

Washington Suburban Sanitary Commission



Annual Financial Report

Year Ended June 30, 2004

Report of Independent Auditors

To the Commissioners
Of the Washington Suburban Sanitary Commission:

We have audited the accompanying balance sheets of the Washington Suburban Sanitary Commission as of June 30, 2004 and 2003, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Company'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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Washington Suburban Sanitary Commission at June 30, 2004 and 2003, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.

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

Ernst & Young LLP

August 26, 2004

MANAGEMENT'S DISCUSSION AND ANALYSIS REQUIRED SUPPLEMENTARY INFORMATION

This section of the Washington Suburban Sanitary Commission (WSSC) annual financial report presents our discussion and analysis of WSSC's financial performance during the fiscal years that ended June 30, 2004 and 2003. Please read it in conjunction with WSSC's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

Fiscal Year 2004

- WSSC maintained AAA bond ratings from FitchRatings, Moody's Investor Services, and Standard & Poors.
- Water and sewer rates did not increase during fiscal year 2004. This was the sixth consecutive year in which rates remained stable.
- Fiscal year 2004 bond refundings will reduce WSSC's total debt service payments over the next 19 years by \$25.8 million.
- Operating revenues decreased \$3.6 million. The volume of water delivered to the system rose slightly during the fiscal year, but average rates billed to water and sewer customers declined approximately 1.5%.
- Expenses increased during fiscal year 2004. Health care insurance costs increased \$.6 million during the year. Water supply operating and maintenance costs increased \$3.3 million. Pension costs charged to operating expenses increased in 2004 because actuarially required contributions were \$1.4 million higher in comparison to the prior fiscal year. Intermunicipal agency sewage disposal expenses increased \$3.1 million primarily as a result of the reconciliation of WSSC's share of estimated and actual expenses. An additional \$2.7 million was expended during the year to provide training to all employees of the Commission. Also, diversity experts were contracted at a cost of \$1.3 million to conduct a study to evaluate, and recommend enhancements, to WSSC's diversity programs, performance and profile.
- Capital assets (water and sewer lines, water tanks, treatment plants, pumping stations, multi-purpose facilities and other facilities), net of accumulated depreciation, increased by \$123.3 million, while overall debt decreased by \$12.0 million.
- The increase in net assets during the year included operating income, net of non-operating expenses, of \$91.5 million, and capital contributions of \$68.7 million.

Fiscal Year 2003

- WSSC maintained AAA bond ratings from FitchRatings, Moody's Investor Services, and Standard & Poors.
- Water and sewer rates did not increase during fiscal year 2003. This was the fifth consecutive year in which rates remained stable.
- The March 2003 bond refunding will reduce WSSC's total debt service payments over the next 17 years by \$47.1 million.
- Operating revenues increased \$15.0 million. The volume of water delivered to the system rose 2% during the fiscal year.
- Expenses increased during fiscal year 2003. The most significant change was a \$6.7 million increase in depreciation and amortization expenses resulting from a 54% increase in capital assets completed and placed into service during 2003. Also, salaries and wages increased \$7.0 million, due primarily to performance incentives and the full year effect of the prior year's cost of living increases and merit pay adjustments. Pension costs charged to operating expenses increased in 2003 because actuarially required contributions were \$3.3 million higher in comparison to the prior fiscal year. Intermunicipal agency sewage disposal expenses decreased \$4.3 million primarily as a result of the reconciliation of WSSC's share of estimated and actual expenses.

- Capital assets (water and sewer lines, water tanks, treatment plants, pumping stations, multi-purpose facilities and other facilities), net of accumulated depreciation, increased by \$114.4 million, while overall debt decreased by \$72.0 million.
- The increase in net assets during the year included operating income, net of non-operating expenses, of \$103.7 million, and capital contributions of \$77.0 million.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of two parts - management's discussion and analysis and the required financial statements. The required financial statements consist of:

- Balance sheets
- Statements of revenues, expenses, and changes in net assets
- Statements of cash flows

The balance sheets provide a snapshot of WSSC's financial position at June 30, the end of the fiscal year. Figures on the balance sheets are cumulative from inception. WSSC's balance sheets present current and long-term assets and liabilities as well as net assets.

WSSC's statements of revenues, expenses and changes in net assets reflect activity for the fiscal year. These statements measure operating revenues and expenses as well as non-operating revenues and expenses. The statements also present capital contributions as well as changes in net assets.

The statements of cash flows present WSSC's inflow and outflow of cash. Cash flows from operating activities, capital and related financing activities, and investment activities are all shown separately. Cash provided by operating activities is reconciled to operating income. WSSC uses the direct method for presenting the cash flow statements.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data.

WSSC operates as an enterprise fund, which is one type of proprietary fund. Enterprise funds operate similarly to private businesses in that charges for services to customers are expected to cover expenses. WSSC's financial statements are presented using the accrual basis of accounting and the economic resources measurement focus. All assets and liabilities are included in the financial statements. Revenue is recognized when water or other services are delivered. Expenses are recognized when goods and services are received. All revenues and expenses are recognized regardless of when cash is received or paid.

FINANCIAL ANALYSIS

Net Assets

Fiscal Year 2004

WSSC's net assets increased 6.6% to \$2,594.8 million (See Table A-1). The majority of this increase is attributable to the change in net assets invested in capital assets, net of related debt. WSSC's capital assets are increasing, while the related debt is decreasing. Capital assets, net of accumulated depreciation, increased 3.3% to \$3,823.0 million. During fiscal year 2004, developers constructed \$23.7 million of these capital assets and donated them to WSSC. Additional information is presented in the Capital Asset and Debt Administration section of this discussion.

Total debt, including current maturities, decreased .8% to \$1,463.1 million. Capital contributions of \$68.7 million were available to finance capital projects during the year. These funding sources reduced the amount of bonds WSSC needed to sell for construction of water and sewer projects. A more detailed description of WSSC's debt can be found in Note H of the financial statements.

Fiscal Year 2003

WSSC's net assets increased 8.0% to \$2,434.7 million (See Table A-1). The majority of this increase is attributable to the change in net assets invested in capital assets, net of related debt. WSSC's capital assets increased, while the related debt decreased. Capital assets, net of accumulated depreciation, increased 3.2% to \$3,699.7 million. During fiscal year 2003, developers constructed \$37.4 million of these capital assets and donated them to WSSC. Additional information is presented in the Capital Asset and Debt Administration section of this discussion.

Total debt, including current maturities, decreased 4.7% to \$1,475.1 million. Capital contributions of \$77.0 million and operating revenues of \$30.8 million were available to finance capital projects during the year. These funding sources reduced the amount of bonds WSSC needed to sell for construction of water and sewer projects. A more detailed description of WSSC's debt can be found in Note H of the financial statements.

TABLE A-1
WSSC's Net Assets
(in millions of dollars)

	FY 2004	FY 2003	FY 2002	FY 2004 % Change	FY 2003 % Change
Current and other assets	\$ 420.5	\$ 401.6	\$ 381.2	4.7	5.4
Capital assets, net of accumulated depreciation	3,823.0	3,699.7	3,585.3	3.3	3.2
Total assets	4,243.5	4,101.3	3,966.5	3.5	3.4
Current and other liabilities	483.7	410.0	345.0	18.0	18.8
Bonds and notes payable, net of current maturities	1,165.0	1,256.6	1,367.5	(7.3)	(8.1)
Total liabilities	1,648.7	1,666.6	1,712.5	(1.1)	(2.7)
Net assets:					
Invested in capital assets, net of related debt	2,390.2	2,242.9	2,046.2	6.6	9.6
Restricted for growth construction	73.7	69.7	64.0	5.7	8.9
Unrestricted	130.9	122.1	143.8	7.2	(15.1)
Total net assets	\$ 2,594.8	\$ 2,434.7	\$ 2,254.0	6.6	8.0

Changes in Net Assets

Fiscal Year 2004

WSSC's operating revenues decreased .8% to \$437.3 million (See Table A-2). The amount of water delivered to the system rose slightly during the fiscal year, but average rates billed to water and sewer customers declined approximately 1.5%. Operating expenses increased by 5.6% to \$313.3 million. Health care insurance costs increased \$.6 million during the year. Water supply operating and maintenance costs increased \$3.3 million. Pension costs charged to operating expenses increased in 2004 because actuarially required contributions were \$1.4 million higher in comparison to the prior fiscal year. Intermunicipal agency sewage disposal expenses increased \$3.1 million primarily as a result of the reconciliation of WSSC's share of estimated and actual expenses. An additional \$2.7 million was expended during the year to provide training to all employees of the Commission. In addition, diversity experts were contracted at a cost of \$1.3 million to conduct a study to evaluate, and recommend enhancements, to WSSC's diversity programs, performance and profile. Increases in operating expenses and decreases in revenues during the year resulted in an 11.8% decline in income before contributions to \$91.5 million. Also, capital contributions decreased by 10.8% to \$68.7 million. Total footage of water and sewer mains constructed and donated by developers in 2004 decreased 26% in comparison to 2003.

Fiscal Year 2003

WSSC's operating revenues increased 3.5% to \$440.9 million (See Table A-2). The amount of water delivered to the system rose 2.0% during the year. Operating expenses increased by 4.4% to \$296.8 million. Depreciation and amortization expenses rose \$6.7 million in comparison to fiscal year 2002 because capital assets completed and placed in service during 2003 increased 54% (See Tables A-4 and A-5). Also, salaries and wages increased \$7.0 million, due primarily to performance incentives and the full year effect of the prior year's cost of living increases and merit pay adjustments. Pension costs charged to operating expenses increased in 2003 because actuarially required contributions were \$3.3 million higher in comparison to the prior fiscal year. Intermunicipal agency sewage disposal expenses decreased \$4.3 million primarily as a result of the reconciliation of WSSC's share of estimated and actual expenses. Increases in operating revenues exceeded increases in expenses during the year resulting in a 12.0% rise in income before contributions to \$103.7 million. Conversely, capital contributions decreased by 8.3% to \$77.0 million. Capital assets donated by developers were comparable to donations in fiscal year 2002.

TABLE A-2
WSSC's Changes in Net Assets
(in millions of dollars)

	FY 2004	FY 2003	FY 2002	FY 2004 % Change	FY 2003 % Change
Operating revenues	\$ 437.3	\$ 440.9	\$ 425.9	(0.8)	3.5
Operating expenses	(313.3)	(296.8)	(284.2)	(5.6)	(4.4)
Non-operating revenues (expenses)	(32.5)	(40.4)	(49.1)	19.6	17.7
Income before contributions	91.5	103.7	92.6	(11.8)	12.0
Capital contributions	68.7	77.0	84.0	(10.8)	(8.3)
Changes in net assets	\$ 160.2	\$ 180.7	\$ 176.6	(11.3)	2.3

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

Fiscal Year 2004

As of June 30, 2004, WSSC had invested \$3,823.0 million in a broad range of capital assets including water and sewer lines, water tanks, treatment plants, pumping stations, multi-purpose facilities and other facilities. This amount represents a net increase of \$123.3 million, or 3.3%, over fiscal year 2003.

Fiscal Year 2003

As of June 30, 2003, WSSC had invested \$3,699.7 million in a broad range of capital assets including water and sewer lines, water tanks, treatment plants, pumping stations, multi-purpose facilities and other facilities. This amount represents a net increase of \$114.4 million, or 3.2%, over fiscal year 2002.

TABLE A-3
WSSC's Capital Assets
(net of depreciation, in millions of dollars)

	FY 2004	FY 2003	FY 2002	FY 2004 % Change	FY 2003 % Change
Land and rights of way	\$ 80.9	\$ 81.4	\$ 82.2	(0.6)	(1.0)
Construction in progress	526.6	544.5	513.9	(3.3)	6.0
Water supply	916.3	845.0	836.2	8.4	1.1
Sewage disposal	1,065.4	996.9	954.0	6.9	4.5
General construction	1,221.6	1,219.3	1,183.8	0.2	3.0
Other	12.2	12.6	15.2	(3.2)	(17.1)
Total capital assets	\$ 3,823.0	\$ 3,699.7	\$ 3,585.3	3.3	3.2

Increases in capital assets in fiscal years 2004 and 2003 were comparable. However, capital assets completed and placed in service increased \$58 million, or 32%, in comparison to fiscal year 2003. Major additions to capital assets being depreciated during fiscal years 2004 and 2003 are illustrated in Tables A-4 and A-5, respectively.

TABLE A-4
WSSC's Additions to Capital Assets Being Depreciated
Fiscal Year 2004
(in millions of dollars)

	Water Supply	Sewage Disposal	General Construction
Financed from proceeds of bonds, notes, operating revenues or capital contributions:			
Water main rehabilitation	\$ 13.4	\$ 3.3	
Water and sewer mains	2.5		\$ 4.7
Water meters			1.9
House connections			9.0
Water filtration facilities	80.0		
Pumping stations		22.1	
Wastewater treatment facilities		28.1	
Joint use facilities		48.1	
Constructed and contributed by developers:			
House connections			6.5
Wastewater pumping stations			
Water and sewer mains			17.1
Total fiscal year 2004 additions to capital assets being depreciated	\$ 95.9	\$101.6	\$ 39.2

TABLE A-5
WSSC's Additions to Capital Assets Being Depreciated
Fiscal Year 2003
(in millions of dollars)

	Water Supply	Sewage Disposal	General Construction
Financed from proceeds of bonds, notes, operating revenues or capital contributions:			
Water main rehabilitation	\$ 16.9		
Water and sewer mains	11.3	\$ 0.6	\$ 18.1
Water meters			2.4
House connections			18.7
Water filtration facilities	3.8		
Pumping stations		0.3	
Wastewater treatment facilities		68.5	
Joint use facilities		0.6	
Constructed and contributed by developers:			
House connections			9.5
Wastewater pumping stations		1.4	
Water and sewer mains			26.6
Total fiscal year 2003 additions to capital assets being depreciated	\$ 32.0	\$ 71.4	\$ 75.3

Bonds and Notes Payable

Fiscal Year 2004

At the end of fiscal year 2004, bonds and notes outstanding totaled \$1,463.1 million. This is an .8% decrease from the previous fiscal year. Three bond refundings during the year will reduce WSSC's total debt service payments over the next 19 years by \$25.8 million. A more detailed description of WSSC's bond refundings can be found in Note I of the financial statements.

The primary sources of revenue utilized for repayment of debt are water consumption and sewer use charges and front foot benefit assessments. In addition, WSSC obtains funds from other sources to reduce the amount of bonds it needs to sell to construct water and sewer projects. These other sources include payments from applicants for new service, payments from other jurisdictions for projects that specifically benefit them, and state and federal grants. A more detailed description of WSSC's bonds and notes payable can be found in Note H of the financial statements.

Fiscal Year 2003

At the end of fiscal year 2003, bonds and notes outstanding totaled \$1,475.1 million. This is a 4.7% decrease from the previous fiscal year. A bond refunding in March 2003 will reduce WSSC's total debt service payments over the next 17 years by \$47.1 million. A more detailed description of WSSC's bond refunding can be found in Note I of the financial statements.

The primary sources of revenue utilized for repayment of debt are water consumption and sewer use charges and front foot benefit assessments. In addition, WSSC obtains funds from other sources to reduce the amount of bonds it needs to sell to construct water and sewer projects. These other sources include payments from applicants for new service, payments from other jurisdictions for projects that specifically benefit them, and state and federal grants. A more detailed description of WSSC's bonds and notes payable can be found in Note H of the financial statements.

TABLE A-6
WSSC's Bonds and Notes Payable
(in millions of dollars)

	FY 2004	FY 2003	FY 2002	FY 2004 % Change	FY 2003 % Change
Water supply	\$ 347.6	\$ 368.3	\$ 396.9	(5.6)	(7.2)
Sewage disposal	378.8	336.5	331.7	12.6	1.4
General construction	732.2	763.8	809.8	(4.1)	(5.7)
Storm water drainage	4.5	6.5	8.7	(30.8)	(25.3)
Total	1,463.1	1,475.1	1,547.1	(0.8)	(4.7)
Current maturities	297.6	218.5	179.6	36.2	21.7
Long-term portion	1,165.5	1,256.6	1,367.5	(7.2)	(8.1)
Total bonds and notes payable	\$ 1,463.1	\$ 1,475.1	\$ 1,547.1	(0.8)	(4.7)

Bond Ratings

During fiscal year 2001, FitchRatings, Moody's Investors Service, and Standard & Poor's assigned ratings of 'AAA', 'Aaa', and 'AAA', respectively, to WSSC's outstanding general obligation bonds. WSSC's superior credit was attributed in large part, to strong fiscal practices, streamlined operations, and management's commitment to keeping the utility competitive. These ratings were affirmed in fiscal years 2003 and 2004.

Limitations on Debt

Maryland law limits the amount of bonds and notes WSSC may have outstanding at any time. This limitation is generally based on legislated percentages of the real property assessable tax base and personal property and operating real property assessments within the Washington Suburban Sanitary District. As of June 30, 2004 and 2003, the calculated limits were \$5,151.9 million and \$4,856.3 million, respectively. WSSC's outstanding debt was significantly below those limits.

BUDGET

WSSC's operating and capital budgets are prepared annually utilizing the debt service method of accounting. These financial statements are presented in accordance with accounting principles generally accepted in the United States. Because different methods of accounting are utilized, comparisons of budgeted and actual revenues and expenses have not been presented.

WASHINGTON SUBURBAN SANITARY COMMISSION
BALANCE SHEETS
AS OF JUNE 30, 2004 AND 2003
(in thousands)

	<u>2004</u>	<u>2003</u>
ASSETS		
Current assets:		
Cash (Note B)	\$ 88	\$ 59
Short-term investments (Note B)	269,136	261,060
Receivables, net (Note C)	102,102	100,259
Federal and State grants receivable, current portion	—	1,694
Prepaid expenses	805	430
Materials and supplies, at average cost	<u>8,846</u>	<u>9,534</u>
Total current assets	<u>380,977</u>	<u>373,036</u>
Non-current assets:		
Capital assets, net of accumulated depreciation (Note E)	3,823,087	3,699,714
Long-term investments (Note B)	30,263	18,372
Federal and State grants receivable, net of current portion	3,260	1,118
Deferred charges and other assets (Note D)	<u>5,971</u>	<u>9,078</u>
Total non-current assets	<u>3,862,581</u>	<u>3,728,282</u>
 Total assets	 <u>\$ 4,243,558</u>	 <u>\$ 4,101,318</u>
LIABILITIES		
Current liabilities:		
Bonds and notes payable, current maturities (Note H)	\$ 297,600	\$ 218,532
Accounts payable and accrued expenses	88,465	89,626
Accrued bond and note interest payable	18,008	19,870
Deposits and deferred credits	<u>1,955</u>	<u>1,738</u>
Total current liabilities	<u>406,028</u>	<u>329,766</u>
Non-current liabilities:		
Bonds and notes payable, net of current maturities (Notes H and I)	1,165,540	1,256,616
Long-term pension liability (Note J)	44,328	47,278
Deposits, deferred credits and other long-term liabilities (Note G)	<u>32,832</u>	<u>32,974</u>
Total non-current liabilities	<u>1,242,700</u>	<u>1,336,868</u>
 Total liabilities	 <u>1,648,728</u>	 <u>1,666,634</u>
COMMITMENTS AND CONTINGENCIES (Note L)		
NET ASSETS		
Invested in capital assets, net of related debt	2,390,210	2,242,938
Restricted for growth construction	73,721	69,670
Unrestricted	<u>130,899</u>	<u>122,076</u>
Total net assets	<u>2,594,830</u>	<u>2,434,684</u>
 Total liabilities and net assets	 <u>\$4,243,558</u>	 <u>\$4,101,318</u>

The accompanying notes are an integral part of these financial statements.

WASHINGTON SUBURBAN SANITARY COMMISSION
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003
(in thousands)

	<u>2004</u>	<u>2003</u>
OPERATING REVENUES:		
Water consumption, sewer use and service charges	\$ 342,811	\$ 346,696
Front foot benefit assessments	68,212	68,019
House connection charges	10,211	9,593
Other	<u>16,077</u>	<u>16,604</u>
Total operating revenues	<u>437,311</u>	<u>440,912</u>
OPERATING EXPENSES:		
Operations	58,831	54,124
Maintenance	66,288	64,368
Intermunicipal agency sewage disposal	39,711	36,199
Administrative and general	53,751	49,245
Depreciation and amortization	<u>94,760</u>	<u>92,894</u>
Total operating expenses	<u>313,341</u>	<u>296,830</u>
Net operating revenue	<u>123,970</u>	<u>144,082</u>
NON-OPERATING REVENUES (EXPENSES):		
Interest on bonds and notes payable	(65,802)	(79,085)
Capitalized interest	19,767	23,295
Prince George's County storm drain debt service reimbursement	2,295	2,662
Interest income on investments	3,969	4,825
Other interest income	<u>7,289</u>	<u>7,915</u>
Net non-operating expenses	<u>(32,482)</u>	<u>(40,388)</u>
Income before capital contributions	91,488	103,694
Capital contributions	<u>68,658</u>	<u>76,954</u>
Changes in net assets	160,146	180,648
Net assets, beginning of year	<u>2,434,684</u>	<u>2,254,036</u>
Net assets, end of year	<u>\$2,594,830</u>	<u>\$2,434,684</u>

The accompanying notes are an integral part of these financial statements.

WASHINGTON SUBURBAN SANITARY COMMISSION
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003
(in thousands)

	<u>2004</u>	<u>2003</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from water and sewer customers	\$ 338,379	\$ 349,558
Receipts from front foot benefit assessments	67,505	68,343
Receipts from house connection charges	10,211	9,593
Receipts from other customers and miscellaneous	15,601	17,339
Payments to employees	(131,719)	(129,018)
Payments to District of Columbia Water & Sewer Authority	(28,711)	(31,848)
Payments to suppliers	<u>(52,093)</u>	<u>(42,440)</u>
Net cash provided by operating activities	<u>219,173</u>	<u>241,527</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Proceeds from bonds and notes	462,607	483,514
Capital contributions	44,891	51,060
Prince George's County storm drain debt service reimbursement	2,295	2,662
Bond redemptions and note repayments	(479,169)	(581,506)
Interest payments, premiums and discounts on bonds and notes	(55,241)	(36,984)
Capital asset construction	<u>(178,530)</u>	<u>(126,303)</u>
Net cash used in capital and related financing activities	<u>(203,147)</u>	<u>(207,557)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from the sale of investments	1,157,078	1,098,681
Purchases of investments	(1,177,127)	(1,142,328)
Interest income received	<u>4,052</u>	<u>5,104</u>
Net cash (used) provided by investing activities	<u>(15,997)</u>	<u>(38,543)</u>
Net (decrease) increase in cash	29	(4,573)
Cash, beginning of year	<u>59</u>	<u>4,632</u>
Cash, end of year	<u>\$ 88</u>	<u>\$ 59</u>
Cash flows from operating activities:		
Net operating revenue	\$ 123,970	\$ 144,082
Adjustments to reconcile net operating revenue to net cash provided by operating activities:		
Depreciation and amortization	99,195	98,622
Changes in assets and liabilities:		
Decrease in receivables, net	(1,843)	3,006
Decrease (increase) in materials and supplies	688	786
Decrease (increase) in deferred charges and other assets	(103)	5
(Decrease) increase in accounts payable and accrued liabilities	(10)	(1,479)
Increase (decrease) in deferred credits	(337)	305
Decrease in long-term pension liability	<u>(2,387)</u>	<u>(3,800)</u>
Net cash provided by operating activities	<u>\$ 219,173</u>	<u>\$ 241,527</u>

Noncash capital financing activities:

Capital assets of \$23,732 and \$37,449 were acquired through contributions from developers in 2004 and 2003, respectively.

The accompanying notes are an integral part of these financial statements.

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Washington Suburban Sanitary Commission (WSSC) is a bi-county political subdivision of the State of Maryland, created to provide water supply and sewage disposal services for Montgomery and Prince George's Counties. The financial statements are presented using the accrual basis of accounting and the economic resources measurement focus. Significant accounting policies are summarized below.

Operating and Non-operating Revenues and Expenses

Revenues and expenses derived from financing and investment activities are classified as non-operating revenues and expenses. All other revenues and expenses are classified as operating.

Water and sewer service rates are established to provide sufficient funds to recover operating costs and debt service relating to the water supply and sanitary sewer systems. Water and sewer revenues are recognized as water is delivered to the system.

Front foot benefit and house connection assessments, levied on properties where water and/or sanitary sewer service is available, are the principal source of funds to service general construction bond debt. Front foot benefit assessments are recorded as operating revenue ratably over the levy year; house connection assessments and fees are deferred and amortized to operating revenue over the life of the bonds issued to finance the house connections.

Recovery of the Prince George's County portion of the cost of storm water drainage debt service is made through annual reimbursement from the County and is recorded as non-operating revenue. If necessary, ad valorem taxes may be levied to cover debt service of storm water drainage bonds and other bonds and notes. No ad valorem taxes were levied in fiscal 2004 or 2003.

Capital Contributions

In July 1993, a system development charge (SDC) was established to help finance the cost of expanding water and sewage systems to accommodate growth in the Washington Suburban Sanitary District. System development charges are recorded as capital contributions when received.

Developer fees and charges are established to recover costs related to services provided to outside developers for the construction of capital assets. These fees are recorded as capital contributions when received.

Federal and State water pollution grants are recognized as capital contributions when related capital costs are incurred.

Donated assets consist principally of capital assets constructed by developers and subsequently donated to WSSC. They are recorded at estimated fair value using developers' estimated costs to construct the assets or WSSC's estimated costs to construct similar assets. The capital assets, and related capital contributions, are recognized upon completion of construction.

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Capital Assets

Capital assets are stated at original construction cost, which includes related payroll, payroll taxes, fringe benefits, administrative costs and interest capitalized during construction.

Depreciation and Amortization

Capital assets are depreciated using the straight-line method over the estimated service lives of the property, which averaged 48 years in fiscal 2004 and 46 years in fiscal 2003.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses. Actual results may differ from these estimates.

Reclassifications

The 2003 financial statements reflect certain reclassifications to conform with the 2004 presentation.

Bond Refunding Costs

The issuance costs of refunding bonds are amortized to operations using a proportionate-to-stated interest method (see Note D). The reacquisition price of the refunded bonds in excess of carrying value is also deferred and amortized to operations (see Note I).

Contributions of Capital Assets

WSSC follows Governmental Accounting Standards Board Statements No. 33, Accounting and Financial Reporting for Nonexchange Transactions (GASB No. 33). GASB No. 33 requires recognition of all contributions of capital assets, including donated assets, as revenues rather than contributed capital.

Net Assets

GASB No. 34 establishes financial reporting standards for state and local governments regarding the required financial statements, presentation of management's discussion and analysis and classification of net assets. GASB No. 34 requires that net assets restricted for particular purposes, and net assets invested in capital assets, net of related debt, be presented separately on the balance sheets.

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Net assets associated with unspent SDC proceeds are restricted for growth construction.

Net assets associated with unspent bond proceeds are restricted for capital projects. As of June 30, 2004, and 2003, unspent bond proceeds total \$30,263,000, and \$18,372,000, respectively. However, cash and investments net of the related debt resulted in a zero net asset balance.

Accounting Guidelines

In accordance with the provisions of Statement No. 20 of the Governmental Accounting Standards Board (GASB), Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting, issued in September 1993, WSSC has elected to continue to apply all applicable GASB pronouncements and not to follow Financial Accounting Standards Board Statements and Interpretations issued after November 30, 1989.

Recent Accounting Pronouncements

In June 2004, the GASB issued Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions. GASB No. 45 will require WSSC to record a liability for certain postemployment benefits. WSSC has not determined the impact of this pronouncement on the financial statements at this time. For WSSC, GASB No. 45 will not be effective until the year ending June 30, 2008.

B. CASH AND INVESTMENTS

Cash

At June 30, 2004 and 2003, cash per WSSC's records amounted to \$88,000 and \$59,000, respectively, and per reported bank balances was (\$695,000) and \$2,630,000, respectively. All collected bank balance funds were secured by Federal depository insurance or by collateral held in WSSC's name by the Federal Reserve Bank.

Investments

As required by State law, WSSC can invest only in obligations of the U.S. Government and U.S. Government agencies, bankers' acceptances, fully collateralized repurchase agreements, commercial paper, and certificates of deposit. Maryland State law requires the securities collateralizing repurchase agreements, commercial paper, and certificates of deposit to have a market value of at least 102 percent of the principal of the investment plus accrued interest.

At June 30, 2004 and 2003, all WSSC investments, or the collateral securities for such investments, were held by WSSC's custodial bank in WSSC's name. None of these investments required securities to be held by a broker's or dealer's trust department or agent in WSSC's name.

WSSC records short-term investments in money market instruments such as repurchase agreements and U.S. Government securities with original maturities at acquisition of less than 1 year at cost, which approximates market value. Non-current investments are recorded at market.

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

B. CASH AND INVESTMENTS (continued)

	<u>Cost</u>	<u>Market Value</u>
Investments at June 30, 2004 (in thousands):		
Short-term:		
Commercial paper	\$ 14,968	\$ 15,000
Repurchase agreements	114,669	114,669
U.S. Government securities	<u>169,762</u>	<u>169,729</u>
 Total investments (includes \$30,263 restricted for capital projects, classified as non-current)	 <u>\$299,399</u>	 <u>\$299,398</u>

	<u>Cost</u>	<u>Market Value</u>
Investments at June 30, 2003 (in thousands):		
Short-term:		
Bankers' acceptances	\$ 14,990	\$ 15,000
Repurchase agreements	69,825	69,825
U.S. Government securities	<u>194,617</u>	<u>194,825</u>
 Total investments (includes \$18,372 restricted for capital projects, classified as non-current)	 <u>\$279,432</u>	 <u>\$279,650</u>

C. RECEIVABLES

Receivables consisted of the following at June 30 (in thousands):

	<u>2004</u>	<u>2003</u>
Front foot benefit assessments accrued and billed	\$ 42,348	\$ 41,938
Water and sewer services unbilled	31,031	31,364
Water and sewer services billed	30,468	25,013
Services billed to others and miscellaneous	<u>2,517</u>	<u>5,974</u>
	106,364	104,289
Less allowance for doubtful accounts	<u>(4,262)</u>	<u>(4,030)</u>
 Total receivables, net	 <u>\$102,102</u>	 <u>\$100,259</u>

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

D. DEFERRED CHARGES AND OTHER ASSETS

Deferred charges and other assets consisted of the following at June 30 (in thousands):

	<u>2004</u>	<u>2003</u>
Net deferred cost of storm water drainage property transferred to Prince George's County	\$4,580	\$6,566
Unamortized issuance cost of refunding bonds	<u>1,391</u>	<u>2,512</u>
Total	<u>\$5,971</u>	<u>\$9,078</u>

E. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2004 was as follows (in thousands):

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets not being depreciated:				
Land and rights of way	\$ 81,420	\$ 129	\$ (611)	\$ 80,938
Construction in progress	<u>544,488</u>	<u>159,725</u>	<u>(177,587)</u>	<u>526,626</u>
Total capital assets not being depreciated	<u>625,908</u>	<u>159,854</u>	<u>(178,198)</u>	<u>607,564</u>
Capital assets being depreciated:				
Water supply	1,137,034	95,932	(956)	1,232,010
Sewage disposal	1,453,109	101,562	(308)	1,554,363
General construction	1,860,099	39,190	(2,099)	1,897,190
Other	<u>69,384</u>	<u>4,252</u>	<u>(2,504)</u>	<u>71,132</u>
Total capital assets being depreciated	<u>4,519,626</u>	<u>240,936</u>	<u>(5,867)</u>	<u>4,754,695</u>
Less accumulated depreciation for:				
Water supply	(292,000)	(24,432)	736	(315,696)
Sewage disposal	(456,240)	(32,765)	72	(488,933)
General construction	(640,789)	(37,263)	2,486	(675,566)
Other	<u>(56,791)</u>	<u>(4,435)</u>	<u>2,249</u>	<u>(58,977)</u>
Total accumulated depreciation	<u>(1,445,820)</u>	<u>(98,895)</u>	<u>5,543</u>	<u>(1,539,172)</u>
Capital assets being depreciated, net	<u>3,073,806</u>	<u>142,041</u>	<u>(324)</u>	<u>3,215,523</u>
Total capital assets, net	<u>\$ 3,699,714</u>	<u>\$301,895</u>	<u>\$ (178,522)</u>	<u>\$3,823,087</u>

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

E. CAPITAL ASSETS (continued)

Capital asset activity for the year ended June 30, 2003 was as follows (in thousands):

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets not being depreciated:				
Land and rights of way	\$ 82,250	\$ 249	\$ (1,079)	\$ 81,420
Construction in progress	<u>513,886</u>	<u>155,872</u>	<u>(125,270)</u>	<u>544,488</u>
Total capital assets not being depreciated	<u>596,136</u>	<u>156,121</u>	<u>(126,349)</u>	<u>625,908</u>
Capital assets being depreciated:				
Water supply	1,105,663	31,968	(597)	1,137,034
Sewage disposal	1,381,797	71,474	(162)	1,453,109
General construction	1,787,342	75,324	(2,567)	1,860,099
Other	<u>70,320</u>	<u>3,208</u>	<u>(4,144)</u>	<u>69,384</u>
Total capital assets being depreciated	<u>4,345,122</u>	<u>181,974</u>	<u>(7,470)</u>	<u>4,519,626</u>
Less accumulated depreciation for:				
Water supply	(269,478)	(23,132)	610	(292,000)
Sewage disposal	(427,777)	(28,506)	43	(456,240)
General construction	(603,566)	(40,431)	3,208	(640,789)
Other	<u>(55,136)</u>	<u>(5,728)</u>	<u>4,073</u>	<u>(56,791)</u>
Total accumulated depreciation	<u>(1,355,957)</u>	<u>(97,797)</u>	<u>7,934</u>	<u>(1,445,820)</u>
Capital assets being depreciated, net	<u>2,989,165</u>	<u>84,177</u>	<u>464</u>	<u>3,073,806</u>
Total capital assets, net	<u>\$ 3,585,301</u>	<u>\$240,298</u>	<u>\$ (125,885)</u>	<u>\$3,699,714</u>

The amount shown in the statements of revenues, expenses and changes in net assets for depreciation and amortization does not include depreciation of vehicles and equipment. Depreciation of these assets, \$4,435,000 in fiscal 2004 and 5,728,000 in fiscal 2003, is classified with other related operating and maintenance costs and is charged to capital assets and operations on the basis of usage, in order to facilitate the rate setting process.

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

F. CAPITAL CONTRIBUTIONS

Capital contributions consisted of the following at June 30 (in thousands):

	<u>2004</u>	<u>2003</u>
System development charges	\$35,776	\$33,278
Developer fees	8,702	6,615
Federal and State water pollution control grants	448	(388)
Donated assets:		
House connections	6,563	9,452
Other construction projects	<u>17,169</u>	<u>27,997</u>
Total	<u>\$68,658</u>	<u>\$76,954</u>

G. DEPOSITS, DEFERRED CREDITS AND OTHER LONG-TERM LIABILITIES

Deposits, deferred credits and other long-term liabilities consisted of the following at June 30 (in thousands):

	<u>2004</u>	<u>2003</u>
Deferred revenue for house connections	\$19,889	\$19,859
Deferred front foot benefit revenue	5,481	6,035
Construction deposits	4,761	4,547
House connection deposits	2,649	2,480
Other	<u>52</u>	<u>53</u>
Total	<u>\$32,832</u>	<u>\$32,974</u>

H. BONDS AND NOTES PAYABLE

Bonds and notes payable activity for the year ended June 30, 2004 was as follows (in thousands):

	<u>Beginning</u> <u>Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending</u> <u>Balance</u>	<u>Current</u> <u>Maturities</u>
Bonds and notes payable:					
Water supply	\$ 366,149	\$ 92,445	\$(113,212)	\$ 345,382	\$ 72,312
Sewage disposal	333,848	154,322	(110,858)	377,312	176,559
General construction	775,190	215,840	(253,149)	737,881	47,434
Storm water drainage	<u>6,490</u>	<u> </u>	<u>(1,950)</u>	<u>4,540</u>	<u>1,295</u>
	1,481,677	462,607	(479,169)	1,465,115	297,600
Less deferred amount	<u>(6,529)</u>	<u>(29,520)</u>	<u>34,074</u>	<u>(1,975)</u>	<u> </u>
Total bonds and notes payable	<u>\$1,475,148</u>	<u>\$ 433,087</u>	<u>\$(445,095)</u>	<u>\$1,463,140</u>	<u>\$297,600</u>

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

H. BONDS AND NOTES PAYABLE (continued)

Bonds and notes payable activity for the year ended June 30, 2003 was as follows (in thousands):

	<u>Beginning</u> <u>Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending</u> <u>Balance</u>	<u>Current</u> <u>Maturities</u>
Bonds and notes payable:					
Water supply	\$ 401,331	\$ 115,155	\$(150,337)	\$ 366,149	\$ 59,412
Sewage disposal	334,662	140,131	(140,945)	333,848	116,514
General construction	834,986	228,228	(288,024)	775,190	40,656
Storm water drainage	<u>8,690</u>	<u> </u>	<u>(2,200)</u>	<u>6,490</u>	<u>1,950</u>
	1,579,669	483,514	(581,506)	1,481,677	218,532
Less deferred amount	<u>(32,487)</u>	<u>(24,064)</u>	<u>50,022</u>	<u>(6,529)</u>	<u>—</u>
Total bonds and notes payable	<u>\$1,547,182</u>	<u>\$ 459,450</u>	<u>\$(531,484)</u>	<u>\$1,475,148</u>	<u>\$218,532</u>

The deferred amounts represent deferred interest on bond refundings and premiums on outstanding debt.

Bonds payable accrue interest at rates ranging from 1.1% to 7.875%, with an effective interest rate of 4.54% at June 30, 2004. All bonds payable at June 30, 2004, exclusive of refunded bonds, are due serially through the year 2028. Generally, the bonds are callable at a premium after a specified number of years.

Bond and note maturities and interest thereon for the next five years are as follows (in thousands):

<u>Year ended</u> <u>June 30</u>	<u>Principal</u> <u>Maturities</u>	<u>Interest</u> <u>Requirements</u>
2005	\$297,600	\$63,671
2006	129,566	58,776
2007	128,257	52,792
2008	122,467	46,452
2009	118,907	43,098

Bond and note maturities and interest thereon in five-year increments for fiscal years after 2009 are as follows (in thousands):

<u>Years ended</u> <u>June 30</u>	<u>Principal</u> <u>Maturities</u>	<u>Interest</u> <u>Requirements</u>
2010 - 2014	\$429,329	\$132,751
2015 - 2019	172,944	51,662
2020 - 2024	59,609	12,801
2025 - 2028	6,436	373

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

H. BONDS AND NOTES PAYABLE (continued)

During fiscal 2004 and 2003, WSSC issued \$85.0 million and \$52.9 million respectively of weekly maturing Bond Anticipation Notes (the Notes) to fund current construction. The Notes were remarketed weekly by WSSC's remarketing agent at prevailing weekly tax-exempt interest rates. Interest rates on the Notes ranged from .68% to 1.25% during fiscal 2004, and from .97% to 1.86% during fiscal 2003. Any or all buyers of the Notes may demand payment from WSSC's remarketing agent upon seven days notice. WSSC's remarketing agent is prepared to remarket the Notes in such eventuality. The Notes were sold under bank line of credit agreements which act as guarantees of liquidity for the Notes in the event that the Notes cannot be remarketed. The maximum amounts available under the lines of credit, which expire in June 2006 and June 2007, and are subject to certain conditions, are \$215 million and \$250 million, respectively.

WSSC gave \$9.0 million and \$3.8 million in available cash to a paying agent to redeem a portion of the Notes in fiscal year 2004 and 2003, respectively. At June 30, 2004 and 2003, \$182.1 million and \$106.1 million respectively, of the Notes were outstanding. WSSC expects to redeem these Notes with proceeds of future bond issues or annual amortization. The Notes are treated as bonds, and as such, are expected to be amortized over a 20-year term. However, because these Notes are callable, the entire \$182.1 million and an estimated \$6.4 million have been included in the 2005 principal maturities and interest requirements, respectively. Additional estimated interest requirements at prevailing rates through 2023 on these Notes, assuming future redemption from proceeds of bonds, would total \$80.4 million.

On August 5, 2003 WSSC issued an additional \$106.1 million of Notes, of which \$71.1 million was used to repay certain Notes outstanding as of June 30, 2003 and \$35 million was used to fund construction.

WSSC borrowed \$28.9 million from the 1990 and 1991 State of Maryland Water Quality Revolving Loan Program to fund the construction of certain sewage treatment facilities.

During fiscal year 2000, WSSC entered into a Master Loan Agreement with the State of Maryland Water Quality Revolving Loan Program to borrow \$107,500,000. This loan is to be used to fund the construction of a consolidated laboratory facility, a water filtration plant solids handling facility, certain sewage treatment facilities and other energy performance projects. As of June 30, 2004, WSSC had borrowed \$53,713,000 from the program.

During fiscal 2004, WSSC issued \$7.0 million of general construction bonds to fund new construction.

WSSC is in compliance with all terms of its debt agreements at June 30, 2004, and during the fiscal years ended June 30, 2004 and 2003.

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

I. BOND REFUNDINGS

In September 2003, WSSC sold \$70,590,000 of refunding bonds with interest rates ranging from 2.0% to 5.0% to current refund \$70,485,000 of outstanding callable water supply, sewage disposal and general construction bonds with interest rates ranging from 4.8% to 5.25%. The net proceeds of \$72,439,000 (including a premium of \$2,157,000 and after payment of \$203,000 of issuance costs) were used to redeem the outstanding bonds. The September 2003 refunding reduced WSSC's total debt service payments over the next 11 years by \$6,254,000 and provided an economic gain of \$6,682,000.

In October 2003, WSSC sold \$15,780,000 of Maryland Water Quality Financing Administration (MWQFA) refunding bonds with an interest rate of 1.2% to advance refund \$14,500,000 of outstanding sewage disposal bonds with interest rates ranging from 4.75% to 6.25%. The net proceeds of \$15,603,000 (after payment of \$177,000 of issuance costs) were used to purchase U.S. Government securities. Those securities were deposited with an escrow agent to provide for all future debt service payments and the early redemption of callable bonds. The October 2003 MWQFA refunding reduced WSSC's total debt service payments over the next 11 years by \$1,827,000 and provided an economic gain of \$1,950,000.

In February 2004, WSSC sold \$266,395,000 of refunding bonds with interest rates ranging from 3.0% to 5.05% to current (\$176,155,000) and advance (\$95,660,000) refund \$271,815,000 of outstanding callable water supply, sewage disposal and general construction bonds with interest rates ranging from 4.5% to 5.625%. The net proceeds of \$285,651,000 (including a premium of \$20,190,000 and after payment of \$268,000 of issuance costs) were used to redeem the outstanding bonds, and the advance portion was used to purchase U.S. Government securities. Those securities were deposited with an escrow agent to provide for all future debt service payments and the early redemption of callable bonds. The February 2004 refunding reduced WSSC's total debt service payments over the next 19 years by \$17,767,000 and provided an economic gain of \$16,677,000.

As a result of the refundings, the refunded bonds are considered to be defeased and the liability is not reflected in the financial statements.

In prior years, WSSC sold refunding bonds totalling \$2,641,100,000 for the purpose of refunding and defeasing \$2,513,335,000 of outstanding bonds. The purpose of these refundings was to reduce total debt service payments over the remaining life of the refunded bonds and to obtain an economic gain (difference between the present value of the old and new debt service payments) from the transactions.

Prior to fiscal 1994, these refundings were accounted for in accordance with Statement of Financial Accounting Standards No. 76, Extinguishment of Debt. At the time of the respective refundings, WSSC recognized extraordinary losses aggregating approximately \$89,726,000 resulting from the issuance of additional principal. However, interest savings over the remaining terms of the refunded bonds are estimated to aggregate approximately \$191,863,000.

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

I. BOND REFUNDINGS (continued)

Effective July 1, 1993, WSSC adopted GASB Statement No. 23, Accounting and Financial Reporting for Refundings of Debt Reported by Proprietary Activities (GASB No. 23). GASB No. 23 requires deferral of the difference between the reacquisition price and the carrying amount of the old debt. The difference is reported in the accompanying financial statements as a deduction from bonds payable and is being amortized to interest on bonds and notes through the year 2022 using the proportionate-to-stated interest method. Amortization totaling \$12,396,000 and \$6,894,000, in fiscal 2004 and 2003, respectively, was recorded as interest on bonds and notes payable in the accompanying statements of revenues, expenses and changes in net assets.

Details of the current year and prior years' refundings are as follows (in thousands):

<u>Date of Refunding</u>	<u>Amount of Refunded Bonds</u>	<u>Remaining Term at Refunding Date</u>	<u>Amount of Refunding Bonds</u>	<u>Estimated Interest Savings</u>	<u>Extraordinary Loss Previously Recognized</u>	<u>Deferred Loss</u>
02-01-04	\$ 271,815	19 years	\$ 266,395	\$ 10,059		\$ 14,941
10-28-03	14,500	11 years	15,780	3,107		1,103
09-15-03	70,485	11 years	70,590	5,435		2,352
03-01-03	454,905	17 years	428,945	22,269		23,612
04-15-02	43,610	10 years	43,705	4,483		904
12-01-01	100,150	14 years	100,095	9,672		(110)
11-15-97	42,400	14 years	45,265	4,967		2,712
01-01-97	74,375	23 years	79,600	7,467		4,595
01-15-94	437,695	22 years	435,675	84,556		42,761
11-01-93	243,835	22 years	278,730	38,845		28,155
03-01-93	127,975	21 years	139,705	12,908	\$ 7,730	—
06-01-92	50,475	20 years	54,775	4,896	4,200	—
11-15-91	88,355	24 years	95,435	8,083	5,580	—
05-15-91	229,775	23 years	248,865	22,276	10,944	—
03-01-90	48,395	21 years	53,885	6,700	4,216	—
10-15-86	64,160	22 years	74,680	15,000	9,182	—
05-15-86	149,055	29 years	172,490	27,000	18,542	—
07-15-85	111,750	23 years	118,015	18,000	11,002	—
04-01-84	24,765	23 years	29,210	8,000	3,797	—
09-01-77	221,660	23 years	242,025	69,000	14,533	—

The refunded bonds continue to be general obligations of WSSC until redeemed or called. However, the net proceeds of the refunding bonds were applied toward the purchase of U.S. Government obligations (held in escrow) with maturities and interest sufficient to meet debt service and call premiums, if any, on the refunded bonds. The holders of the refunded bonds have first lien on all assets held in escrow. Refunded bonds outstanding at June 30, 2004 and 2003, which amounted to \$168,355,000 and \$134,290,000, respectively, are considered to be defeased and are not reflected in the accompanying financial statements.

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

J. RETIREMENT PLAN

Plan Description

Substantially all WSSC employees participate in the Washington Suburban Sanitary Commission Employees' Retirement Plan (the Plan), which is administered by WSSC. The Plan, established in 1967, is a single-employer contributory defined benefit retirement plan. The Commission has been designated as the Plan sponsor and amendments to the Plan must be approved by the Commission. Effective July 1, 1978, WSSC approved a new version of the Plan (Open Version). Members of the Plan as of June 30, 1978 had an option through December 31, 1978 to be included in the Open Version or to continue participation in the original version of the Plan (Closed Version). The Open Version is mandatory for all new employees. It generally provides for reduced employee contributions and benefits.

The Plan requires employees under the Closed Version to contribute 6% of gross wages and employees under the Open Version to contribute 3% of gross wages as a condition of employment. Upon withdrawal from the Plan, participants are refunded their contributions plus 5% interest thereon.

The Plan provides for 100% vesting of retirement benefits after five years of credited service. Generally, the normal retirement benefits payable to an eligible participant are equal to the sum of 2.1% of the participant's final average monthly compensation times Closed Version credited service, if applicable, plus 1.4% of final average monthly compensation, as defined, times Open Version credited service.

Actuarial Assumptions

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Significant actuarial assumptions used in the most recent valuation, as of June 30, 2003, are as follows:

Actuarial method	Frozen initial liability modification of the entry age normal method.
Rate of return on investments	8%
Yearly increase in cost of living	3.5%
Yearly increase in salary scale	5.0%
Yearly increase in total payroll	5.0%
Annual rates of severance prior to retirement	Severance due to withdrawal is based on WSSC experience. Severance due to mortality or disability is based on published rates adjusted to reflect actual experience.
Mortality rates after retirement	Group Annuity - 1983 tables adjusted.
Retirement age assumptions	Ranging from age 45 to 69.

WASHINGTON SUBURBAN SANITARY COMMISSION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

J. RETIREMENT PLAN (continued)

Actuarially Determined Contribution Requirements
And Contribution Made

WSSC's retirement plan funding policy provides for actuarially determined yearly contributions calculated on a level percentage of payroll costs basis. The covered payroll used by the actuary in determining the contribution was \$80,448,000, and the total actual payroll was \$89,065,000. The significant actuarial assumptions used to compute the actuarially determined contribution requirement are the same as those previously described.

WSSC's annual pension cost and long-term pension liability for fiscal 2004 and fiscal 2003 are (in thousands):

	<u>2004</u>	<u>2003</u>
Annual required contribution	\$ 8,574	\$ 6,577
Interest on Long-term Pension Liability	<u>3,284</u>	<u>3,502</u>
Annual Pension Cost	11,858	10,079
Contributions Made	(14,808)	(14,746)
Decrease in Long-term Pension Liability	(2,950)	(4,667)
Long-term Pension Liability – beginning of year	<u>47,278</u>	<u>51,945</u>
Long-term Pension Liability – end of year	<u>\$44,328</u>	<u>\$47,278</u>

The difference between the amount contributed and the amount charged to operating expenses and utility plant is recorded as a reduction to the long-term pension liability. The annual required contribution for the current year was determined as part of an annual actuarial valuation.

Historical Trend Information

The historical trend information designed to provide information about the Plan's progress made in accumulating sufficient assets to pay benefits when due is presented in Schedule A.

Six-year historical trend information showing the Plan's progress is presented in the Plan's December 31, 2003 comprehensive annual financial report, which can be requested from WSSC's offices.

Retirement Restoration Plan

Effective July 1, 1995, WSSC established the Washington Suburban Sanitary Commission Employees' Retirement Restoration Plan (the Restoration Plan), a non-qualified plan. The purpose of the Restoration Plan is to restore most of the benefits foregone by participants in the WSSC Employees' Retirement Plan when such benefits are limited by the maximum benefit provisions of Section 415 of the Internal Revenue Code. During fiscal years 2004 and 2003, the Restoration Plan paid benefits totaling \$31,000 and \$37,000, respectively.

WASHINGTON SUBURBAN SANITARY COMMISSION
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FOR THE YEARS ENDED JUNE 30, 2004 AND 2003

J. RETIREMENT PLAN (continued)

Post Retirement Benefits

In addition to providing pension benefits, WSSC provides certain health care and life insurance benefits for retired employees.

Eligibility for post retirement health care benefits requires a minimum of two years participation in a WSSC sponsored plan immediately prior to retirement. At the end of fiscal 2004, substantially all of the 1,417 retired employees (or beneficiaries) are eligible for those benefits. WSSC contributes from 78% to 80% of the amount of health care insurance costs for eligible retired employees and their families. Health care benefits are expensed as insurance costs are incurred, rather than over the service life of the employee. During fiscal 2004 and 2003, WSSC expensed approximately \$8,404,000 and \$7,444,000, respectively, for post retirement benefits. If such costs were accrued over the lives of employees, the amount expensed on an annual basis would be substantially greater and a liability for amounts to be funded in the future for services rendered to date would need to be recorded.

Employees who retired in 1982 and after are eligible for post retirement life insurance benefits. The amount of retiree life insurance begins at 85% of the employee's salary as of the day immediately prior to retirement, and decreases over a four year period, until coverage equals either 25% of that salary or \$5,000, whichever is greater. During fiscal 2004, WSSC paid premiums of \$58,000 for 1,004 retirees, and, during fiscal 2003, paid \$67,000 for 989 retirees. The cost of these benefits are expensed when the premiums are paid, rather than over the service life of the employee.

K. DEFERRED COMPENSATION PLAN

WSSC offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The deferred compensation plan, available to all employees, permits them to defer a portion of their salaries until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency. All of the assets of the deferred compensation plan are held in a trust for the exclusive benefit of participants and beneficiaries. Participants' rights under the plan are equal to the fair market value of the deferred account for each participant.

L. COMMITMENTS AND CONTINGENCIES

Construction expenditures for fiscal 2005 are not expected to exceed \$226 million, a portion of which will be funded by capital contributions. Commitments in connection with this construction program approximated \$33 million at June 30, 2004.

Intermunicipal agency sewage disposal expenses are accrued as incurred, based on estimates. These expenses are subject to audit by WSSC and others.

WASHINGTON SUBURBAN SANITARY COMMISSION
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L. COMMITMENTS AND CONTINGENCIES (continued)

WSSC administers several Federal and State grants. The grant funds expended are subject to compliance audits by the grantors. During fiscal 2004 and 2003, WSSC and the United States Environmental Protection Agency (EPA) settled certain grants that were being audited by the EPA. These settlements did not have a significant impact on WSSC's financial position or changes in net assets.

The United States Department of Justice, the United States Environmental Protection Agency and the Maryland Department of the Environment (collectively "the Regulators") allege that sanitary sewer overflows ("SSOs") from WSSC's sanitary sewer collection system are violations of the Federal Clean Water Act and analogous State law and have proposed certain remedial measures to be undertaken by WSSC to eliminate and/or reduce such occurrences. Federal agencies are pursuing similar enforcement actions nationally against public wastewater treatment system owners. Remedies available to the federal and state regulators include civil penalties up to \$31,500 per violation and injunctive relief requiring WSSC to undertake corrective measures. WSSC and the Regulators are currently in negotiations in an attempt to resolve the enforcement action through the entry of a mutually agreeable Consent Decree. These negotiations, which began in March 2002 and will continue into fiscal year 2005 involve alleged SSO occurrences for a seven and one-half year period. During this time, there have been approximately 950 to 1,100 SSOs experienced by WSSC. WSSC continues to contest this action and the initial remedial measures proposed by the Regulators. At this point in the negotiations, it is not possible for WSSC's legal counsel to assess whether the negotiations will result in the entry of a Consent Decree agreeable to the WSSC. It is expected, however, that if the parties are able to resolve this matter through the entry of a mutually agreeable Consent Decree, the cost of remedial measures undertaken pursuant to the Decree would be several hundred million dollars over a 10 to 15 year term. Not all of this cost would be attributable solely to the Consent Decree, however, a significant portion of the remedial measures currently under consideration are already included in WSSC's budget and capital improvements program. If the parties are unable to resolve this matter through the entry of a Consent Decree, the Regulators will likely file suit in federal court seeking broad remedial measures and the imposition of civil penalties. If such a suit is filed, WSSC intends to contest the allegations strenuously and the likely remedial measures requested.

WSSC is involved in judicial, condemnation and administrative proceedings including matters discussed in the previous paragraph. These actions include personal injury, property damage and personnel claims and various claims filed by contractors against WSSC for cost overruns on construction contracts. While the outcomes of these matters are uncertain, it is the opinion of management and WSSC's General Counsel that resolution of all claims outstanding will not have a material adverse effect on the financial position or changes in net assets of WSSC.

WASHINGTON SUBURBAN SANITARY COMMISSION
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L. COMMITMENTS AND CONTINGENCIES (continued)

WSSC purchases insurance on its property (structures, contents, boiler and machinery, etc.) for physical damages where it has been determined that a reasonable amount of exposure exists. In addition, WSSC is self-insured for workers' compensation in accordance with the statutory requirements of the State of Maryland. The workers' compensation accrued liability includes an estimate for claims incurred but not yet reported to the claims administrator. WSSC also maintains crime and terrorism insurance and fiduciary liability policies having various self-insured retention levels.

WSSC is self-insured for all public liability. Each year, funds are budgeted for normal claims. However, should the past loss experience change, or should a catastrophic loss occur in excess of applicable insurance coverage, funds for such loss or losses would have to be obtained from ad valorem taxation or other sources of revenue since a self-insurance fund has not been established.

During fiscal 2004 and 2003, WSSC leased various equipment with annual rental payments of approximately \$275,000 and \$456,000 respectively. There are no annual commitments under long term non-cancelable operating leases as of June 30, 2004.

**WASHINGTON SUBURBAN SANITARY COMMISSION
 REQUIRED SUPPLEMENTAL INFORMATION
 SCHEDULE OF HISTORICAL PENSION INFORMATION
 Unaudited
 (In thousands)**

SCHEDULE A

Actuarial Valuation Date <u>June 30</u>	Actuarial Value of <u>Assets</u>	Actuarial Accrued <u>Liability</u>	Unfunded Actuarial Accrued <u>Liability (UAAL)</u>	Funded <u>Ratio</u>	Covered <u>Payroll</u>	UAAL as a Percentage of <u>Covered Payroll</u>
2001	\$546,267	\$613,077	\$66,811	89.1%	\$77,423	86.3%
2002	538,099	594,414	56,316	90.5	80,448	70.0
2003	530,071	579,970	49,899	91.4	86,048	58.0

Fiscal Year Ended <u>June 30</u>	Annual Pension Cost (APC) <u> </u>	Percentage of <u>APC Contributed</u>	Long-Term Pension <u>Liability</u>
2002	\$5,873	251%	\$51,945
2003	10,079	146	47,278
2004	11,858	125	44,328