,130	2	4.30%
GE Wilmington	3,000	3	3.13%
The University of North Carolina at Wilmington	1,810	4	1.89%
New Hanover County	1,670	5	1.74%
PPD, Inc.	1,420	6	1.48%
Cape Fear Community College	1,260	7	1.31%
City of Wilmington	1,200	8	1.25%
Verizon Wireless	1,200	9	1.25%
Corning, Inc.	1,000	10	1.04%
			22.49%

Total # Employed June 30 of the respective FY (2) 95,964

Note: Fiscal year 2009 was the first year of operations for the Authority.

(1) Source: Wilmington Chamber of Commerce, verified by CFPUA staff.

(2) Source: North Carolina Employment Security Commission

(3) Source: New Hanover County CAFR for Fiscal Year Ended June 30, 2009 using Wilmington Industrial Development, Inc. and NC State Demographics Web Site

Cape Fear Public Utility Authority

Principal Customers
Current Fiscal Year and Two Years Ago

2011				
	Thousand Gallons	% of System	Revenue (\$)	% of Revenue
Ten Largest Users of the Water System Annual Consumption				
1 UNC Wilmington	183,400	3.34%	\$ 670,500	2.37%
2 New Hanover Regional Medical Center	60,103	1.10%	253,431	0.90%
3 New Hanover County Schools	51,773	0.94%	288,296	1.02%
4 Wilmington Housing Authority	37,520	0.68%	158,505	0.56%
5 New Hanover County	36,290	0.66%	195,927	0.69%
6 Lake Forest Apartments	33,107	0.60%	128,507	0.45%
7 College Manor Apartments	30,588	0.56%	123,732	0.44%
8 Mayfaire Complex	25,244	0.46%	163,222	0.58%
9 Tribute Properties	24,645	0.45%	174,715	0.62%
10 Wilmington Hilton	18,448	0.34%	71,652	0.25%
Total Consumption	501,118 	9.13%	\$ 2,228,487	7.88%
Total system annual consumption	<u>5,485,532</u>		<u>\$ 28,288,199</u>	
Ten Largest Users of the Sewer System Annual Consumption				
1 Town of Wrightsville Beach	242,837	4.79%	\$ 358,180	1.28%
2 UNC Wilmington	111,952	2.21%	399,691	1.42%
3 New Hanover County Schools	49,331	0.97%	272,876	0.97%
4 New Hanover Regional Medical Center	59,071	1.17%	236,881	0.84%
5 New Hanover County	34,159	0.67%	172,881	0.62%
6 Wilmington Housing Authority	37,420	0.74%	149,983	0.53%
7 College Manor Apartments	30,588	0.60%	117,478	0.42%
8 Lake Forest Apartments	33,107	0.65%	120,990	0.43%
9 Mayfaire Complex	25,012	0.49%	159,386	0.57%
10 Tribute Properties	24,382	0.48%	192,464	0.69%
Total Consumption	647,859 	12.77%	\$ 2,180,810	7.77%
Total system annual consumption	<u>5,070,084</u>		<u>\$ 28,052,866</u>	

Note: Fiscal year 2009 was the first year of operations for the Authority.

(1) Prior year data has been updated to reflect adjustments made in the current year.
 Water includes domestic and irrigation connections.

2009 (1)

	Thousand Gallons	% of System	Revenue (\$)	% of Revenue
1 UNC Wilmington	135,005	2.31%	\$ 423,415	1.86%
2 New Hanover County	63,491	1.09%	234,834	1.03%
3 New Hanover Regional Medical Center	71,800	1.23%	212,373	0.93%
4 Mayfaire Complex	54,782	0.94%	219,690	0.96%
5 New Hanover County Schools	48,853	0.84%	209,638	0.92%
6 Wilmington Housing Authority	40,961	0.70%	137,552	0.60%
7 Lake Forest Apartments	30,109	0.52%	97,442	0.43%
8 College Manor Apartments	23,411	0.40%	80,985	0.36%
9 Elementis Chromium	22,469	0.39%	68,562	0.30%
10 Wilmington Hilton	18,194	0.31%	57,865	0.25%
	<u>509,075</u>	<u>8.73%</u>	<u>1,742,356</u>	<u>7.64%</u>
	<u>5,834,129</u>		<u>\$ 22,781,177</u>	
1 Town of Wrightsville Beach	214,743	4.42%	322,115	1.46%
2 UNC Wilmington	87,395	1.80%	266,776	1.21%
3 New Hanover Regional Medical Center	69,080	1.42%	177,762	0.80%
4 Mayfaire Complex	54,999	1.13%	216,142	0.98%
5 New Hanover County Schools	46,910	0.97%	202,111	0.91%
6 Wilmington Housing Authority	40,657	0.84%	129,305	0.59%
7 New Hanover County	37,267	0.77%	142,352	0.64%
8 Lake Forest Apartments	30,101	0.62%	92,180	0.42%
9 College Manor Apartments	23,411	0.48%	77,352	0.35%
10 Wilmington Hilton	17,935	0.37%	54,278	0.25%
	<u>622,498</u>	<u>12.82%</u>	<u>1,680,373</u>	<u>7.61%</u>
	<u>4,856,146</u>		<u>\$ 22,089,335</u>	

Cape Fear Public Utility Authority

Consumption by Customer Group Last Three Fiscal Years

	2011		2010 (1)		2009 (1)	
	Thousand Gallons	% of Consumption	Thousand Gallons	% of Consumption	Thousand Gallons	% of Consumption
Water Customers						
Residential	3,887,894	70.88%	3,652,988	70.13%	4,152,536	71.17%
Commercial	1,075,703	19.61%	1,032,322	19.82%	1,094,936	18.77%
Industrial	62,278	1.13%	57,719	1.11%	102,707	1.76%
Institutional and Governmental	459,656	8.38%	465,940	8.94%	483,950	8.30%
Total	5,485,531	100.00%	5,208,969	100.00%	5,834,129	100.00%
Sewer Customers						
Residential	3,497,483	68.98%	3,329,608	69.30%	3,543,624	72.97%
Commercial	957,062	18.88%	842,782	17.54%	869,266	17.90%
Town of Wrightsville Beach	214,479	4.23%	234,303	4.88%	214,743	4.42%
Pender County	16,224	0.32%	13,550	0.28%	14,139	0.30%
Industrial	18,219	0.36%	23,060	0.48%	24,964	0.51%
Institutional and Governmental	366,618	7.23%	361,467	7.52%	189,410	3.90%
Total	5,070,085	100.00%	4,804,770	100.00%	4,856,146	100.00%

Notes: Fiscal year 2009 was the first year of operations for the Authority.

(1) Prior year data has been updated to reflect adjustments made in the current year.

Water include domestic and irrigation connections.

Cape Fear Public Utility Authority

**Schedule of New Connections
Last Three Fiscal Years**

Fiscal Year							
Ended	Water	Cumulative	% Water	Sewer	Cumulative	% Sewer	Total
June 30	Connections (1)	Connections	Growth	Connections	Connections	Growth	Services
2011	1,569	67,468	2.4%	471	65,032	0.7%	132,500
2010 (2)	1,542	65,899	2.4%	1,053	64,561	1.7%	130,460
2009	-	64,357	-	-	63,508	-	127,865

Note: Fiscal year 2009 was the first year of operations for the Authority.

(1) Water connections include domestic and irrigation connections

(2) Prior years restated based on more accurate data from the Customer Service Division.

Cape Fear Public Utility Authority

**Pledged-Revenue Coverage
Water and Sewer Revenue Bonds
Last Three Fiscal Years**

Fiscal Year Ended June 30	Gross Revenues (1)	Less Operating Expenses (2)	Net Available Revenue	Debt Service Principal	Debt Service Interest	Total Debt Service	Coverage
2011							
Parity Debt Coverage Ratio	\$ 62,820,928	\$ 29,378,869	\$ 33,442,059	\$ 3,329,579	\$ 8,612,881	\$ 11,942,460	\$ 2.80
Total Debt Coverage Ratio				\$ 9,147,645	\$ 11,160,138	\$ 20,307,783	\$ 1.65
2010 (3)							
Parity Debt Coverage Ratio	\$ 53,457,074	\$ 29,314,125	\$ 24,142,949	\$ 2,320,562	\$ 5,220,454	\$ 7,541,016	\$ 3.20
Total Debt Coverage Ratio				\$ 8,706,072	\$ 8,092,789	\$ 16,798,861	\$ 1.44
2009 (3)							
Parity Debt Coverage Ratio	\$ 47,783,403	\$ 31,517,799	\$ 16,265,604	\$ 2,232,043	\$ 4,040,421	\$ 6,272,464	\$ 2.59
Total Debt Coverage Ratio				\$ 7,987,738	\$ 7,508,261	\$ 15,495,999	\$ 1.05

Note: Fiscal year 2009 was the first year of operations for the Authority.

(1) Gross revenues include all fees (including system development charges), other charges and investment income.

(2) Operating expenses do not include interest, OPEB, depreciation and amortization expenses.

(3) Debt coverage ratios were restated due to a restatement of investment earnings to be consistent with fiscal year ended June 30, 2011.

Cape Fear Public Utility Authority

Ratios of Outstanding Debt by Type Last Three Fiscal Years

Fiscal Year	Revenue Bonds	General	ARRA	Installment Obligations	Capital Leases	Total	% of	
		Obligation Bonds	Revolving Loan				Personal Income (1)	Per Capita
2011	\$ 255,556,814	\$11,712,630	\$ 330,545	\$ 39,918,647	\$179,315	\$ 307,697,951	N/A	\$ 1,518
2010	259,225,928	16,371,000	-	42,475,207	413,381	318,485,516	N/A	1,641
2009	261,888,896	21,605,709	-	45,007,970	155,324	328,657,899	0.014%	1,710

Note: Fiscal year 2009 was the first year of operations for the Authority.

(1) Personal income demographics provided by US Census Bureau; data provided for as many years as available.

Cape Fear Public Utility Authority

Demographic Statistics Last Three Fiscal Years

Fiscal Year Ended June 30	City of Wilmington Population (1)	New Hanover County Population (1)(2)	Median Age (1)	Public School Enrollment (3)	Local Unemployment Rate % (4)	Personal Income (5)	Per Capita Income (5)
2011	106,476	202,667	36.7	23,934	10.1%	N/A	N/A
2010	102,207	194,054	38.5	23,643	9.4%	N/A	N/A
2009	101,526	192,235	38	23,614	9.0%	\$ 44,719	\$ 29,148

Note: Fiscal year 2009 was the first year of operations for the Authority.

(1) N. C. State Demographics.

(2) 2011 population information provided by US Census Bureau

(3) Figures are provided by the NHC Public Schools.

(4) North Carolina Employment Security Commission.

(5) Provided by US Census Bureau; data provided for as many years as available.

Cape Fear Public Utility Authority

**Full Time Equivalent Employees
Last Three Fiscal Years**

Departments	2011	2010	2009
General and Administrative			
Administration	5	6	7
Human Resources	4	4	4
Finance/Information Technology	15	15	16
Engineering	22	24	25
Operations			
Administration/Warehouse	9	9	9
Utility Services - Lines and Meters	43	55	55
Water Treatment	30	31	31
Wastewater Treatment	40	41	41
Sewer Collections	53	49	49
Environmental & Safety Management	30.5	29.5	30.5
Customer Service	41	41	42
Total FTE's	292.5	304.5	309.5

Note: Fiscal year 2009 was the first year of operations for the Authority.

Cape Fear Public Utility Authority
Water Production and Wastewater Treatment
(thousands of gallons)
Last Six Fiscal Years

Fiscal Year Ended June 30	Water Processed and Pumped to System (1)	Wastewater Treated (1)
2011	6,179,900	5,777,917
2010	5,989,700	6,122,662
2009	6,375,455	5,696,412
2008	6,590,075	5,429,210
2007	6,906,195	6,132,272
2006	6,940,475	6,004,330

Note: Fiscal year 2009 was the first year of operations for the Authority.

(1) Information for fiscal years ended June 30, 2006, 2007, 2008 provided by City of Wilmington and New Hanover County.

Cape Fear Public Utility Authority

Operating Statistics Last Three Fiscal Years

	Fiscal Year		
	2011	2010	2009
Water System			
Number of service connections	67,468	65,899	64,357
Number of treatment plants - surface water system	1	1	1
Treatment capacity (mgd) - surface water	27.5	27.5	27.5
Average production (mgd) - surface water	13.7	13.3	14.3
Number of groundwater systems	3	3	3
Number of treatment plants - groundwater system (1)	1	1	-
Number of wells - groundwater system	36	36	36
Treatment capacity (mgd) - groundwater plant	6	6	-
Treatment capacity (mgd) - other groundwater systems	0.7	0.7	7.0
Average production (mgd) - groundwater	3.2	3.3	3.1
Miles of water mains	1070 (3)	1,129	1,103
Wastewater System			
Number of service connections	65,032	64,561	63,508
Number of treatment plants	3	3	3
WPC plant permit (mgd)	22.1	22.1	22.1
Average annual daily flow (mgd)	15.8	16.8	15.6
Number of lift stations	141	142	142
Miles of sewer gravity mains	840	881	877
Miles of sewer force mains (2)	104	100	100
Number of Manholes	20,300	N/A	N/A

Source: Cape Fear Public Utility Authority Records

Note: Fiscal year 2009 was the first year of operations for the Authority.

- (1) During FY 2010, a groundwater treatment plant began operations providing advanced treatment for the largest of the three groundwater systems and resulted in a .3 mgd reduction in total treatment capacity.
- (2) Prior years restated based on more accurate data from the Authority's Operations Division.
- (3) Current year number is based on more accurate information as a result of implementing an asset management system.

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Compliance Section

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**Independent Auditor's 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**

To the Board of Directors
Cape Fear Public Utility Authority
Wilmington, North Carolina

We have audited the financial statements of Cape Fear Public Utility Authority (the "Authority") as of and for the year ended June 30, 2011, and have issued our report thereon dated October 25, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

Management of Cape Fear Public Utility Authority is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered Cape Fear Public Utility Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Cape Fear Public Utility Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Cape Fear Public Utility Authority's internal control over financial reporting.

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 entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified a certain deficiency in internal control over financial reporting, described in the accompanying Schedule of Findings and Questioned Costs as Finding 2011-1, that we consider to be a significant deficiency in internal control over financial reporting. 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.

Compliance and Other Matters

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

We noted certain matters that we reported to management of Cape Fear Public Utility Authority in a separate letter dated October 25, 2011.

Cape Fear Public Utility Authority's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. We did not audit Cape Fear Public Utility Authority's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, the finance committee, others within the entity, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

McGladrey & Pullen, LLP

Wilmington, North Carolina
October 25, 2011



**Independent Auditor's Report
on Compliance With Requirements That Could Have a Direct and Material Effect
on Each Major Program and Internal Control Over Compliance
in Accordance with OMB Circular A-133**

To the Board of Directors
Cape Fear Public Utility Authority
Wilmington, North Carolina

Compliance

We have audited Cape Fear Public Utility Authority's (the "Authority") compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on Cape Fear Public Utility Authority's major federal program for the year ended June 30, 2011. Cape Fear Public Utility Authority's major federal program is identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of Cape Fear Public Utility Authority's management. Our responsibility is to express an opinion on Cape Fear Public Utility Authority's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and the State Single Audit Implementation Act. Those standards, OMB Circular A-133 and the State Single Audit Implementation Act require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Cape Fear Public Utility Authority's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Cape Fear Public Utility Authority's compliance with those requirements.

In our opinion, Cape Fear Public Utility Authority complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2011.

Internal Control over Compliance

Management of Cape Fear Public Utility Authority is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Cape Fear Public Utility Authority's internal control over compliance with requirements that could have a direct and material effect on a major federal program to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133 and the State Single Audit Implementation Act, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Cape Fear Public Utility Authority's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of management, the audit committee, others within the entity, the United States Environmental Protection Agency and the North Carolina Department of Environment and Natural Resources and is not intended to be and should not be used by anyone other than these specified parties.

McGladrey & Pullen, LLP

Wilmington, North Carolina
October 25, 2011

Cape Fear Public Utility Authority

**Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2011**

Section I - Summary Auditor's Results

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

- | | | |
|---|-----------|--------------------|
| ◆ Material weakness(es) identified? | _____yes | _____✓no |
| ◆ Significant deficiency(ies) identified
that are not considered to be material
weakness(es)? | _____✓yes | _____none reported |

Noncompliance material to financial
statements noted?

_____yes _____✓no

Federal Awards

Internal control over major Federal programs:

- | | | |
|---|----------|---------------------|
| ◆ Material weakness(es) identified? | _____yes | _____✓no |
| ◆ Significant deficiency(ies) identified
that are not considered to be material
weaknesses? | _____yes | _____✓none reported |

Type of auditor's report issued on compliance for major Federal programs: Unqualified

Any audit findings disclosed that are
required to be reported in accordance
with Section 510(a) of Circular A-133?

_____yes _____✓no

Identification of major Federal program:

CFDA #

Program Name

66.468

Capitalization Grants for Drinking Water
State Revolving Funds

Dollar threshold used to distinguish
between Type A and Type B Programs:

\$300,000

Auditee qualified as low-risk auditee?

_____yes _____✓no

Cape Fear Public Utility Authority

**Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2011**

Section II - Financial Statement Findings

Finding 2011-1

Significant Deficiency

Calculation of Capitalized Interest

Criteria: Interest expense during the period of construction for a capital project is one of the costs of constructing the project and placing the project into service. Therefore, interest expense during the period of construction should be capitalized as part of overall project/asset costs. The Authority should have controls in place to ensure that the calculation of interest expense to be capitalized follows Generally Accepted Accounting Principles ("GAAP").

Condition: The Authority calculated the interest rate to be used for determining capitalized interest expense without netting certain investment earnings against interest expense.

Context: The Authority follows GASB standards for financial accounting and reporting and has elected to apply only FASB statements and interpretations issued before November 30, 1989 to the extent that those standards do not conflict with or contradict the guidance of GASB. GASB guidance addresses capitalization of interest cost as part of the historical cost of assets, but has historically been vague about how to determine the appropriate interest cost. Relevant FASB guidance indicates that the interest cost of acquiring assets with the proceeds of tax-exempt borrowings should be offset by the interest earned on the temporary investment of those proceeds if those funds are externally restricted to finance the acquisition of specified qualifying assets or to service the related debt. In December 2010 the GASB issued Statement No. 62 (which is not yet effective) to clarify the application of FASB statements and interpretations issued before November 30, 1989.

The Authority has been calculating its capitalized interest without reduction for interest earned on the proceeds of tax-exempt borrowings which meet the requirements noted in the guidance. This error has existed in the calculation used for capitalized interest since the inception of the Authority, however has gone undetected during the two prior years' audits. In the current year, the calculation was subjected to increased scrutiny due to an error in the calculation of interest income on the part of the bond Trustee.

Effect: Overcapitalization of interest in prior years. This resulted in understatement of interest expense in prior years by approximately \$1.8 million, which was corrected in the current year. This error has no impact on the Authority's Debt Service Coverage calculations in the current year or either of the prior two years.

Cause: Misinterpretation of relevant GAAP guidance.

Recommendation: The Authority should carefully review its calculation of capitalized interest in light of GASB 62 to ensure that capitalized interest is calculated in accordance with GAAP.

Cape Fear Public Utility Authority

**Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2011**

Section II - Financial Statement Findings (Continued)

Views of responsible
officials:

Management agrees with this finding. Interest expense in the basic financial statements was understated in prior years and corrected in the current year. This error has had no effect on Debt Service Coverage or the Budget-to-Actual statements used by the Board and management to analyze the Authority's operating results. A large majority of the understatement was in the Authority's first year of operations (fiscal year ended June 30, 2009). The Authority has used the same calculation each of its three years of operations. The calculation has been audited by the same audit firm each year, and although they commented on the interest capitalization calculation, they did not mention the requirement to reduce interest expense by interest earned.

Cape Fear Public Utility Authority

Schedule of Findings and Questioned Costs (Continued)
For the Year Ended June 30, 2011

Section III - Federal Award Findings

None.

Cape Fear Public Utility Authority
Corrective Action Plan
For the Fiscal Year Ended June 30, 2011

Section II – Financial Statement Finding

Finding 2011-1:

Name of contact person: Cheryl J. Spivey, CFO

Corrective Action: The Finance and Accounting Manager will plan to attend the UNC School of Government's four-day Government Accounting and Financial Reporting course in spring 2012 for an in-depth refresher of generally accepted accounting principles. Information obtained from this course will be used to prepare future financial statements.

Proposed Completion Date: Spring 2012.

Cape Fear Public Utility Authority
Summary Schedule of Prior Audit Findings
For the Year Ended June 30, 2011

None

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Cape Fear Public Utility Authority

Schedule of Expenditures of Federal and State Awards For the Year Ended June 30, 2011

Grantor/Pass-through <u>Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>State/ Pass-through Grantor's Number</u>	<u>Federal (Direct & Pass-through) Expenditures</u>	<u>State Expenditures</u>	<u>Local Expenditures</u>
Federal Awards:					
<u>U.S. Environmental Protection Agency</u>					
Passed-through the N.C. Dept. of Environment and Natural Resources:					
Division of Environmental Health:					
ARRA - DWSRF Revolving Loan	66.468	DEH-1314	\$ 279,225	\$ -	\$ -
ARRA - DWSRF Principal Forgiveness Loan	66.468	DEH-1314	279,225	-	-
			<u>558,450</u>	<u>-</u>	<u>-</u>
Total U.S. Environmental Protection Agency			<u>558,450</u>	<u>-</u>	<u>-</u>
Total federal awards			<u>\$ 558,450</u>	<u>\$ -</u>	<u>\$ -</u>

Notes to the Schedule of Expenditures of Federal and State Awards:

Note 1. Basis of Presentation

The accompanying schedule of expenditures of federal and State awards includes all of the federal and State grant activity of Cape Fear Public Utility Authority and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations and the State Single Audit Implementation Act. Therefore, some amounts presented in schedule may differ from amounts presented in or used in the preparation of the basic financial statements.

Note 2. Loans Outstanding

During the year ended June 30, 2010, the Authority was approved for a loan from the State of North Carolina, Department of Environment and Natural Resources (DENR). The loan will be drawn down as expenditures are paid on a certain capital project, to a maximum of \$2,716,357. Half of the loan amount is subject to immediate principal forgiveness under an American Recovery and Reinvestment Act of 2009 (ARRA) program awarded by the Environmental Protection Agency (EPA) through the State Revolving Fund program administered by DENR. The remaining \$1,358,179 will be due in twenty equal, annual installments of \$67,909, commencing on May 1 immediately following the completion of the project. The loan does not bear interest. At June 30, 2011, \$661,089 of this loan had been drawn down of which \$330,545 is recorded as an outstanding loan as of June 30, 2011.

Supplemental Schedule - Statement of Revenues and Expenditures

Aquifer Storage Retrieval

Project No. 09W113

For the Period 07/01/2008 to 06/30/2011

Statement of Revenues

Source of Funds:

Federal Funds Received:

ARRA - DWSRF Revolving Loan \$ 330,545

ARRA - DWSRF Principal Forgiveness Loan 330,544

Federal Funds Not Yet Reimbursed:

ARRA - DWSRF Revolving Loan 138,884

ARRA - DWSRF Principal Forgiveness Loan 138,884

Total Sources of Funds \$ 938,857

Statement of Expenditures

Construction Cost

1. Sydnor Hydro Inc., Part A-Well Drilling \$ 585,705

Engineering Fees 293,903

Administrative Expense

1. NCDENR Closing Costs 54,327

2. Administration and Legal 4,621

4. Signage 301

Total Statement of Expenditures \$ 938,857

Note: Total expenditures as reported on the Schedule of Federal and State Awards were as follows:

Fiscal year ended June 30, 2010 \$ 380,407

Fiscal year ended June 30, 2011 558,450

\$ 938,857