

LINCOLN WATER SYSTEM

Financial Statements & Schedules

Fiscal Year Ended August 31, 2007



ANNUAL FINANCIAL REPORT

DEPARTMENT OF PUBLIC WORKS/UTILITIES

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WATER SYSTEM

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Lincoln Water System
August 31, 2007 and 2006

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Independent Accountants' Report on Financial Statements and Supplementary Information

The Honorable Mayor and Members of the City Council
Lincoln Water System
Lincoln, Nebraska

We have audited the accompanying basic financial statements of Lincoln Water System as of and for the years ended August 31, 2007 and 2006, as listed in the table of contents. These financial statements are the responsibility of Lincoln Water System's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements of the City of Lincoln, Nebraska Water System are intended to present the financial position, the changes in financial position and cash flows of only that portion of the City of Lincoln, Nebraska, that is attributable to the transactions of the Lincoln Water System. They do not purport to, and do not, present fairly the financial position of the City of Lincoln, Nebraska, as of August 31, 2007 and 2006, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Lincoln Water System as of August 31, 2007 and 2006, and its changes in financial position and cash flows for the years 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 November 28, 2007 on our consideration of Lincoln Water System's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The accompanying management's discussion and analysis is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on Lincoln Water System's basic financial statements. The accompanying supplementary information as listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information, except for that portion marked "Unaudited", on which we express no opinion, has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

BKD, LLP

November 28, 2007

LINCOLN WATER SYSTEM
Management's Discussion and Analysis

This Management's Discussion and Analysis of the Lincoln Water System's (the "System") financial performance provides an overview of the financial activities for the years ended August 31, 2007 and 2006. Please read this information in conjunction with the accompanying basic financial statements and notes to the financial statements.

Using This Annual Report

The System's financial statements consist of three statements – a balance sheet; a statement of revenues, expenses and changes in net assets; and a statement of cash flows. These statements provide information about the activities of the System, including resources held by the System but restricted for specific purposes by creditors, contributors, or enabling legislation. The System is accounted for as a business-type activity and presents its financial statements using the economic resources measurement focus and the accrual basis of accounting.

The Balance Sheet and Statement of Revenues, Expenses and Changes in Net Assets

The Balance Sheet and the Statement of Revenues, Expenses and Changes in Net Assets report information about the System's resources and its activities. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. Using the accrual basis of accounting means that all of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the System's net assets and changes in them. The System's total net assets – the difference between assets and liabilities – is one measure of the System's financial health or financial position. Over time, increases or decreases in the System's net assets are an indicator of whether its financial health is improving or deteriorating.

The Statement of Cash Flows

The Statement of Cash Flows reports cash receipts, cash payments and net changes in cash and cash equivalents resulting from four defined types of activities. It provides answers to such questions as where did cash come from, what was cash used for and what was the change in cash and cash equivalents during the reporting period.

The System's Net Assets

The System's net assets are the difference between its assets and liabilities reported in the Balance Sheet. The System's net assets increased by \$7,711,981 (3.42%) in 2007 over 2006 as shown in Table 1.

Financial Analysis

The following comparative condensed financial statements summarize Lincoln Water System's financial position and operating results for the years ended August 31, 2007, 2006, and 2005.

Table 1

Condensed Balance Sheets

	August 31		Variance	
	2007	2006	Dollars	Percent
Current assets	\$ 18,341,575	\$ 18,289,325	\$ 52,250	0.29%
Capital assets	260,778,290	250,025,768	10,752,522	4.30%
Restricted assets	26,185,342	31,429,446	(5,244,104)	-16.69%
Long-term investments	8,120,246	8,044,681	75,565	0.94%
Deferred charges	710,058	780,091	(70,033)	-8.98%
Total assets	314,135,511	308,569,311	5,566,200	1.80%
Current liabilities	12,025,855	8,511,529	3,514,326	41.29%
Long-term liabilities	69,174,307	74,834,414	(5,660,107)	-7.56%
Total liabilities	81,200,162	83,345,943	(2,145,781)	-2.57%
Net assets				
Invested in capital assets, net of related debt	204,223,192	199,305,348	4,917,844	2.47%
Restricted for debt service	205,715	253,434	(47,719)	-18.83%
Restricted for capital acquisition	2,203,158	1,573,744	629,414	39.99%
Unrestricted	26,303,284	24,090,842	2,212,442	9.18%
Total net assets	232,935,349	225,223,368	7,711,981	3.42%
Total liabilities and net assets	\$314,135,511	\$308,569,311	\$5,566,200	1.80%

Financial Highlights – Fiscal Year 2007

- Total assets at year-end were \$314,135,511 and exceeded total liabilities by \$232,935,349, which results in an improved positive accumulated net assets position.
- Current assets increased by \$52,250 (0.29%) due to unspent bond proceeds and operating profits being retained in working capital.
- Capital assets increased by \$10,752,522 (4.30%) due to major project additions, which included:
 - Water Distribution Main – approximately \$5,952,000
 - Selected Main Replacements – approximately \$4,691,000

Table 2**Condensed Balance Sheets**

	August 31		Variance	
	2006	2005	Dollars	Percent
Current assets	\$ 18,289,325	\$ 23,581,875	(\$5,292,550)	-22.44%
Capital assets	250,025,768	238,649,313	11,376,455	4.77%
Restricted assets	31,429,446	32,280,661	(851,215)	-2.64%
Long-term investments	8,044,681	8,190,046	(145,365)	-1.77%
Deferred charges	780,091	850,124	(70,033)	-8.24%
Total assets	308,569,311	303,552,019	5,017,292	1.65%
Current liabilities	8,511,529	8,054,443	457,086	5.67%
Long-term liabilities	74,834,414	80,366,311	(5,531,897)	-6.88%
Total liabilities	83,345,943	88,420,754	(5,074,811)	-5.74%
Net assets				
Invested in capital assets, net of related debt	199,305,348	191,109,551	8,195,797	4.29%
Restricted for debt service	253,434	249,875	3,559	1.42%
Restricted for capital acquisition	1,573,744	1,265,311	308,433	24.38%
Unrestricted	24,090,842	22,506,528	1,584,314	7.04%
Total net assets	225,223,368	215,131,265	10,092,103	4.69%
Total liabilities and net assets	\$308,569,311	\$303,552,019	\$5,017,292	1.65%

Financial Highlights – Fiscal Year 2006

- Total assets at year-end were \$308,569,311 and exceeded total liabilities by \$225,223,368 which results in an improved positive accumulated net assets position.
- Current assets decreased by \$5,292,550 (-22.44%) due to construction spending.
- Capital assets increased by \$11,376,455 (4.77%) due to major project additions, which included:
 - Pumping Stations – approximately \$1,789,000
 - Water Distribution Main – approximately \$4,960,000
 - Water Trans Pump Station & Mains – approximately \$472,000
 - Selected Main Replacements – approximately \$2,355,000
 - Wellfield & Water Treatment Plant – approximately \$1,796,000

Table 3

Condensed Statements of Revenues, Expenses, and Changes in Net Assets

	August 31		Variance	
	2007	2006	Dollars	Percent
Operating revenue				
Water revenue	\$24,566,224	\$25,082,457	(\$516,233)	-2.06%
Other revenue	683,408	564,750	118,658	21.01%
Total operating revenue	<u>25,249,632</u>	<u>25,647,207</u>	<u>(397,575)</u>	<u>-1.55%</u>
Operating expenses				
Supply, pumping and purification	11,815,384	11,385,602	429,782	3.77%
Transmission and distribution	7,068,748	6,879,966	188,782	2.74%
Accounting and collecting	864,001	906,679	(42,678)	-4.71%
Administrative and general	1,327,440	1,034,904	292,536	28.27%
Total operating expenses	<u>21,075,573</u>	<u>20,207,151</u>	<u>868,422</u>	<u>4.30%</u>
Operating income	4,174,059	5,440,056	(1,265,997)	-23.27%
Net nonoperating revenues (expenses)	117,642	(1,233,077)	1,350,719	-109.54%
Capital contributions	3,420,280	5,885,124	(2,464,844)	-41.88%
Change in net assets	<u>\$7,711,981</u>	<u>\$10,092,103</u>	<u>(\$2,380,122)</u>	<u>-23.58%</u>

Financial Highlights – Fiscal Year 2007

- Operating revenues decreased by \$397,575 (-1.55%) compared to 2006. This decrease was primarily due to the user fee increase of 7.00% that was implemented with the water billings beginning in February of 2007; however, there was a decrease in water sold because of amount of rain increased during fiscal year. Total water pumpage for 2007 was 12,795,850 gallons, 1,229,236,250 gallons less than the water pumpage for 2006.
- Operating expenses increased \$868,422 (4.30%) compared to 2006, in part due to increased employee benefit costs, electricity costs, and chemical costs.
- Net nonoperating revenues (expenses) provided a net increase in 2007 of \$1,350,719 compared to 2006 due to higher interest rates on investments and decreased interest expense. Developer capital contributions decreased approximately \$2,500,000 from 2006 to 2007 due to completion of fewer projects.

Table 4

Condensed Statements of Revenues, Expenses, and Changes in Net Assets

	August 31		Variance	
	2006	2005	Dollars	Percent
Operating revenue				
Water revenue	\$25,082,457	\$23,826,036	\$1,256,421	5.27%
Other revenue	564,750	536,138	28,612	5.34%
Total operating revenue	<u>25,647,207</u>	<u>24,362,174</u>	<u>1,285,033</u>	<u>5.27%</u>
Operating expenses				
Supply, pumping and purification	11,385,602	10,627,425	758,177	7.13%
Transmission and distribution	6,879,966	6,594,266	285,700	4.33%
Accounting and collecting	906,679	872,292	34,387	3.94%
Administrative and general	1,034,904	1,072,166	(37,262)	-3.48%
Total operating expenses	<u>20,207,151</u>	<u>19,166,149</u>	<u>1,041,002</u>	<u>5.43%</u>
Operating income	5,440,056	5,196,025	244,031	4.70%
Net nonoperating expenses	(1,233,077)	(1,844,312)	611,235	-33.14%
Capital contributions	5,885,124	5,231,057	654,067	12.50%
Change in net assets	<u>\$10,092,103</u>	<u>\$8,582,770</u>	<u>\$1,509,333</u>	<u>17.59%</u>

Financial Highlights – Fiscal Year 2006

- Operating revenues increased by \$1,285,033 (5.27%) compared to 2005. This increase was primarily due to the user fee increase of 7.00% that was implemented with the water billings beginning in February of 2006 and increased water usage. Total water pumpage for 2006 was 14,025,100,000 gallons, 203,680,000 gallons more than the water pumpage for 2005.
- Operating expenses increased \$1,041,002 (5.43%) compared to 2005, due to power, pumping and purification, and transmission and distribution costs being higher than last fiscal year. No one item increased substantially. All operating expense categories increased by a relatively small amount, causing the over all increase.

Debt Activity

In November 2004, the Lincoln Water System issued \$40,000,000 in Water Revenue Bonds at an interest rate of 4.3%.

In connection with its bond issues the System is required, among other things, to maintain certain financial conditions and the System's ability to issue new debt is restricted.

System Credit and Bond Ratings

The outstanding revenue bonds of the System are currently rated by Standard & Poor's and Moody's. This rating takes into account the amount of unrestricted net assets maintained by the System, to which the revenue bonds' obligation of the System is pledged. Currently, the credit rating received from Standard & Poor's Rating Services is AA-. The credit rating issued by Moody's Rating Services is Aa2.

Commitments and Contingencies

Lincoln Water System has commitments under major construction contracts in progress of approximately \$9,166,000 at August 31, 2007.

Forward-Looking Information

The approved Capital Improvement Program for Fiscal Year 2007/08 -2012/13 identifies the need for \$106,865,000 to fund capital improvements for the Water System. Approximately \$56,367,000 of that total is projected to be funded by revenue bonds. Future user fee increases will be necessary to make the necessary improvements possible.

Contact Information

This financial report is intended to provide users with a general overview of the System's financial performance for 2007 and 2006. If you have questions about this report or need additional financial information, please contact the Business Office of the Public Works & Utilities Department at 555 South 10th Street, Lincoln, NE 68508.

LINCOLN WATER SYSTEM

Balance Sheets

August 31, 2007 and 2006

Assets	2007	2006
Current assets:		
Equity in pooled cash and investments	\$ 7,012,925	6,352,912
Receivables:		
Accounts receivable	2,765,516	2,893,615
Unbilled revenues	3,497,537	3,261,410
Impact fees	2,203,158	1,573,744
Due from other funds	2,039,588	3,346,976
Total receivables	10,505,799	11,075,745
Inventories	822,851	860,668
Total current assets	18,341,575	18,289,325
Noncurrent assets:		
Restricted assets:		
Equity in pooled cash and investments	26,185,342	31,429,446
Investments	8,120,246	8,044,681
Total restricted assets	34,305,588	39,474,127
Utility plant	346,195,887	328,980,562
Less accumulated depreciation	85,417,597	78,954,794
Net utility plant	260,778,290	250,025,768
Unamortized bond issuance costs	710,058	780,091
Total noncurrent assets	295,793,936	290,279,986
Total assets	\$ 314,135,511	308,569,311
Liabilities and Net Assets		
Current liabilities:		
Accounts payable	\$ 540,974	661,384
Accrued liabilities	1,017,356	563,253
Deposits liability	93,000	101,800
Accrued compensated absences	350,348	306,575
Construction contracts	4,326,913	1,386,369
Current maturities of long-term debt	5,555,000	5,340,000
Accrued interest	142,264	152,148
Total current liabilities:	12,025,855	8,511,529
Long-term liabilities:		
Long-term debt, excluding current maturities	68,835,091	74,590,829
Accrued compensated absences	339,216	243,585
Total long-term liabilities	69,174,307	74,834,414
Total liabilities	81,200,162	83,345,943
Net assets:		
Invested in capital assets, net of related debt	204,223,192	199,305,347
Restricted for debt service	205,715	253,434
Restricted for capital acquisition	2,203,158	1,573,744
Unrestricted	26,303,284	24,090,843
Total net assets	232,935,349	225,223,368
Total liabilities and net assets	\$ 314,135,511	308,569,311

See accompanying notes to financial statements.

LINCOLN WATER SYSTEM

Statements of Revenues, Expenses and Changes in Net Assets

Years ended August 31, 2007 and 2006

	2007	2006
Operating revenues:		
Water sales	\$ 24,566,224	25,082,457
Service and materials, net	683,408	564,750
Total operating revenues	25,249,632	25,647,207
Operating expenses:		
Supply, pumping and purification	11,815,384	11,385,602
Transmission and distribution	7,068,748	6,879,966
Accounting and collecting	864,001	906,679
Administrative and general	1,327,440	1,034,904
Total operating expenses	21,075,573	20,207,151
Operating income	4,174,059	5,440,056
Nonoperating revenues (expenses):		
Investment income	2,587,058	1,697,768
Interest expense on revenue bonds	(2,399,383)	(2,860,812)
Amortization of bond costs	(70,033)	(70,033)
Net nonoperating revenues (expenses)	117,642	(1,233,077)
Increase in net assets before capital contributions	4,291,701	4,206,979
Capital contributions from:		
Developers	1,870,475	4,215,100
Impact fees	1,133,595	1,147,976
Tap fees	416,210	522,048
Total capital contributions	3,420,280	5,885,124
Increase in net assets	7,711,981	10,092,103
Total net assets - beginning	225,223,368	215,131,265
Total net assets - ending	\$ 232,935,349	225,223,368

See accompanying notes to financial statements.

LINCOLN WATER SYSTEM

Statements of Cash Flows

Years ended August 31, 2007 and 2006

	2007	2006
Operating activities:		
Receipts from customers and users	\$ 24,503,390	25,654,701
Payments to suppliers	(6,825,121)	(7,002,626)
Payments to employees	(7,015,101)	(7,269,902)
Net cash provided by operating activities	10,663,168	11,382,173
Non capital financing activities:		
Repayment from (advance to) other funds, net	1,307,388	(81,242)
Net cash provided by (used in) non capital financing activities:	1,307,388	(81,242)
Capital and related financing activities:		
Acquisition and construction of capital assets	(11,116,135)	(11,292,597)
Principal paid on revenue bonds	(5,340,000)	(5,130,000)
Interest paid on revenue bonds	(2,610,005)	(3,070,863)
Net cash used in capital and related financing activities	(19,066,140)	(19,493,460)
Investing activities:		
Purchases of investments	(13,730,491)	(2,721,141)
Proceeds from investment maturities	19,548,800	3,393,784
Interest on investments	1,937,288	2,021,705
Net cash provided by investing activities	7,755,597	2,694,348
Net increase (decrease) in cash and cash equivalents	660,013	(5,498,181)
Cash and cash equivalents at beginning of year	6,352,912	11,851,093
Cash and cash equivalents at end of year	\$ 7,012,925	6,352,912
Reconciliation of net operating income to net cash provided by operating activities:		
Operating income	\$ 4,174,059	5,440,056
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	6,724,437	6,398,937
Changes in operating assets and liabilities:		
Accounts receivable	(737,442)	(156)
Inventories	37,817	(124,233)
Accounts payable	(120,410)	(178,713)
Accrued liabilities and deposit liability	445,303	(182,350)
Accrued compensated absences	139,404	28,632
Total adjustments	6,489,109	5,942,117
Net cash provided by operating activities	\$ 10,663,168	11,382,173

Supplemental disclosure of noncash transactions:

Contributed capital improvements of \$1,870,475 and \$4,215,100 were added to utility plant in 2007 and 2006, respectively.

Accounts payable incurred for utility plant purchases were \$4,326,913 and \$1,386,369 in 2007 and 2006, respectively.

See accompanying notes to financial statements.

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

(1) Organization and Summary of Significant Accounting Policies

Organization and Nature of Operations

Lincoln Water System is a public utility accounted for as an enterprise fund by the City of Lincoln, Nebraska (City). Lincoln Water System (System) is operated under the direction of the Mayor and City Council. The authority to adopt the annual budget, to incur debt and to fix rates and charges is vested in the City Council by the Charter of the City of Lincoln. As the Lincoln Water System is a part of the City, it is exempt from federal income tax.

Measurement Focus and Basis of Accounting

The financial statements of the Lincoln Water System are prepared on the accrual basis of accounting using the economic resources measurement focus. Lincoln Water System follows the uniform system of accounts as prescribed by the National Association of Regulatory Utility Commissioners. In reporting financial activity, Lincoln Water System applies all applicable Government Accounting Standards Board (GASB) pronouncements, as well as Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins, that do not conflict with or contradict GASB pronouncements.

The financial statements referred to above present only the Lincoln Water System and do not purport to, and do not, present fairly the financial position of the City of Lincoln, Nebraska, as of August 31, 2007 and 2006, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The System first applies restricted net assets when an expense or outlay is incurred for purposes for which both restricted and unrestricted net assets are available.

Operating Revenues and Expenses

As an enterprise fund, the Lincoln Water System distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Lincoln Water System's principal ongoing operations. The principal operating revenues of the Lincoln Water System are charges to customers for sales and services. Operating expenses 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.

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

Utility Plant (Capital Assets)

Cost of additions and replacements to utility plant are capitalized. Cost includes labor, materials, payments to contractors, equipment use and indirect costs. Interest expense, net of interest earned on unspent bond proceeds, is capitalized in connection with the construction of major assets. The capitalized interest is recorded as part of the asset to which it relates and is amortized over the asset's estimated useful life. Contributed assets are capitalized at their fair value at the date of contribution. The cost of property retired, together with removal cost, less salvage, is charged to accumulated depreciation at such time as property is removed from service, except for land, on which gain or loss is recognized upon disposition. Expenditures for maintenance and repairs are charged to current expenses.

Depreciation expense is calculated on the straight-line method over the estimated useful lives of the assets. Depreciation expense recognized on contributed assets is charged to operations in accordance with similar utility assets.

The following estimated useful lives are being used by the System:

Buildings and improvements	5 - 50 years
Infrastructure	33 - 100 years
Furniture, fixtures and equipment	5 - 15 years

Deposits and Investments

The City Treasurer is responsible for the safekeeping of cash and invested funds of Lincoln Water System. The City is authorized to invest in "certificates of deposit, time deposits, and any securities in which the State investment officer is authorized to invest pursuant to the Nebraska Capital Expansion Act and the Nebraska State Funds Investment Act and as provided in the authorized investment guidelines of the Nebraska Investment Council in effect on the date the investment is made." Cash balances in excess of current requirements are invested along with funds from other governmental bodies, and the interest earned on these investments is allocated monthly to the various governmental bodies by the City Treasurer on a pro rata basis of aggregate monthly balances.

For purposes of the Statements of Cash Flows, Lincoln Water System considers cash on hand and in the bank, as well as cash and equity in pooled cash and investments held by the City Treasurer, which are readily convertible to known amounts of cash and have original maturities of three months or less, to be cash and cash equivalents.

The System participates in a cash management pool, managed by the City. The pool consists of bank deposits and investments. The System's interest in this pool is shown as equity in pooled cash and investments in the balance sheets.

Fair value of the equity in the pool is the same as the value of the pool shares determined using the fair value of the pool's underlying investment portfolio.

Investment income includes interest income and the net change for the year in the fair value of investments carried at fair value.

U.S. government and government agency securities are carried at fair value as determined based on quoted market price. Collateralized investment agreements are carried at contract value.

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LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

Capital Contributions

Developer contributions are water improvements made to developments. Revenues from developer contributions are recorded at fair value when the development is complete. These are considered imposed non-exchange transactions.

Unamortized Premium on Revenue Bonds

The premiums received on bond issuances are being amortized over the life of the bonds using the interest method.

Inventories

Inventories of materials and supplies are stated at the lower of cost or market. Cost is generally determined on a weighted-average basis.

Revenues

Water usage is billed on a two-month cycle for substantially all customers. Unbilled revenues, representing estimated consumer usage for the period between the last billing date and the end of the period, are accrued in the period of consumption.

The City Council sets the rate schedule for the Lincoln Water System. The following rates were assessed per one hundred cubic feet of water usage for the years ended August 31, 2007 and 2006:

	<u>August 31, 2007</u>	<u>August 31, 2006</u>
<u>Water Usage</u>		
Residential:		
100 to 800 cubic feet	\$ 1.05	\$.995
801 to 2,300 cubic feet	1.48	1.38
2,301 and up	2.28	2.10
Nonresidential low volume user:		
100 to 8,000 cubic feet	1.05	.995
8,001 and up	1.48	1.38
Nonresidential high volume user:		
Base usage which is average water usage for previous three calendar years	1.00 to 1.13	.935 to 1.065
<u>Service Charge</u>		
Residential: single-family dwelling unit	\$ 2.95	\$ 2.95
Residential: multiple-family dwelling unit	1.81	1.81
Non-residential:	Based on size and number of water meters or number of dwelling units.	

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

Bond Issuance Costs

The issuance costs on the revenue bonds are amortized using the straight-line method over the terms of the related issues.

Net Assets Classification

Net assets are required to be classified into three components - invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

Invested in capital assets, net of related debt - This component of net assets consists of capital assets, net of accumulated depreciation, and unamortized bond issuance costs reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested in capital assets, net of related debt.

Restricted - This component of net assets consists of constraints placed on net assets use through external constraints imposed by creditors (such as through debt covenants), contributors, or law or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted - This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

Compensated Absences

Employees earn vacation days at varying rates dependent on years of service. In the event of termination, an employee is reimbursed for accumulated vacation time up to a maximum allowed accumulation which is in no case longer than 35 days. Employees earn sick leave at the rate of approximately one day per month. Upon retirement or death, an employee or their beneficiary is reimbursed for one-fourth or up to one-half of accumulated sick leave, which may in some cases be placed directly in a medical spending account instead of reimbursing the employee directly. The Lincoln Water System accrues for vacation, sick leave and other compensated absences with similar characteristics.

Compensated absences of the Lincoln Water System at August 31, 2007 and 2006 are summarized below:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
August 31, 2007	\$550,160	445,979	306,575	689,564	350,348
August 31, 2006	521,528	315,417	286,785	550,160	306,575

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

Use of Estimates

Management of Lincoln Water System has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets, liabilities, and revenues to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to the 2006 financial statements to conform to the 2007 financial statement presentation. These reclassifications had no effect on the change in net assets.

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

(2) Deposits, Investments, and Investment Return

Deposits

State statutes require banks either to give bond or to pledge government securities to the City Treasurer in the amount of the City's deposits. The System has been allocated a portion of the City's pooled cash and investments. The City's cash deposits, including certificates of deposit, are insured up to \$100,000 by the Federal Deposit Insurance Corporation (FDIC). Any cash deposits or certificates of deposit in excess of the \$100,000 FDIC limits are covered by collateral held in a Federal Reserve pledge account or by an agent for the City and thus no custodial risk exists.

Investments

The City may legally invest in direct obligations of and other obligations guaranteed as to principal by the U.S. Treasury and U.S. agencies and instrumentalities and in bank repurchase agreements. It may also invest to a limited extent in corporate bonds, bankers' acceptances, and collateralized investment agreements.

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the City will not be able to recover the value of its investment securities that are in the possession of an outside party. None of the underlying securities for the Lincoln Water System's investments at August 31, 2007 and 2006 are subject to custodial credit risk, as they are held in an account in the Lincoln Water System's name, and by an agent who is not the counterparty to the investment transactions.

At August 31, 2007 and 2006, the Lincoln Water System had the following investments and maturities:

Type	August 31, 2007			
	Carrying Value	Maturities in Years		
		1-5	6-10	More than 10
U.S. Treasury obligations	\$3,190,246	3,190,246	—	—
Collateralized Investment Agreement	<u>4,930,000</u>	<u>—</u>	<u>—</u>	<u>4,930,000</u>
	<u>\$8,120,246</u>	<u>3,190,246</u>	<u>—</u>	<u>4,930,000</u>

Type	August 31, 2006			
	Carrying Value	Maturities in Years		
		1-5	6-10	More than 10
U.S. Treasury obligations	\$3,114,681	—	3,114,681	—
Collateralized Investment Agreement	<u>4,930,000</u>	<u>—</u>	<u>—</u>	<u>4,930,000</u>
	<u>\$8,044,681</u>	<u>—</u>	<u>3,114,681</u>	<u>4,930,000</u>

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

Interest Rate Risk:

As a means of limiting its exposure to fair value losses arising from rising interest rates, the City's investment policy limits current operating funds to be invested with maturities of no longer than twenty-four months. Fixed income investments in construction funds, operating funds, and other non-operating funds are limited to ten year maturities. Collateralized Investment Agreements are not subject to interest rate risk, as the interest rate is guaranteed by the issuer.

Credit Risk:

Credit Risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. The City's investment policy allows Investment Agreements with a rating at least Aa3 by Moody's Investor Service and AA- by Standard and Poor's. As of August 31, 2007 and 2006, the Lincoln Water System collateralized investment agreements were rated Aa2 by Moody's Investors Service and AA by Standard and Poor's.

Concentration of Credit Risk:

The City's Investment Policy places various limits on the amount that may be invested in any one issuer. Per the Policy, allocation limits do not apply to the investment of debt proceeds. These investments shall be governed by the debt covenant included in the debt instrument. As of August 31, 2007 and 2006, the Lincoln Water System collateralized investment agreements constituted 11% of its total funds available for investing. These collateralized investment agreements were made with funds from the bond debt reserve funds established.

The carrying amount of equity interests in pooled cash and investments at August 31, 2007 and 2006 are:

	<u>2007</u>	<u>2006</u>
Equity in Pooled cash and investments	<u>\$33,198,267</u>	<u>\$37,782,358</u>

Investment Income

Investment income for the years ended August 31, 2007 and 2006 consisted of:

	<u>2007</u>	<u>2006</u>
Interest and dividend income	\$1,956,619	\$2,020,880
Net increase (decrease) in fair value of investments	<u>630,439</u>	<u>(323,112)</u>
	<u>\$2,587,058</u>	<u>\$1,697,768</u>

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

(3) Inventories

Balances of the major classes of inventory at August 31, 2007 and 2006, are shown below:

	2007	2006
Heavy materials	\$549,450	672,209
Diesel fuel	96,461	70,979
Water meters and parts	150,728	91,348
Chemicals	26,212	26,132
Total inventories	\$822,851	860,668

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

(4) Utility Plant

Utility plant is summarized by major classification at August 31, 2007 as follows:

Asset Class	Capital Assets				Accumulated Depreciation				Net Capital Assets
	August 31, 2006	Increases	Decreases	August 31, 2007	August 31, 2006	Increases	Decreases	August 31, 2007	August 31, 2007
Airport	\$ 42,172	-	-	42,172	(24,479)	(422)	-	(24,901)	17,271
Structures and improvements	94,771,662	332,301	-	95,103,963	(23,242,487)	(2,133,162)	-	(25,375,649)	69,728,314
Other power and production equipment	1,893,984	-	-	1,893,984	(1,276,634)	(62,958)	-	(1,339,592)	554,392
Electric pumping equipment	25,288,931	104,007	-	25,392,938	(6,272,035)	(901,075)	-	(7,173,110)	18,219,828
Purification system	25,909,954	14,438	-	25,924,392	(7,977,540)	(781,837)	-	(8,759,377)	17,165,015
Transmission mains	51,213,065	116,666	-	51,329,731	(10,802,545)	(608,139)	-	(11,410,684)	39,919,047
Distribution mains and accessories	98,176,008	13,089,197	-	111,265,205	(18,725,698)	(1,144,610)	-	(19,870,308)	91,394,897
Hydrants	4,844,227	-	-	4,844,227	(2,922,953)	(140,534)	-	(3,063,487)	1,780,740
Office furniture and equipment	1,615,597	265,963	-	1,881,560	(1,267,504)	(141,125)	-	(1,408,629)	472,931
Shop equipment	179,277	35,364	-	214,641	(173,617)	(2,827)	-	(176,444)	38,197
Laboratory equipment	321,974	30,360	-	352,334	(183,364)	(44,068)	-	(227,432)	124,902
Tools and work equipment	599,011	-	(56,552)	542,459	(512,732)	(19,488)	56,552	(475,668)	66,791
Communications system	382,220	-	-	382,220	(167,423)	(18,072)	-	(185,495)	196,725
Meters	12,033,015	65,289	(194)	12,098,110	(3,959,684)	(544,700)	194	(4,504,190)	7,593,920
Vehicles	2,423,501	57,219	(209,248)	2,271,472	(1,446,099)	(181,420)	204,888	(1,422,631)	848,841
Total depreciable assets	319,694,598	14,110,804	(265,994)	333,539,408	(78,954,794)	(6,724,437)	261,634	(85,417,597)	248,121,811
Land and land rights	4,712,330	-	(153)	4,712,177	-	-	-	-	4,712,177
Construction in progress	4,573,634	15,152,747	(11,782,079)	7,944,302	-	-	-	-	7,944,302
Total nondepreciable assets	9,285,964	15,152,747	(11,782,232)	12,656,479	-	-	-	-	12,656,479
Total capital assets	\$ 328,980,562	29,263,551	(12,048,226)	346,195,887	(78,954,794)	(6,724,437)	261,634	(85,417,597)	260,778,290

During 2007, Lincoln Water System incurred \$3,473,462 of interest cost. Interest capitalized into construction in progress during 2007 was \$1,001,995. Capitalized interest is added to the cost of the underlying assets and is amortized over the useful lives of the assets.

The composite depreciation rate was approximately 2.02% in 2007.

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

(4) Utility Plant

Utility plant is summarized by major classification at August 31, 2006 as follows:

Asset Class	Capital Assets				Accumulated Depreciation				Net Capital Assets
	August 31, 2005	Increases	Decreases	August 31, 2006	August 31, 2005	Increases	Decreases	August 31, 2006	August 31, 2006
Airport	\$ 42,172	-	-	42,172	(24,057)	(422)	-	(24,479)	17,693
Structures and improvements	91,667,071	3,104,591	-	94,771,662	(21,230,527)	(2,011,960)	-	(23,242,487)	71,529,175
Other power and production equipment	1,893,984	-	-	1,893,984	(1,213,441)	(63,193)	-	(1,276,634)	617,350
Electric pumping equipment	23,081,445	2,207,486	-	25,288,931	(5,399,379)	(872,656)	-	(6,272,035)	19,016,896
Purification system	25,903,189	6,765	-	25,909,954	(7,189,569)	(787,971)	-	(7,977,540)	17,932,414
Transmission mains	50,799,666	413,399	-	51,213,065	(10,203,601)	(598,944)	-	(10,802,545)	40,410,520
Distribution mains and accessories	84,046,715	14,130,622	(1,329)	98,176,008	(17,722,390)	(1,004,637)	1,329	(18,725,698)	79,450,310
Hydrants	4,844,227	-	-	4,844,227	(2,776,422)	(146,531)	-	(2,922,953)	1,921,274
Office furniture and equipment	1,693,032	44,145	(121,580)	1,615,597	(1,276,206)	(112,878)	121,580	(1,267,504)	348,093
Shop equipment	193,975	-	(14,698)	179,277	(184,579)	(3,736)	14,698	(173,617)	5,660
Laboratory equipment	402,090	32,217	(112,333)	321,974	(247,357)	(48,340)	112,333	(183,364)	138,610
Tools and work equipment	577,704	26,683	(5,376)	599,011	(496,286)	(21,822)	5,376	(512,732)	86,279
Communications system	382,220	-	-	382,220	(148,688)	(18,735)	-	(167,423)	214,797
Meters	11,473,920	609,229	(50,134)	12,033,015	(3,486,445)	(523,373)	50,134	(3,959,684)	8,073,331
Vehicles	2,383,442	99,356	(59,297)	2,423,501	(1,317,928)	(183,739)	55,568	(1,446,099)	977,402
Total depreciable assets	299,384,852	20,674,493	(364,747)	319,694,598	(72,916,875)	(6,398,937)	361,018	(78,954,794)	240,739,804
Land and land rights	4,712,330	-	-	4,712,330	-	-	-	-	4,712,330
Construction in progress	7,469,006	13,057,495	(15,952,867)	4,573,634	-	-	-	-	4,573,634
Total nondepreciable assets	12,181,336	13,057,495	(15,952,867)	9,285,964	-	-	-	-	9,285,964
Total capital assets	\$ 311,566,188	33,731,988	(16,317,614)	328,980,562	(72,916,875)	(6,398,937)	361,018	(78,954,794)	250,025,768

During 2006, Lincoln Water System incurred \$3,624,251 of interest cost. Interest capitalized into construction in progress during 2006 was \$763,439. Capitalized interest is added to the cost of the underlying assets and is amortized over the useful lives of the assets.

The composite depreciation rate was approximately 2.00% in 2006.

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

(5) Long-term Debt

Long-term debt of the Lincoln Water System at August 31, 2007 and 2006 is summarized below:

2007

Type of Debt	August 31, 2006	Additions	Reductions	August 31, 2007	Due Within One Year
2.75%-5.00% Water Revenue Bonds, Series 2002, due in annual principal installments on August 15, increasing from \$805,000 in 2008 to the final payment of \$1,465,000 on August 15, 2022.	\$17,020,000	-	780,000	16,240,000	805,000
5% Water Revenue Bonds, Refunding Series 2003, due in annual principal installments on August 15, increasing from \$3,755,000 in 2008 to the final payment of \$2,630,000 on August 15, 2012.	22,380,000	-	3,585,000	18,795,000	3,755,000
3.00%-5.00% Water Revenue Bonds, Series 2004, due in annual principal installments on August 15, increasing from \$995,000 in 2008 to the final payment of \$3,065,000 on August 15, 2025.	38,150,000	-	975,000	37,175,000	995,000
Unamortized premium on bonds Deferred for refunding	3,189,472 (808,643)	- -	336,454 (135,716)	2,853,018 (672,927)	- -
	<u>\$79,930,829</u>	<u>-</u>	<u>5,540,738</u>	<u>74,390,091</u>	<u>5,555,000</u>

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

(5) Long-term Debt, (continued)

2006

Type of Debt	August 31, 2005	Additions	Reductions	August 31, 2006	Due Within One Year
2.75%-5.00% Water Revenue Bonds, Series 2002, due in annual principal installments on August 15, increasing from \$780,000 in 2007 to the final payment of \$1,465,000 on August 15, 2022.	\$17,775,000	-	755,000	17,020,000	780,000
5% Water Revenue Bonds, Refunding Series 2003, due in annual principal installments on August 15, increasing from \$3,585,000 in 2007 to the final payment of \$2,630,000 on August 15, 2012.	25,800,000	-	3,420,000	22,380,000	3,585,000
3.00%-5.00% Water Revenue Bonds, Series 2004, due in annual principal installments on August 15, increasing from \$975,000 in 2007 to the final payment of \$3,065,000 on August 15, 2025.	39,105,000	-	955,000	38,150,000	975,000
Unamortized premium on bonds	3,525,928	-	336,456	3,189,472	-
Deferred for refunding	(944,360)	-	(135,717)	(808,643)	-
	<u>\$85,261,568</u>	<u>-</u>	<u>5,330,739</u>	<u>79,930,829</u>	<u>5,340,000</u>

In connection with these bond issues the System is required, among other things, to maintain certain financial conditions and the System's ability to issue new debt is restricted.

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

(5) Long-term Debt, (continued)

The net revenues derived from the operations of Lincoln Water System and any future extensions, additions and improvements to the waterworks system are pledged as security for the revenue bonds.

Maturities and sinking fund requirements on long-term debt at August 31, 2007 are as follows:

Years ending August 31	Principal	Interest	Total
2008	\$ 5,555,000	3,376,200	8,931,200
2009	5,795,000	3,128,414	8,923,414
2010	6,050,000	2,873,677	8,923,677
2011	6,310,000	2,602,526	8,912,526
2012	5,380,000	2,315,309	7,695,309
2013-2017	15,375,000	8,874,633	24,249,633
2018-2022	18,950,000	4,745,480	23,695,480
2023-2025	8,795,000	803,472	9,598,472
Total	\$72,210,000	28,719,711	100,929,711

(6) Commitments and Contingencies

Lincoln Water System has commitments under major construction contracts in progress of approximately \$9,166,000 at August 31, 2007.

The Lincoln Water System has entered into various agreements with developers to be reimbursed for eligible infrastructure construction. After construction is substantially complete, the developer will be reimbursed by the System on a quarterly basis from impact fee dollars collected within that development area. These agreements project construction costs and impact fee revenue based on the final plat at the time of acceptance of the agreement. As of August 31, 2007, the System's commitment to these developers is estimated to be approximately \$884,000.

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

(7) Disclosure About the Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

- *Cash, accounts receivable and accounts payable* - The carrying amount approximates fair value because of the short maturity of these instruments.
- *Long-term debt* - The estimated fair value of the System's long-term debt is approximately \$73,866,000 based on borrowing rates currently available as of August 31, 2007.
- *Investments* - The fair values of investments are based on quoted market prices for those investments as shown in Note 2.

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

(8) Related Party Transactions

The City billed the Water System approximately \$467,000 and \$420,000 for administrative services during 2007 and 2006, respectively.

A special revenue fund of the City collects and holds impact fees until they are disbursed in accordance with City ordinance. The Lincoln Water System was due impact fees of \$2,203,158 and \$1,573,744 as of August 31, 2007 and 2006, respectively.

The City of Lincoln general fund has borrowed moneys from the pooled cash and investment account. The Water System's allocated share of the borrowing was \$2,039,588 and \$3,346,976 as of August 31, 2007 and 2006, respectively. This amount is reflected as a current asset and is included in Due from Other Funds on the balance sheets.

(Continued)

LINCOLN WATER SYSTEM

Notes to Financial Statements

August 31, 2007 and 2006

(9) Risk Management

Lincoln Water System participates in the City's self-insurance program administered by the City's Risk Management Division (the Division). The City 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. On behalf of the City, the Division purchases insurance and administers funds for its self-insured program. The Division maintains a workers' compensation fund and a self-insurance loss fund. The Division provides first dollar coverage for all liability and workers' compensation exposure with insurance acting as an umbrella or excess coverage. The maximum exposure would be the deductible amounts for property and auto physical damage, as well as losses not covered by insurance. Lincoln Water System had no claims or judgments exceeding the policy limits during each of the last three prior years. Budgeted premium amounts charged to Lincoln Water System are placed in the appropriate fund maintained by the Division. Premium expense was approximately \$261,000 and \$243,000 in 2007 and 2006, respectively.

(10) Pension Plan

Employees of Lincoln Water System are participants in the City of Lincoln Employees' Retirement Plan. Plan participation is required if the employee has completed five years of continuous service and attained the age of 40. An employee may voluntarily enter the plan upon attaining age 19 and after completing six months of service. The plan is a defined contribution plan requiring employees to contribute 3% of earnings on the first \$4,800 and 6% on the balance of earnings. Lincoln Water System contributes \$2 for every \$1 contributed by the employees. Plan participants vest in the City's contributions in year three of participation at 20%, up to 100% vesting in year seven. All past service costs and vested benefits are fully paid. Contributions made by the System were approximately \$567,000 and \$560,000 for 2007 and 2006, respectively. Contributions made by the plan members were approximately \$307,000 and \$304,000 for 2007 and 2006, respectively.

LINCOLN WATER SYSTEM

Schedule 1

Summary of Long-Term Debt

August 31, 2007

Due years ending August 31	Series 2002		Series 2003		Series 2004		Total		
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Total
2008	\$ 805,000	732,470	3,755,000	939,750	995,000	1,703,980	5,555,000	3,376,200	8,931,200
2009	835,000	702,282	3,940,000	752,000	1,020,000	1,674,132	5,795,000	3,128,414	8,923,414
2010	865,000	675,145	4,135,000	555,000	1,050,000	1,643,532	6,050,000	2,873,677	8,923,677
2011	895,000	644,870	4,335,000	348,250	1,080,000	1,609,406	6,310,000	2,602,526	8,912,526
2012	930,000	612,203	2,630,000	131,500	1,820,000	1,571,606	5,380,000	2,315,309	7,695,309
2013-2017	5,250,000	2,447,853	-	-	10,125,000	6,426,780	15,375,000	8,874,633	24,249,633
2018-2022	6,660,000	1,031,500	-	-	12,290,000	3,713,980	18,950,000	4,745,480	23,695,480
2023-2025	-	-	-	-	8,795,000	803,472	8,795,000	803,472	9,598,472
	\$ 16,240,000	6,846,323	18,795,000	2,726,500	37,175,000	19,146,888	72,210,000	28,719,711	100,929,711

Operating Expenses

Years ended August 31, 2007 and 2006

	2007	2006
Lincoln Water Plant:		
Source of supply expenses:		
Supervision, management and administrative support	\$ 47,205	46,323
Electrical maintenance	-	451
Grounds maintenance	8,009	8,320
Wellfield maintenance	23,676	22,200
Wellfield operations	5,367	8,257
Depreciation of wells and houses	16,697	16,245
Total source of supply	\$ 100,954	101,796
Power and pumping expenses:		
Supervision, management and administrative support	\$ 93,576	94,307
Training and education	25,111	29,559
Data management	7,267	6,997
General operations	137,425	117,900
Structures maintenance	35,998	14,748
Control system maintenance	51,531	50,745
Electrical maintenance	126,474	121,189
Grounds maintenance	305,870	243,572
Main repair/maintenance	3,255	10,453
Customer services	26,368	33,920
Laboratory operations	46,907	47,507
Pumping and transmission maintenance	117,821	171,432
Pumping and transmission operations	1,826,773	1,853,246
Depreciation of pumping equipment	336,568	308,422
Depreciation of general plant and improvements	13,360	15,091
Depreciation of structures and improvement	835,039	820,748
Total power and pumping	\$ 3,989,343	3,939,836
Total - Lincoln Water Plant	\$ 4,090,297	4,041,632
Ashland Water Plant:		
Source of supply expenses:		
Supervision, management and administrative support	\$ 129,304	116,944
Control system maintenance	49,394	32,764
Electrical maintenance	42,418	26,687
Grounds maintenance	101,504	94,251
Main repair/maintenance	29,196	4,154
Laboratory operations	17,604	12,530
Wellfield maintenance	189,477	158,263
Wellfield operations	781,988	726,946
Depreciation of transmission mains	260,420	258,369
Depreciation of wells and houses	796,185	767,640
Total source of supply	\$ 2,397,490	2,198,548

Operating Expenses

	2007	2006
Power and pumping expenses:		
Supervision, management and administrative support	\$ 111,506	105,637
General operations	5,908	6,981
Control system maintenance	25,833	6,871
Electrical maintenance	30,042	20,950
Grounds maintenance	3,335	-
Main repair/maintenance	6,069	814
Pumping and transmission maintenance	51,313	45,607
Pumping and transmission operations	211,852	265,152
Depreciation of pumping equipment	295,929	296,877
Depreciation of structures and improvement	159,218	159,218
Depreciation of general plant	1,929	1,929
Depreciation of transmission mains	2,243	2,243
Depreciation of other production equipment	62,958	63,194
Total power and pumping	\$ 968,135	975,473
Purification expense:		
Supervision, management and administrative support	\$ 266,772	255,377
Training and education	50,640	74,908
General operations	88,935	96,087
Treatment and process control	116,782	104,696
Structures maintenance	11,295	15,179
Process equipment maintenance	69,331	50,585
Control system maintenance	95,784	122,729
Electrical maintenance	70,661	55,031
Grounds maintenance	597,722	593,030
Laboratory operations	328,680	358,782
Treatment operations	1,180,442	1,026,733
Depreciation of structures and improvements	612,542	533,619
Depreciation of purification equipment	781,837	787,971
Depreciation of general plant & equipment	88,039	95,222
Total purification expenses	\$ 4,359,462	4,169,949
Total Ashland Water Plant	\$ 7,725,087	7,343,970
Total supply, pumping and purification	\$ 11,815,384	11,385,602

Operating Expenses

	2007	2006
Transmission and distribution expenses:		
Supervision and management	\$ 915,035	817,833
Administrative and support staff	463,481	419,617
Training and education	116,620	176,935
Data management	332,896	342,347
General operations	304,880	287,515
Main repair/maintenance	1,245,120	1,281,240
Contractor services	203,191	146,483
Customer services	1,238,302	1,350,416
Depreciation of structures and improvements	1,033	1,033
Depreciation of transmission mains	343,905	336,761
Depreciation of distribution mains	1,683,525	1,522,025
Depreciation of hydrants and fountains	140,534	146,531
Depreciation of general plant and equipment	80,226	51,230
Total transmission and distribution	\$ 7,068,748	6,879,966
Accounting and collecting expenses:		
Supervision and management	\$ 166,903	219,688
Administrative and support staff	1,451	2,843
Meter reading	128,159	141,494
Billing and accounting	290,760	278,851
Collections	121,419	124,546
Customer services and billing	112,349	97,743
Customer contracts and orders	32,779	31,333
Depreciation of general plant and equipment	10,181	10,181
Total accounting and collecting	\$ 864,001	906,679
Administrative and general expenses:		
Supervision and management	\$ 1,203,851	958,048
Administrative and support staff	102,940	56,207
Depreciation of general plant and equipment	20,649	20,649
Depreciation of general plant structures	-	-
Total administrative and general	\$ 1,327,440	1,034,904

LINCOLN WATER SYSTEM

Schedule 3

Utility Plant in Service

August 31, 2007

Asset Class	Capital Assets				Accumulated Depreciation			Net Capital Assets	
	August 31, 2006	Increases	Decreases	August 31, 2007	August 31, 2006	Increases	Decreases	August 31, 2007	
Lincoln Water Plant:									
Airport	\$ 42,172	-	-	42,172	(24,479)	(422)	-	(24,901)	17,271
Structures and improvements	36,476,685	24,344	-	36,501,029	(11,906,112)	(851,866)	-	(12,757,978)	23,743,051
Other power and production equipment	-	-	-	-	-	-	-	-	-
Electric pumping equipment	13,930,990	104,007	-	14,034,997	(2,024,454)	(318,497)	-	(2,342,951)	11,692,046
Purification system	-	-	-	-	1,072	-	-	1,072	1,072
Transmission mains	29,217,865	181,812	-	29,399,677	(5,324,538)	(345,476)	-	(5,670,014)	23,729,663
Distribution mains and accessories	98,176,008	13,089,197	-	111,265,205	(18,725,698)	(1,144,610)	-	(19,870,308)	91,394,897
Hydrants	4,844,227	-	-	4,844,227	(2,922,953)	(140,534)	-	(3,063,487)	1,780,740
Office furniture and equipment	1,275,093	237,986	-	1,513,079	(1,006,516)	(99,369)	-	(1,105,885)	407,194
Shop equipment	161,326	35,364	-	196,690	(155,856)	(2,701)	-	(158,557)	38,133
Laboratory equipment	-	-	-	-	310	-	-	310	310
Tools and work equipment	446,834	-	(56,552)	390,282	(373,860)	(15,470)	56,552	(332,778)	57,504
Communications system	382,220	-	-	382,220	(167,423)	(18,072)	-	(185,495)	196,725
Meters	12,033,015	65,289	(194)	12,098,110	(3,959,684)	(544,700)	194	(4,504,190)	7,593,920
Lincoln depreciable assets	196,986,435	13,737,999	(56,746)	210,667,688	(46,590,191)	(3,481,717)	56,746	(50,015,162)	160,652,526
Land and land rights	1,128,950	-	-	1,128,950	-	-	-	-	1,128,950
Lincoln nondepreciable assets	1,128,950	-	-	1,128,950	-	-	-	-	1,128,950
Total Lincoln plant	198,115,385	13,737,999	(56,746)	211,796,638	(46,590,191)	(3,481,717)	56,746	(50,015,162)	161,781,476
Ashland Water Plant:									
Structures and improvements	58,294,977	307,957	-	58,602,934	(11,336,375)	(1,281,296)	-	(12,617,671)	45,985,263
Transmission mains and accessories	21,995,200	(65,146)	-	21,930,054	(5,478,007)	(262,663)	-	(5,740,670)	16,189,384
Office furniture and equipment	340,504	27,977	-	368,481	(260,988)	(41,756)	-	(302,744)	65,737
Shop equipment	17,951	-	-	17,951	(17,761)	(126)	-	(17,887)	64
Laboratory equipment	321,974	30,360	-	352,334	(183,674)	(44,068)	-	(227,742)	124,592
Other power and production	1,893,984	-	-	1,893,984	(1,276,634)	(62,958)	-	(1,339,592)	554,392
Electric pumping equipment	11,357,941	-	-	11,357,941	(4,247,581)	(582,578)	-	(4,830,159)	6,527,782
Purification system	25,909,954	14,438	-	25,924,392	(7,978,612)	(781,837)	-	(8,760,449)	17,163,943
Tools and work equipment	152,177	-	-	152,177	(138,872)	(4,018)	-	(142,890)	9,287
Ashland depreciable assets	120,284,662	315,586	-	120,600,248	(30,918,504)	(3,061,300)	-	(33,979,804)	86,620,444
Land and land rights	3,583,380	-	(153)	3,583,227	-	-	-	-	3,583,227
Ashland nondepreciable assets	3,583,380	-	(153)	3,583,227	-	-	-	-	3,583,227
Total Ashland plant	123,868,042	315,586	(153)	124,183,475	(30,918,504)	(3,061,300)	-	(33,979,804)	90,203,671
Vehicles and work equipment (all locations)	2,423,501	57,219	(209,248)	2,271,472	(1,446,099)	(181,420)	204,888	(1,422,631)	848,841
Utility plant in service	\$ 324,406,928	14,110,804	(266,147)	338,251,585	(78,954,794)	(6,724,437)	261,634	(85,417,597)	252,833,988
Construction in progress	4,573,634	15,152,747	(11,782,079)	7,944,302	-	-	-	-	7,944,302
Total capital assets	\$ 328,980,562	29,263,551	(12,048,226)	346,195,887	(78,954,794)	(6,724,437)	261,634	(85,417,597)	260,778,290

GENERAL STATISTICS

Year Ended August 31, 2007

(Unaudited)

Altitude of Lincoln, Nebraska	1,167 Feet
Area of Lincoln, Nebraska	88.72 Square Miles
Population	243,900 Estimate
Source of Water Supply	Wells
Location of Supply - Platte River, Ashland, Nebraska	
Well Capacity - Ashland	110 Million Gallons
Well Capacity - Lincoln	10 Million Gallons
Treatment of Water - Ashland West Plant	Aeration; Chlorination; Contact Sedimentation and Rapid Sand Filtration
Treatment of Water - Ashland East Plant	Ozonation; Filtration; Chlorination
Rainfall for Year Ended August 31, 2007	33.58
Kind and Size of Main Used	Cast Iron/Ductile Iron/PVC 4 Inches to 54 Inches
Kind and Size of Transmission Mains	
from Ashland to Lincoln	36-Inch Cast Iron 48-Inch Reinforced Concrete
Kind and Size of Transmission Mains	
from Ashland to Greenwood	54-Inch Steel
Length of Transmission Mains	
from Ashland to Lincoln	25.1 Miles
Total Miles of Distribution Mains in Use:	
Miles in use September 1, 2006	1,182.7
Estimated Added During Year	31.1
Estimated Removed During Year	12.9
Total as of August 31, 2007	1,200.9 Miles
Amount of Water Pumped During Year Ended August 31, 2007	12,795,850,000 gallons
Average Daily Consumption of Water	35,057,123 gallons
Average Daily Consumption Per Capita	144 gallons
Total Number of Active Residential Water Customers	
End of Fiscal Year	72,274
Total Number of Active Non-Residential Water Customers	
End of Fiscal Year	4,542
Bonded Debt of Lincoln Water System at August 31, 2007	\$72,210,000

LINCOLN WATER SYSTEM

Schedule 5

TOP TEN CUSTOMERS**Year Ended August 31, 2007**

(Unaudited)

	<u>USAGE</u> (HCF)	<u>AMOUNT</u>
1. University of Nebraska	575,646	\$833,555
2. Archer-Daniels Midland Company	375,912	371,550
3. City of Lincoln	282,697	426,497
4. Goodyear Tire & Rubber	279,478	284,604
5. State of Nebraska	274,096	427,891
6. BryanLGH Medical Center	167,150	243,393
7. ConAgra Refrigerator Foods	166,501	174,742
8. Pfizer Animal Health	139,323	148,399
9. Lincoln Public Schools	132,583	208,426
10. Lincoln Housing Authority	93,126	144,166
Top Ten Users Totals	2,486,512	\$3,263,223

07R-152

Introduce: 8-13-07

RESOLUTION NO. A- 84484

1 WHEREAS, the City Council of Lincoln, Nebraska, is authorized under Section
2 17.22.010 of the Lincoln Municipal Code to establish water use charges for all customers of the
3 Lincoln Water System.

4 WHEREAS, Both the Mayor's Advisory Committees, Streets, Roads and Trails (SRT)
5 and the Mayor's Infrastructure Finance Committee (MIFC) support the water rate increases
6 proposed by the City's Public Works & Utilities Department over the next 10 years, to help
7 finance the infrastructure needs identified in the City's Capital Improvement Program. The
8 current projections acknowledge the need for approval of a 7% increase for Fiscal Year 2007-
9 08; a 5% increase for Fiscal Year 2008-09; and a 4% increase for Fiscal Year 2009-10.

10 WHEREAS, Lincoln's water infrastructure is a necessary component and is required
11 under city charter to be provided to all areas served within the city limits.

12 And WHEREAS, Lincoln's water rates have historically remained low, and even with
13 the proposed rate increases will continue this tradition of competitive rates within the region and
14 nationally.

15 NOW, THEREFORE, BE IT RESOLVED by the City Council of the City of Lincoln,
16 Nebraska:

17 Effective with the billing cycle commencing on November 15, 2007, and ending January
18 15, 2008, the following schedule of water use charges is hereby established and adopted:

SCHEDULE A

20 The following rate schedule shall apply to all residential property. "Residential
21 Property" shall be defined as property consisting of dwelling units. If there is more than one

1 use per master meter on any one property including the residential use, the schedule to be used
2 will be determined as residential, if the residential portion is 50 percent or more of the area of
3 the building.

4 113.0 cents per 100 cubic feet for the first 800 cubic feet of water used per dwelling unit
5 each month.

6 159.0 cents per 100 cubic feet for the next 1500 cubic feet of water used per dwelling
7 unit each month.

8 248.0 cents per 100 cubic feet for all additional water used each month.

9 The monthly Service Charge shall be hereinafter provided.

10 SCHEDULE B

11 The following rate schedule shall apply for the current calendar year to all non-
12 residential property that used less than 12,000,000 cubic feet of water in the previous calendar
13 year:

14 113.0 cents per 100 cubic feet for the first 8000 cubic feet of water used per month.

15 159.0 cents per 100 cubic feet for all additional water used each month.

16 The minimum monthly Service Charge shall be as hereinafter provided.

17 SCHEDULE C

18 The following rate schedule shall apply for the current year to all non-residential
19 property that used more than 12,000,000 cubic feet of water in the previous calendar year. On
20 a calendar year basis, a "base usage" of each high user customer will be determined. The base
21 usage is an average of the water usage of each high user customer for the previous three (3)
22 calendar years.

1 The following fees would apply:

2 107.0 cents per 100 cubic feet for water usage less than base to 5% above base.

3 111.0 cents per 100 cubic feet for water usage 5% - 15% above base.

4 115.0 cents per 100 cubic feet for water usage 15% - 25% above base.

5 120.0 cents per 100 cubic feet for water usage for all water usage over 25% above base.

6 The minimum monthly Service Charge shall be as hereinafter provided.

7 SCHEDULE D - PROVISIONS APPLICABLE -
8 TO ALL TYPES OF WATER SERVICE

9 Service Charge. There shall be a Service Charge per month to each property using the
10 Lincoln Water System, determined by the number and size of the water meter, or meters,
11 serving such property, to-wit:

	WATER METER SIZE	SERVICE CHARGE FOR WATER METER
12	5/8 inch	\$ 2.95
13	3/4 inch	2.95
14	1 inch	2.95
15	1-1/2 inch	5.90
16	2 inch	11.80
17	3 inch	26.55
18	4 inch	47.20
19	6 inch	106.15
20	8 inch	188.75
21	10 inch	294.90

22 The Service Charge for a multiple dwelling unit or mobile home shall be at least \$1.81
23 per dwelling unit or mobile home hookup space per month. In those instances where fire
24 protection considerations dictate that a water meter larger than 1-inch service a single-family
25 dwelling unit located on a single lot, the monthly service charge shall be \$2.95 per dwelling
26 unit. A dwelling unit shall, for the purpose of this schedule, be defined as a room or rooms in
27
28

1 which kitchen facilities are provided, located in the building or structure used by a facility or
2 household as a home or residence of the family or household.

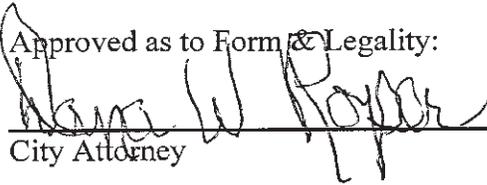
3 WATER RATES TO CUSTOMERS OUTSIDE
4 THE CITY LIMITS

5 Customers located outside the City Limits of Lincoln and served by the water system of
6 the City of Lincoln shall pay no less than the water rates charged to customers within the City
7 Limits of Lincoln for water furnished them by the water system of the City of Lincoln.

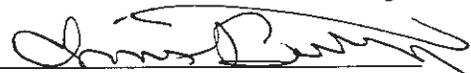
8 BE IT FURTHER RESOLVED that Resolution No. A-83988, adopted by the City
9 Council on August 21, 2006, is hereby superseded.

Introduced by: 

AYES: Camp, Emery, Eschliman,
Marvin, Spatz, Svoboda; NAYS:
Cook.

Approved as to Form & Legality:

City Attorney

ADOPTED
AUG 20 2007
BY CITY COUNCIL

Approved this 23 day of Aug, 2007:

Mayor

Quantitative Statistics

Years ended August 31, 2007 and 2006

(Unaudited)

	2007	2006	Increase (decrease)
Water pumpage in one hundred cubic feet: (H.C.F.) by months:			
September	1,489,071	2,122,968	(633,897)
October	1,371,121	1,572,520	(201,399)
November	1,129,092	1,181,368	(52,276)
December	1,041,401	1,085,116	(43,715)
January	1,077,869	1,075,676	2,193
February	978,828	1,045,548	(66,720)
March	1,088,756	1,026,371	62,385
April	1,108,584	1,205,880	(97,296)
May	1,310,836	1,587,717	(276,881)
June	1,736,909	2,242,712	(505,803)
July	2,778,667	2,578,012	200,655
August	1,950,003	1,976,227	(26,224)
Total H.C.F. pumped	17,061,137	18,700,115	(1,638,978)
H.C.F. sold and donated:			
Customer metered sales	16,380,430	17,301,877	(921,447)
Used in new building construction (estimated)	10,000	10,000	—
Used in flushing on new sewers, water main construction, etc. (estimated)	5,500	5,500	—
Hydrant permits	38,523	56,637	(18,114)
Used for testing meters (estimated)	250	250	—
Used by Fire Department (estimated)	3,200	3,200	—
Lawn sprinkling and service shop water	100	100	—
Total water accounted for	16,438,003	17,377,564	(939,561)
Total H.C.F. unaccounted for	623,134	1,322,551	699,417
Percent of H.C.F. unaccounted for	3.65%	7.07%	

LINCOLN WATER SYSTEM

Schedule 8

COMPARATIVE PUMPING REPORT

For Fiscal Years as Shown by Gallons

(Unaudited)

MONTH	August 31, 2007	August 31, 2006	August 31, 2005	August 31, 2004	August 31, 2003
September	1,116,800,000	1,592,226,000	1,480,430,000	1,372,488,000	1,523,935,000
October	1,028,340,000	1,179,390,000	1,128,140,000	1,230,054,000	979,028,000
November	846,820,000	886,026,000	794,620,000	816,023,250	827,521,000
December	781,050,000	813,837,000	761,380,000	794,745,000	848,382,000
January	808,400,000	806,757,000	809,030,000	786,438,000	863,192,000
February	734,120,000	784,161,000	747,670,000	757,842,000	781,163,000
March	816,570,000	769,778,250	774,520,000	823,634,250	858,968,000
April	831,440,000	904,410,000	844,140,000	1,003,313,250	912,982,000
May	983,130,000	1,190,787,750	1,272,810,000	1,077,558,750	1,040,289,000
June	1,302,680,000	1,682,034,000	1,436,260,000	1,208,910,750	1,150,092,000
July	2,084,000,000	1,933,509,000	2,139,790,000	1,295,531,250	2,051,310,000
August	1,462,500,000	1,482,170,250	1,632,630,000	1,659,762,750	1,857,923,000
Total	12,795,850,000	14,025,086,250	13,821,420,000	12,826,301,250	13,694,785,000

LINCOLN WATER SYSTEM
ANNUAL RAINFALL FOR THE PERIOD OF
September 1, 2006 to August 31, 2007
(Unaudited)

	Inches of <u>Rainfall</u>
September	3.93
October	0.90
November	0.09
December	3.05
January	0.64
February	1.31
March	2.79
April	3.44
May	8.13
June	2.28
July	1.22
August	<u>5.80</u>
TOTAL INCHES FOR FISCAL YEAR	<u>33.58</u>

LINCOLN WATER SYSTEM

WATER ANALYSIS

(All Results in Parts Per Million)
(Collected July 25, 2007)
(Unaudited)

550 W. Cornhusker Hwy.

Hydrogen Ion Concentration (pH)	7.46
Total Dissolved Solids	331 ppm.
Total Iron (Fe)	<0.050 ppm.
Manganese (Mn)	3.22 ppb.
Calcium (as Ca)	52.9 ppm.
Total Alkalinity (CaCO ₃)	156 ppm.
Chloride (Cl)	18.6 ppm.
Fluoride (F)	1.10 ppm.
Nitrate (+Nitrite)	0.36 ppm.
Sodium (Na)	31.4 ppm.
Hardness as (CaCO ₂) Total Hardness	190 ppm.

(All above analysis made in accordance with Standard Methods for Water and Wastewater,
20th Ed.)

Lincoln Water System

Summary of Insurance Coverage

August 31, 2007

(Unaudited)

Type of policy	Insurance coverage	Policy limits	Self-insured retention deductible	Self-insurance deductible	Insurance carrier	Policy number
Automobile Fleet Liability	Self-Insured Excess Coverage Excess Coverage	0 - 250,000 250,000 - 1,000,000 1,000,000 - 5,000,000	250,000		Genesis	XYB300909D
Automobile Fleet Physical Damage**	Self-Insured	Actual cash value	2,500	2,500		
Building and Contents (Includes Boiler & Machinery)	Blanket policy - buildings and contents	Replacement cost	50,000	2,500	FM Global	FM325
Money and Securities	Inside/outside premises	50,000	500	0	Fidelity & Deposit	CCP003595
Water Distribution	Water distribution center	25,000,000	50,000	10,000	FM Global	FM325
Data Processing Equipment	Computer equipment, data and media	Replacement cost	50,000	2,500	FM Global	FM325
Equipment Floater (911)	Radio tower floater	Replacement cost	50,000	2,500	FM Global	FM325
Equipment Floater (NON-LIC)	Nonlicensed scheduled equipment	Actual Cash Value	50,000	2,500	FM Global	FM325
General Liability ***	\$1,000,000 occurrence	5,000,000	250,000	0	Genesis	XYB300909D
Public Employee Blanket Bond	Employees blanket bond coverage	1,000,000	25,000	0	Fidelity & Deposit	CCP 003 05 95
Public Officials Liability***	\$1,000,000 occurrence	5,000,000	250,000	0	Genesis	XYB300909D
Workers' Compensation Excess	Statutory	Statutory	500,000	0	Midwest Employers Casualty (MECC)	EWC007744

** Self-insured for both comp & collision.

LINCOLN WATER SYSTEM

Summary of Insurance Coverage

This summary of insurance coverage provides general information regarding the City's casualty-property insurance policies.

AUTOMOBILE INSURANCE

Liability Coverage: Provides coverage for accidents involving all owned, nonowned and hired vehicles. Protects the City against third-party claims from members of the public for bodily injury or property damage.

Physical Damage: Provides comprehensive (other than collision) and collision coverage for City-owned vehicles on a self-insured basis.

PROPERTY INSURANCE

Building and Contents: Provides coverage for damage to City-owned buildings and contents provided the buildings are listed on the City's property schedule.

Boiler and Machinery: Provides coverage for damage to boilers, vessels, steam generators, refrigerating and air conditioning vessels and piping, deep well pump units, turbines and certain machines.

Crime: Coverage for theft, disappearance or destruction of money and securities both inside and outside the premises.

Inland Marine Floaters: Provides physical damage coverage for specifically scheduled property. Current floaters insured include: data processing equipment, radio towers, and nonlicensed equipment.

WATER DISTRIBUTION SYSTEM

Provides coverage for underground pipeline between Lincoln and Ashland.

GENERAL LIABILITY

Provides coverage for general liability (bodily injury and property damage) claims made against the City.

PUBLIC EMPLOYEES BLANKET BOND

Provides coverage for loss of money and securities resulting from employee dishonesty. This is a blanket policy covering City employees.

PUBLIC OFFICIALS LIABILITY (Claims-made)

The insurance company will pay on behalf of the City of Lincoln (amount over self-insured retention) for any civil claim or claim made against them on a *claims-made basis* because of any wrongful act. A wrongful act under the coverage is defined as any actual or alleged error or misstatement or misleading statement or act of omission or neglect or breach of duty including misfeasance, malfeasance and nonfeasance by an insured. Also covered are claims arising out of employment practices.

WORKERS' COMPENSATION

Provides excess workers' compensation insurance for injuries arising out of and in the course of employment. This provides indemnity and medical coverage above our self-insured retention limits.



Independent Accountants' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Financial Statements Performed in Accordance with Government Auditing Standards

The Honorable Mayor
and Members of the City Council
Lincoln Water System
Lincoln, Nebraska

We have audited the financial statements of Lincoln Water System as of and for the year ended August 31, 2007, and have issued our report thereon dated November 28, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Lincoln Water System'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 the Lincoln Water System's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Lincoln Water System's internal control over financial reporting.

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

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

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

Compliance and Other Matters

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

This report is intended solely for the information and use of the governing body and management and others within Lincoln Water System is not intended to be and should not be used by anyone other than these specified parties.

BKD, LLP

November 28, 2007