

In the opinion of Bond Counsel, under existing law and assuming continued compliance with the Internal Revenue Code of 1986, as amended, interest on the Series A/B Bonds is not included in gross income for federal income tax purposes and is not an item of tax preference for the purpose of computing the alternative minimum tax imposed on individuals and corporations. However, interest on the Series A/B Bonds will be taken into account in determining adjusted current earnings for the purpose of computing the alternative minimum tax imposed upon certain corporations. In the opinion of Bond Counsel, the Series A/B Bonds, their transfer and the income therefrom, including any profit made on the sale thereof, are exempt from Massachusetts personal income taxes and the Series A/B Bonds are exempt from Massachusetts personal property tax. For federal and Massachusetts tax purposes, interest includes original issue discount. See "Tax Exemption" herein.



\$847,950,000
MASSACHUSETTS WATER RESOURCES AUTHORITY
\$200,000,000 General Revenue Bonds, 2007 Series A
\$647,950,000 General Revenue Refunding Bonds, 2007 Series B

Dated: Date of Delivery**Due: August 1, as shown on the inside cover page hereof**

The Series A/B Bonds will be issued as fully registered bonds and will be registered in the name of Cede & Co., as nominee for The Depository Trust Company ("DTC"), New York, New York. Purchases of the Series A/B Bonds will be made in book-entry form only, in the denominations of \$5,000 or any integral multiple thereof, and no physical delivery of the Series A/B Bonds will be made to purchasers. So long as Cede & Co. is the registered owner of the Series A/B Bonds, principal and semiannual interest (payable February 1 and August 1, commencing August 1, 2007) are payable to DTC by U.S. Bank National Association, as Trustee. See "The Series A/B Bonds – Book-Entry Only System." A portion of the Series A/B Bonds is subject to redemption prior to maturity as described herein.

The Series A/B Bonds will constitute general obligations of the Massachusetts Water Resources Authority (the "Authority"). In addition, the Series A/B Bonds will be secured by a lien on and pledge of certain revenues and other moneys of the Authority. Neither The Commonwealth of Massachusetts (the "Commonwealth") nor any political subdivision thereof shall be obligated to pay the principal of, premium, if any, or interest on any Series A/B Bond, and neither the faith and credit nor the taxing power of the Commonwealth or any political subdivision thereof is pledged to such payment. The Authority has no taxing power.

The scheduled payment of principal of and interest on the Series A/B Bonds when due will be guaranteed under a municipal insurance policy to be issued concurrently with the delivery of the Series A/B Bonds by Financial Security Assurance Inc. ("Financial Security").

[FSA logo]

The Series A/B Bonds are offered when, as and if issued by the Authority and received by the Underwriters, subject to the approval of legality by Ropes & Gray LLP, Boston, Massachusetts, Bond Counsel, and certain other conditions. Certain legal matters will be passed upon for the Authority by its Disclosure Counsel, Edwards Angell Palmer & Dodge LLP, Boston, Massachusetts, and for the Underwriters by their counsel, Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C., Boston, Massachusetts. Delivery of the Series A/B Bonds to DTC or its custodial agent is expected in New York, New York on or about February 1, 2007.

Bear, Stearns & Co. Inc.

Goldman, Sachs & Co.
Citigroup
First Albany Capital Inc.

Lehman Brothers

Merrill Lynch & Co.

Morgan Stanley

JPMorgan
UBS Investment Bank
Raymond James & Associates, Inc.

January 17, 2007

[†]See "Ratings" herein.

Massachusetts Water Resources Authority

\$200,000,000

General Revenue Bonds, 2007 Series A

<u>Maturity</u> <u>(August 1)</u>	<u>Amount</u>	<u>Rate</u>	<u>Yield</u>	<u>Maturity</u> <u>(August 1)</u>	<u>Amount</u>	<u>Rate</u>	<u>Yield</u>
2022*	\$2,000,000	5.00%	4.03%	2026*	\$2,000,000	5.00%	4.13%
2023*	2,000,000	5.00	4.05	2027*	2,000,000	5.00	4.15
2024*	2,000,000	5.00	4.09	2028*	2,000,000	5.00	4.16
2025*	2,000,000	5.00	4.11				

\$29,450,000 4.375% Term Bond due August 1, 2032 – Yield 4.48%

\$35,180,000 4.50% Term Bond due August 1, 2036 – Price 100%

\$121,370,000 4.50% Term Bond due August 1, 2046 – Yield 4.58%

* Priced to call at par on February 1, 2017.

\$647,950,000

General Revenue Refunding Bonds, 2007 Series B

<u>Maturity</u> <u>(August 1)</u>	<u>Amount</u>	<u>Rate</u>	<u>Yield</u>	<u>Maturity</u> <u>(August 1)</u>	<u>Amount</u>	<u>Rate</u>	<u>Yield</u>
2023	\$45,675,000	5.25%	4.11%	2031	\$30,130,000	5.25%	4.210%
2024	48,140,000	5.25	4.13	2032	27,295,000	5.25	4.220
2025	50,735,000	5.25	4.15	2033	34,575,000	5.25	4.225
2026	53,470,000	5.25	4.16	2034	26,980,000	5.25	4.230
2027	56,350,000	5.25	4.17	2035	19,515,000	5.25	4.235
2028	59,390,000	5.25	4.18	2036	34,180,000	5.25	4.240
2029	62,595,000	5.25	4.19	2037	14,995,000	5.25	4.245
2030	65,695,000	5.25	4.20	2038	17,960,000	5.25	4.250

The information set forth herein has been obtained from the Authority, The Depository Trust Company, Financial Security and other sources that are deemed to be reliable but, as to information from sources other than the Authority, it is not to be construed as a representation of the Authority. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale of the Series A/B Bonds shall under any circumstances create any implication that there has been no change in the affairs of the Authority since the date hereof.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, their responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

No dealer, broker, salesperson or other person has been authorized to give any information or to make any representation other than as contained in this Official Statement and, if given or made, such other information or representation must not be relied upon as having been authorized by the Authority. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of the Series A/B Bonds by any person in any jurisdiction in which it is unlawful for such person to make such offer, solicitation or sale.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVERALLOT OR EFFECT TRANSACTIONS TO STABILIZE OR MAINTAIN THE MARKET PRICES OR YIELDS OF THE SERIES A/B BONDS AT A LEVEL ABOVE THAT WHICH MAY OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

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MASSACHUSETTS WATER RESOURCES AUTHORITY

Board of Directors

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Frederick A. Laskey, *Executive Director*

Financial Advisors

Public Financial Management, Inc.
Lamont Financial Services Corporation

Consulting Engineer

Camp Dresser & McKee Inc.

Bond Counsel

Ropes & Gray LLP

Disclosure Counsel

Edwards Angell Palmer & Dodge LLP

Independent Accountants

KPMG LLP

Bond Trustee

U.S. Bank National Association

OFFICIAL STATEMENT
OF THE
MASSACHUSETTS WATER RESOURCES AUTHORITY
RELATING TO

\$200,000,000 General Revenue Bonds, 2007 Series A
\$647,950,000 General Revenue Refunding Bonds, 2007 Series B

INTRODUCTION

Purpose. This Official Statement provides certain information concerning the Massachusetts Water Resources Authority (the “Authority”) in connection with the sale of its \$200,000,000 aggregate principal amount of General Revenue Bonds, 2007 Series A (the “Series A Bonds”) and its \$647,950,000 aggregate principal amount of General Revenue Refunding Bonds, 2007 Series B (the “Series B Bonds” and together with the Series A Bonds, the “Series A/B Bonds”). The Series A/B Bonds are to be issued under and secured by the Authority’s General Revenue Bond Resolution adopted January 24, 1990, as amended and supplemented (the “General Resolution”). In addition, the Series A/B Bonds will be issued and secured under the Authority’s Fifty-second Supplemental Resolution, approved by the Authority by resolution adopted on January 10, 2007 (the “Supplemental Resolution”). The Series A/B Bonds will constitute valid and binding general obligations of the Authority and will be further secured by a pledge of certain revenues of the Authority in accordance with the terms of the General Resolution on a parity basis with other outstanding Bonds of the Authority. See “Security for the Series A/B Bonds – General,” “– Outstanding Indebtedness” and “– Additional Indebtedness.” In addition, payment of the principal of and interest on the Series A/B Bonds when due will be guaranteed by a municipal bond insurance policy to be issued by Financial Security Assurance Inc. (“Financial Security”). See “Bond Insurance” and Appendix F. The proceeds of the Series A/B Bonds will be used to finance costs of the Authority’s capital program, to pay certain of the Authority’s outstanding tax-exempt commercial paper notes, which financed a portion of the Authority’s capital program, and to advance and currently refund certain Outstanding Bonds. See “Application of Series A/B Bond Proceeds and Other Moneys.”

The Authority. The Authority, established by the Massachusetts Water Resources Authority Act, Chapter 372 of the Acts of 1984 of The Commonwealth of Massachusetts (as amended, the “Act”), is a body politic and corporate, a public instrumentality and an independent public authority of The Commonwealth of Massachusetts (the “Commonwealth”). In 1985, the Authority assumed possession and control from the Metropolitan District Commission (the “MDC”) (which became part of the Department of Conservation and Recreation (the “DCR”) in July 2003), a department of the Commonwealth, of a water distribution system (the “Waterworks System”) and a sewer system (the “Sewer System”) (collectively, the “Systems”), which provide wholesale services in service areas encompassing, in whole or in part, 61 communities located primarily in eastern Massachusetts, including most of the metropolitan Boston area. Forty-nine cities, towns and special purpose entities currently are authorized to receive water from the Waterworks System. Forty-three cities, towns and special purpose entities connect their local sewer systems to the regional sewage collection and treatment facilities constituting the Sewer System. Approximately 2.6 million people, or approximately 43% of the total population of the Commonwealth, live in the Authority’s service areas. See “The Authority and its Service Areas.”

The Capital Improvement Program. In addition to its operating responsibilities, the Authority is responsible for rehabilitating, repairing and maintaining the Systems and for operating them in compliance with applicable environmental laws, including major facilities construction to comply with the requirements of the federal Safe Drinking Water Act (the “SDWA”) and the federal Clean Water Act. Since its assumption of the ownership and operations of the Systems in 1985, the Authority has undertaken an ambitious program of capital improvements to the Systems (the “CIP”), with estimated expenditures for Fiscal Years 1986 through 2016 and beyond of approximately \$7.9 billion, including completed expenditures of approximately \$6.7 billion through December 1, 2006. The Authority has completed most of the major projects in the CIP. For a discussion of major projects completed since 1985, see “Capital Improvement Program-Summary of Capital Investment” herein.

The largest component of the Authority's current CIP is related to the implementation of the CSO Facilities Plan and Environmental Impact Report (the "CSO Control Plan"), which is intended to address the discharge of combined wastewater and stormwater overflows ("CSOs") into certain waterways during heavy rainstorms. In April 2006, the Federal District Court approved a joint motion filed by the U.S. Department of Justice ("DOJ") and the Authority, which incorporated into the court order changes to the CSO Control Plan agreed to by the parties. The joint motion provides greater certainty as to the scope of the Authority's CSO obligations through 2020. The Authority's Proposed Fiscal Year 2008 CIP (the "Proposed FY08 CIP") includes the 35 projects contained in the CSO Control Plan. Sixteen of the 35 projects are complete, and eight more are in construction. See "The Systems – The Sewer System – Combined Sewer Overflows; Infiltration and Inflow" and "Capital Improvement Program – Major Capital Projects – Wastewater Projects."

The Authority has completed most of the major capital improvement projects in its Integrated Water Supply Improvement Program designed to protect and improve the quality of water delivered through the Waterworks System, including projects mandated by the SDWA. The largest of these projects, the MetroWest Water Supply Tunnel, was placed in service in November 2003. Two other major components of the Waterworks System capital improvements are the Norumbega Covered Storage Reservoir and the John J. Carroll Water Treatment Plant. The Norumbega facility came on line in November 2003, eliminating open air distribution storage reservoirs. The John J. Carroll Water Treatment Plant came on line in July 2005.

The Authority is developing a master plan ("Master Plan"), expected to be completed in Fiscal Year 2007, for the repair, maintenance, rehabilitation, replacement and additional construction of its infrastructure. Because the majority of court-mandated projects are complete, the Master Plan is intended to assess Authority-wide needs, to identify and prioritize projects to address those needs, and to establish timeframes for rehabilitation and replacement of existing facilities and infrastructure and construction of new projects. In December 2006, the Authority's Board approved the transmittal of the Proposed FY08 CIP to the Advisory Board. The Authority's Proposed FY08 CIP restores priority capital projects removed from the CIP following the loss of debt service assistance funding from the Commonwealth in Fiscal Year 2003 and incorporates the highest priority projects identified in the Master Plan which have projected spending in the Fiscal Year 2009 to Fiscal Year 2018 timeframe. The Proposed FY08 CIP establishes a five-year capital spending cap for the five Fiscal Years 2009 through 2013 of \$1 billion and incorporates the recommendations established in the Master Plan. See "Capital Improvement Program – Capital Improvement Planning" herein.

The Authority reviews and reevaluates the CIP from time to time and adjusts it, as necessary, to respond to changing factors, such as changing environmental law and mandates, including requirements of the Clean Water Act and the SDWA, construction industry costs, and unforeseen physical conditions that can affect both the cost and timing of particular projects.

For further information on the CIP, see "Capital Improvement Program," "Environmental Regulation and Litigation" and Appendix B – Supplemental Engineering and Financial Feasibility Report."

Rates and Charges. In Fiscal Year 2007, approximately 90% of the Authority's revenues are budgeted to be derived from wholesale rates and charges assessed to the cities, towns and special purpose entities (collectively, the "Local Bodies") which are served by the Systems. One Local Body, the Boston Water and Sewer Commission (the "BWSC"), a public instrumentality of the Commonwealth providing retail water and sewer services within the City of Boston, will account for approximately 32% of the Authority's combined water and sewer charges in Fiscal Year 2007. The obligation to pay the Authority's rates and charges for services rendered is a general obligation of each Local Body, supported by its full faith and credit and payable from all available revenue sources, including local retail user charges and, in the case of city and town Local Bodies ("Municipal Local Bodies") only, real and personal property taxes and financial aid distributed to such Municipal Local Bodies by the Commonwealth ("local aid"). No specific revenues of the Local Bodies, however, are pledged for the payment of the Authority's wholesale rates and charges. Since its inception, the Authority has collected 100% of its rates and charges within the fiscal year in which they were due.

The Authority is required by the Act to set its rates and charges at levels sufficient to pay, among other things, its current expenses and its debt service, and is required by the General Resolution to provide debt service coverage at specified levels. In accordance with the Act, the Authority's rate-setting responsibility is exercised by its Board of Directors independent of the approval of any department, agency or other instrumentality of the Commonwealth or any other governmental body. The Authority's rate-setting is not subject to certain limitations imposed by the Massachusetts

law, commonly known as “Proposition 2½”, on the rate of growth of assessments by state and other governmental entities on municipalities. See “Local Bodies – Municipal Sources of Revenue.”

From Fiscal Year 2003 through Fiscal Year 2007, the average annual increase in the Authority’s rates and charges was approximately 4.2%, with a 4.9% increase in Fiscal Year 2007 as adopted in the Fiscal Year 2007 Current Expense Budget (the “FY07 CEB”). The Authority expects to receive approximately \$18.75 million of debt service assistance from the Commonwealth in Fiscal Year 2007, which was reflected in the FY07 CEB. See “Rates and Charges – Historical Rates and Charges” and “Legislative and Other Developments.” From Fiscal Year 2007 to Fiscal Year 2012, the Authority projects that future rates and charges will increase significantly due to increases in debt service costs and the annual operating expenses of the Systems. The Authority believes that economic and environmental benefits of an improved infrastructure help to maintain public support for its CIP and expects that these considerations, together with the statutory enforcement mechanisms available to it for collection of its rates and charges, will continue to assure that the Authority’s revenue requirements are met. See “Rates and Charges – Future Rates and Charges” and “– Enforcement.”

Appendices. Attached hereto as Appendix A is the report of the Authority’s independent accountants on the Authority’s financial statements at June 30, 2006 and for the Fiscal Year then ended. Attached hereto as Appendix B is the Supplemental Engineering and Financial Feasibility Report prepared by Camp Dresser & McKee Inc., the Authority’s consulting engineer (the “Consulting Engineer”) dated as of November 15, 2006, as supplemented by the Consulting Engineer’s Letter dated January 11, 2007 (together, the “Supplemental Feasibility Report”), in connection with the Series A/B Bonds. The Engineering and Financial Feasibility Report dated as of February 23, 2006 (the “February Report” and together with the Supplemental Feasibility Report, the “Feasibility Report”) prepared by the Consulting Engineer and included as Appendix B to the Official Statement dated March 2, 2006 with respect to the Authority’s General Revenue Bonds, 2006 Series A and General Revenue Refunding Bonds, 2006 Series B, is incorporated herein by reference. Attached hereto as Appendix C is a Summary of Certain Provisions of the General Resolution prepared by Bond Counsel to the Authority. Attached hereto as Appendix D is the proposed form of legal opinion of Bond Counsel. Appendix E is the Table of Refunded Bonds. Appendix F contains the Specimen Municipal Bond Insurance Policy to be issued by Financial Security with respect to the Series A/B Bonds.

THE SERIES A/B BONDS

The following is a summary of certain provisions of the Series A/B Bonds. Reference is hereby made to the Series A/B Bonds and the General Resolution, each in its entirety, for detailed provisions of the Series A/B Bonds.

GENERAL

The Series A/B Bonds shall be dated their date of delivery and shall bear interest from such date payable semiannually on each February 1 and August 1, commencing August 1, 2007, at the rates per annum shown on the inside cover page hereof. Interest on the Series A/B Bonds will be calculated on the basis of twelve 30-day months for a 360-day year. The Series A/B Bonds shall mature on the dates and in the principal amounts shown on the inside cover page hereof.

REDEMPTION PROVISIONS

Mandatory Sinking Fund Redemption. The Series A Bonds maturing August 1, 2032, August 1, 2036 and August 1, 2046 shall be subject to mandatory sinking fund redemption and shall be redeemed by sinking fund installments on August 1 of each of the years and in the amounts set forth in the following table at a redemption price equal to 100% of the principal amount thereof plus accrued interest to the date of redemption:

Series A Bonds due August 1, 2032

<u>Year</u>	<u>Sinking Fund Installment</u>
2029	\$6,885,000
2030	7,195,000
2031	7,515,000
2032 [†]	7,885,000

[†] Stated Maturity.

Series A Bonds due August 1, 2036

<u>Year</u>	<u>Sinking Fund Installment</u>
2033	\$8,210,000
2034	8,590,000
2035	8,985,000
2036 [†]	9,395,000

[†] Stated Maturity.

Series A Bonds due August 1, 2046

<u>Year</u>	<u>Sinking Fund Installment</u>
2037	\$ 9,830,000
2038	10,280,000
2039	10,755,000
2040	11,250,000
2041	11,770,000
2042	12,310,000
2043	12,875,000
2044	13,470,000
2045	14,090,000
2046 [†]	14,740,000

[†] Stated Maturity.

The Series B Bonds are not subject to mandatory sinking fund redemption.

Optional Redemption. The Series A Bonds shall be subject to optional redemption prior to maturity in whole or in part on any date, beginning on February 1, 2017, at the option of the Authority and in such order of maturity or sinking fund installments as may be determined by the Authority, at a redemption price of par plus accrued interest to the date of redemption.

The Series B Bonds are not subject to optional redemption prior to maturity.

Notice of Redemption and Other Notices. So long as The Depository Trust Company (“DTC”), New York, New York, or its nominee is the Bondholder, the Authority and the Trustee will recognize DTC or its nominee as the Bondholder for all purposes, including notices and voting. Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory and regulatory requirements as may be in effect from time to time.

The Trustee shall give notice of redemption to the Bondholders not less than thirty (30) days or more than forty-five (45) days prior to the date fixed for redemption. Failure to mail notice to a particular Bondholder, or any defect in the notice to such Bondholder, shall not affect the redemption of any other Bond. So long as DTC or its nominee is the Bondholder, any failure on the part of DTC or failure on the part of a nominee of a Beneficial Owner (having received notice from a Direct Participant or otherwise) to notify the Beneficial Owner so affected, shall not affect the validity of the redemption.

Notice of optional redemption of any Series A Bonds may and, if the Authority shall so instruct the Trustee, shall be given conditionally. If and to the extent that any conditions specified or referred to in a notice of redemption are not satisfied on or prior to the proposed redemption date and, if not satisfied, are not waived by the Authority, then such

Series A Bonds shall not be redeemed pursuant to such notice and shall remain outstanding in accordance with their terms.

Selection for Redemption. In the event that less than all of the Series A/B Bonds of any one maturity are to be redeemed and for so long as the book-entry system remains in effect for the Series A/B Bonds, the portion of any Series A/B Bond of a particular maturity to be redeemed shall be selected by DTC in such manner as DTC may determine. If the book-entry only system for the Series A/B Bonds is no longer in effect, selection for redemption of less than all the Series A/B Bonds of any one maturity will be made by the Trustee by lot or in any other manner of selection the Trustee in its discretion shall deem appropriate and fair.

BOOK-ENTRY ONLY SYSTEM

DTC will act as securities depository for the Series A/B Bonds. The Series A/B Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Series A/B Bond certificate will be issued for each maturity of the Series A/B Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC, the world's largest depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2.2 million issues of U.S. and non-U.S. equity, corporate and municipal debt issues, and money market instruments from over 100 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Fixed Income Clearing Corporation, and Emerging Markets Clearing Corporation, ("NSCC", "FICC", and "EMCC", also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtc.org or www.dtcc.com.

Purchases of Series A/B Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Series A/B Bonds on DTC's records. The ownership interest of each actual purchaser of each Security ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Series A/B Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Series A/B Bonds, except in the event that use of the book-entry system for the Series A/B Bonds is discontinued.

To facilitate subsequent transfers, all Series A/B Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Series A/B Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Series A/B Bonds; DTC's records reflect only the identity of the Direct Participants to

whose accounts such Series A/B Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices shall be sent to DTC. If less than all of the Series A/B Bonds within a maturity are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such maturity to be redeemed.

Neither DTC nor Cede & Co. (nor such other DTC nominee) will consent or vote with respect to Series A/B Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Authority as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Series A/B Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the Series A/B Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Authority or the Trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC (nor its nominee), the Trustee, or the Authority, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Authority or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as securities depository with respect to the Series A/B Bonds at any time by giving reasonable notice to the Authority or the Trustee. Under such circumstances, in the event that a successor securities depository is not obtained, Series A/B Bond certificates are required to be printed and delivered.

The Authority may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Series A/B Bond certificates will be printed and delivered to DTC.

The information contained in this section concerning DTC and DTC's book-entry system has been obtained from sources that the Authority believes to be reliable, but the Authority takes no responsibility for the accuracy thereof. Neither the Trustee nor the Authority will have any responsibility or obligation to such DTC Participants or the persons for whom they act as nominees with respect to the payments to the DTC Participants, the Indirect Participants or Beneficial Owners.

EXCHANGE AND TRANSFER

If for any reason the book-entry only system is discontinued, the Series A/B Bonds will be exchangeable and transferable on the registration books of the Authority at the designated corporate trust office of the Trustee in denominations of \$5,000 of principal amount or any whole multiple thereof. Upon presentation and surrender of any Series A/B Bond for transfer or exchange, the Trustee will authenticate and deliver in the name of the designated transferee or transferees or the registered owner, as appropriate, one or more new fully registered Series A/B Bonds in any authorized denomination or denominations. For every exchange or transfer of Series A/B Bonds, the Authority or the Trustee may make a charge sufficient to reimburse it for any tax, fee or other governmental charge required to be paid with respect to such exchange or transfer. The Authority shall not be obligated to make any transfer or exchange of any Series A/B Bonds during the 15-day period preceding an interest or principal payment date. Neither the Authority nor the Trustee shall be required to transfer or exchange the Series A/B Bonds for a period of fifteen days next preceding the mailing of any notice of redemption or to transfer or exchange any Series A/B Bond called for redemption.

BOND INSURANCE

INVESTORS SHOULD BE AWARE THAT THE FOLLOWING TEXT OF THIS SECTION WAS FURNISHED BY FINANCIAL SECURITY ASSURANCE INC. THESE PROVISIONS SHOULD BE READ IN CONJUNCTION WITH THIS OFFICIAL STATEMENT AS A WHOLE. THE AUTHORITY DOES NOT AND CANNOT MAKE ANY REPRESENTATION REGARDING THESE MATTERS. REFERENCE IS MADE TO APPENDIX F FOR A SPECIMEN OF FINANCIAL SECURITY ASSURANCE INC.'S MUNICIPAL BOND INSURANCE POLICY.

BOND INSURANCE POLICY

Concurrently with the issuance of the Series A/B Bonds, Financial Security will issue its Municipal Bond Insurance Policy for the Series A/B Bonds (the "Policy"). The Policy guarantees the scheduled payment of principal of and interest on the Series A/B Bonds when due as set forth in the form of the Policy included as an exhibit to this Official Statement.

The Policy is not covered by any insurance security or guaranty fund established under New York, California, Connecticut or Florida insurance law.

FINANCIAL SECURITY ASSURANCE INC.

Financial Security is a New York domiciled financial guaranty insurance company and a wholly owned subsidiary of Financial Security Assurance Holdings Ltd. ("Holdings"). Holdings is an indirect subsidiary of Dexia, S.A., a publicly held Belgian corporation, and of Dexia Credit Local, a direct wholly-owned subsidiary of Dexia, S.A. Dexia, S.A., through its bank subsidiaries, is primarily engaged in the business of public finance, banking and asset management in France, Belgium and other European countries. No shareholder of Holdings or Financial Security is liable for the obligations of Financial Security.

At September 30, 2006, Financial Security's combined policyholders' surplus and contingency reserves were approximately \$2,581,107,000 and its total net unearned premium reserve was approximately \$1,992,163,000 in accordance with statutory accounting principles. At September 30, 2006, Financial Security's consolidated shareholder's equity was approximately \$3,058,987,000 and its total net unearned premium reserve was approximately \$1,590,538,000 in accordance with generally accepted accounting principles.

The consolidated financial statements of Financial Security included in, or as exhibits to, the annual and quarterly reports filed after December 31, 2005 by Holdings with the Securities and Exchange Commission are hereby incorporated by reference into this Official Statement. All financial statements of Financial Security included in, or as exhibits to, documents filed by Holdings pursuant to Section 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 after the date of this Official Statement and before the termination of the offering of the Series A/B Bonds shall be deemed incorporated by reference into this Official Statement. Copies of materials incorporated by reference will be provided upon request to Financial Security Assurance Inc.: 31 West 52nd Street, New York, New York 10019, Attention: Communications Department (telephone (212) 826-0100).

The Policy does not protect investors against changes in market value of the Series A/B Bonds, which market value may be impaired as a result of changes in prevailing interest rates, changes in applicable ratings or other causes. Financial Security makes no representation regarding the Series A/B Bonds or the advisability of investing in the Series A/B Bonds. Financial Security makes no representation regarding the Official Statement, nor has it participated in the preparation thereof, except that Financial Security has provided to the Authority the information presented under this caption for inclusion in the Official Statement.

APPLICATION OF SERIES A/B BOND PROCEEDS AND OTHER MONEYS

GENERAL

The proceeds of the Series A/B Bonds together with other available funds are expected to be applied on the date of issue of the Series A/B Bonds in the estimated amounts as follows (rounded to the nearest dollar):

Sources of Funds:

Principal Amount of Series A/B Bonds	\$	847,950,000
Net Original Issue Premium.....		97,616,733
Available Moneys Under General Resolution.....		<u>57,173,924</u>
 TOTAL.....	 \$	 <u>1,002,740,657</u>

Use of Funds:

Deposit to Note Payment Fund to retire Commercial Paper Notes		\$196,805,714
Deposit to the Refunding Trust Fund.....		740,405,610
Deposit to the Debt Service Reserve Fund.....		57,173,924
Costs of Issuance (including Bond Insurance Premium).....		3,756,674
Underwriters' Discount.....		4,598,735
 TOTAL.....	 \$	 <u>1,002,740,657</u>

PLAN OF REFUNDING

A portion of the proceeds from the sale of the Series B Bonds, together with certain amounts available under the General Resolution, will be deposited into the Refunding Trust Fund established under a Refunding Trust Agreement (the "Refunding Trust Agreement") to be entered into between the Authority and U.S. Bank National Association, as trustee for the Refunded Bonds listed in Appendix E hereto (the "Refunded Bonds"). Such amounts will be invested in United States Treasury Securities – State and Local Government Series (the "Escrow Securities") maturing in the amounts and at such times so as to provide for the payment of the redemption price of and interest on the Refunded Bonds on their stated maturity dates or on the first available optional redemption dates, as indicated in such Appendix E, and at the redemption prices also set forth in Appendix E. Any refunding is contingent upon delivery of the Series B Bonds.

SECURITY FOR THE SERIES A/B BONDS

GENERAL

The following summary of the security for the Series A/B Bonds is qualified in its entirety and reference is hereby made to Appendix C hereto and to the General Resolution, which set forth in further detail provisions relating to the security for the Series A/B Bonds. For definitions of certain capitalized terms used but not defined herein, see "Summary of Certain Provisions of the General Resolution" in Appendix C.

The Series A/B Bonds constitute valid and binding general obligations of the Authority and the full faith and credit of the Authority is pledged to the payment of the principal and redemption price of and interest on the Series A/B Bonds. The Authority is subject to suit, but its property is not generally subject to attachment or levy by execution to satisfy a judgment on the Series A/B Bonds. The Authority has no taxing power.

Neither the Commonwealth nor any political subdivision thereof shall be obligated to pay the principal of, or premium or interest on any Series A/B Bond and neither the faith and credit nor taxing power of the Commonwealth or of any political subdivision thereof is pledged to such payment.

The Authority may issue additional Bonds on a parity with the Bonds issued to date and the Series A/B Bonds (collectively, "Bonds") upon the satisfaction of certain conditions. See "Additional Indebtedness" below and "Summary of Certain Provisions of the General Resolution – Additional Indebtedness," "- Conditions Precedent to Delivery of a Series of Bonds" and "- Conditions Precedent to Delivery of a Series of Parity or Senior Secured Bonds" in Appendix C. All Bonds are equally and ratably secured under the provisions of the General Resolution and by the Funds and Accounts established thereunder, including, without limitation, the Debt Service Reserve Fund. See "Debt Service Reserve Fund" below.

The General Resolution also permits the issuance of Subordinated Bonds which are referred to herein, together with the Bonds, as "Secured Bonds." The Authority expects to issue additional Secured Bonds, the majority of which are expected to constitute Bonds, to finance its CIP. The Act limits the total amount of the Authority's unrefunded bonds and notes which may be Outstanding at any time. See "Financial Operations – Debt Limitation." For a table showing the debt service on Outstanding Secured Bonds, see "Financial Operations – Outstanding and Proposed Indebtedness."

The Authority has approved proposed modifications to the General Resolution which, if and when consented to by the requisite numbers of bondholders and certain third parties, would materially change a number of the provisions of the General Resolution discussed below. These modifications are expected to become effective at a time when the Series A/B Bonds will still be Outstanding. At the time of issuance of the Series A/B Bonds, the Underwriters, as the initial purchasers of all of the Series A/B Bonds, will consent to all of the proposed modifications on behalf of themselves and all subsequent holders of the Series A/B Bonds. The proposed modifications will not become effective with respect to any Bonds of the Authority, whether or not consent to the proposed modifications has been granted with respect to such Bonds, until the requisite numbers of bondholders and certain third parties have consented to such proposed modifications, as further described below. See "Proposed Modifications to the General Resolution" below and "Summary of Certain Provisions of the General Resolution" in Appendix C.

NET REVENUE PLEDGE

In the General Resolution, the Authority pledges as security for Bonds (i) its Revenues, (ii) all moneys or securities held in any Fund or Account established under the General Resolution (except the Operating Fund, the Note Payment Fund, the Rebate Fund and any Subordinated Debt Service Reserve Fund) together with all investment earnings thereon (except to the extent such earnings are required to be deposited into the Rebate Fund), and (iii) all other moneys and securities to be received by the Authority or by any Fiduciary pursuant to the General Resolution. This pledge is subject to the provisions of the General Resolution regarding the application of Revenues and the other moneys pledged as security for Secured Bonds. For the definition of Revenues see "Summary of Certain Provisions of the General Resolution" in Appendix C.

The General Resolution provides that the Authority shall promptly cause all Revenues received to be deposited in the Revenue Fund held by the Trustee and that prior to application to the Debt Service Fund, the Subordinated Debt Service Fund and the other Funds and Accounts established under the General Resolution, the Revenues on deposit in the Revenue Fund are to be applied to the Authority's expenses of maintaining, repairing and operating the Systems and engaging in other activities authorized by the Act.

The General Resolution provides that the funds on deposit in the Revenue Fund be transferred by the Trustee on the last Business Day of each month to the following funds and accounts in the following order:

First, to the Operating Fund, an amount necessary to make the amount on deposit therein equal to the Operating Expenses for the next succeeding three months as shown in the Operating Budget of the Authority on file with the Trustee.

Second, to the Debt Service Fund, the amounts necessary on a pro rata basis (i) to make up any deficiency in any Subaccount resulting from an increase in the applicable interest rate on any Variable Rate Bonds over the rate assumed in calculating the amount required for a prior deposit pursuant to the General Resolution, (ii) to increase the amount on deposit in each Subaccount of the Interest Account to equal interest included in Adjusted Debt Service next coming due on Outstanding

Bonds of the applicable Series accrued and unpaid and to accrue to and including the last day of the next succeeding month after taking into account any available moneys in the corresponding Subaccount of the Capitalized Interest Account, (iii) to increase the amount on deposit in each Subaccount of the Principal Account to equal that portion of the Principal Installment included in Adjusted Debt Service next coming due (within twelve months) on Outstanding Bonds of the applicable Series accrued and unpaid and to accrue to and including the last day of the next succeeding month, and (iv) to increase the amount on deposit in each Subaccount of the Redemption Account to equal the Redemption Price of Outstanding Bonds of the applicable Series then called for redemption (other than Sinking Fund Installments) as of any date on or prior to the last day of the next succeeding month.

Third, to the Subordinated Debt Service Fund, the amounts with respect to Subordinated Bonds determined in the same manner as the amounts in the Debt Service Fund set forth in the preceding paragraph with respect to Bonds; provided, that there are also deposited to the Subordinated Debt Service Fund any amounts necessary to increase each Subaccount of the Interest Account providing for the Authority's obligations to counterparties under interest rate swap agreements or other hedge agreements relating to Series of Subordinated Bonds designated by the Authority to equal the amount of such obligations next coming due with respect to such Series accrued and unpaid and to accrue to and including the last day of the next succeeding month.

Fourth, to the Debt Service Reserve Fund, (i) one-twelfth of the amount necessary to increase the amount on deposit in each Series Subaccount of the Common Account to equal the applicable Series Debt Service Reserve Fund Requirement, and (ii) the deposit required by any Supplemental Resolution to any Special Account.

Fifth, to the Subordinated Debt Service Reserve Fund, (i) an amount necessary to increase the amount on deposit in each Series Subaccount of the Common Account to equal the level required by any Supplemental Resolution, and (ii) the deposit required by any Supplemental Resolution to any Special Account.

Sixth, to each Series Subaccount of the General Account of the Community Obligation and Revenue Enhancement Fund, one-twelfth of the difference between the Supplemental Bond Coverage Requirement with respect to such Series of Bonds and the amount on deposit in such Subaccount on the first day of the Fiscal Year.

Seventh, to the Commonwealth Obligation Fund, an amount equal to the amount of Commonwealth Obligations payable during the next succeeding month.

Eighth, to the Rebate Fund, the amount of the Rebate Fund Requirement, if any, determined in accordance with the applicable Supplemental Resolution.

Each fund and account must be funded from Revenues to the amount required under the General Resolution before Revenues are transferred to funds and accounts lower in the flow of funds.

On each December 31 and June 30 or, if such day is not a Business Day, on the next preceding Business Day, the Trustee is required under the General Resolution to transfer funds in the Revenue Fund to the Operating Reserve Fund, the Insurance Reserve Fund, the Renewal and Replacement Reserve Fund and the Water Pollution Abatement Fund in the amounts specified in the General Resolution, then to the Revolving Fund, as directed by the Authority, and the remainder to the General Fund except to the extent that the Authority directs that the remainder be retained in the Revenue Fund.

See "Summary of Certain Provisions of the General Resolution – Flow of Funds from the Revenue Fund" in Appendix C for a more detailed explanation of the flow of funds.

The proposed modifications of the General Resolution would modify the flow of funds described above by (1) in paragraph *Second*, adding to the deposits to the Debt Service Fund designated amounts for obligations owing under interest rate swap agreements or other hedge agreements relating to Series of Bonds designated by the Authority, in a manner similar to that already provided with respect to such agreements relating to Subordinated Bonds and described in paragraph *Third*, (2) changing paragraph *Fourth* to require deposits to the Common Account in the Debt Service Reserve Fund equal to one-twelfth (1/12) the amount necessary to increase the amount on deposit in such Account, determined as of the first day of the current Fiscal Year, to the Debt Service Reserve Fund Requirement (a new term representing an aggregate debt reserve requirement for Bonds, which would replace the existing per-Series requirement and would reduce the total of debt service reserves required with respect to the Authority's Bonds); provided that no such deposit would be required in a Fiscal Year following the funding of the Common Account in connection with the issuance of a Series of Bonds, and (3) deleting paragraph *Sixth*, because the Community Obligation and Revenue Enhancement Fund would be terminated. See "Debt Service Reserve Fund," "Community Obligation and Revenue Enhancement Fund" and "Proposed Modifications to the General Resolution" below and "Summary of Certain Provisions of the General Resolution" in Appendix C.

COVERAGE COVENANTS

Under the Act and the General Resolution, the Authority is required to meet the following three covenants with respect to Rates and Charges (collectively, the "Coverage Covenants").

Rate Covenant. Pursuant to the General Resolution, and as required by the Act, the Authority covenants that for each fiscal year it will maintain Revenues sufficient to pay Current Expenses, debt service on Indebtedness, required deposits to reserves, costs of maintenance, replacement or improvement of the Systems to be funded as Current Expenses, and all amounts which the Authority may be obligated to pay by any law or contract (the "Rate Covenant").

Combined Debt Service Coverage Ratio Covenant. In addition to the Rate Covenant, the Authority is required under the General Resolution to fix and adjust Rates and Charges sufficient to provide Revenues Available for Bond Debt Service in each fiscal year at least equal to (a) debt service for such fiscal year on all Outstanding Bonds times the Primary Bond Coverage Ratio of 1.2 (the "Primary Bond Coverage Requirement") plus (b) the amount necessary to fund the Community Obligation and Revenue Enhancement Fund so that the balance thereof equals debt service for such fiscal year on Bonds Outstanding as of the beginning of such fiscal year times the Supplemental Bond Coverage Ratio of 0.1 (the "Supplemental Bond Coverage Requirement"). This requirement to fix Rates and Charges is referred to herein as the "Combined Debt Service Coverage Ratio Covenant." Pursuant to modifications of the Act and the General Resolution made in 1996, for purposes of calculating compliance with the Combined Debt Service Coverage Requirement for any fiscal year the Authority may treat state debt service assistance received by it either as Revenues or as a deduction from debt service requirements. The Authority has elected the latter alternative.

The Primary Bond Coverage Ratio and the Supplemental Bond Coverage Ratio may be adjusted by the Authority provided that such adjustment will not adversely affect the then current ratings, if any, assigned to any series of Secured Bonds by each Rating Agency. In any event, the Primary Bond Coverage Ratio shall not be less than 1.1, and no such adjustment shall cause the sum of the Primary Bond Coverage Ratio and the Supplemental Bond Coverage Ratio to be less than 1.2.

The proposed modifications to the General Resolution would terminate the Community Obligation and Revenue Enhancement Fund and would remove the Supplemental Bond Coverage Requirement component of the Combined Debt Service Ratio Covenant. The effect would be to reduce the requirement of this covenant to the amount described in clause (a) of the first paragraph under this subheading. The Authority would remain obligated to observe the Primary Bond Coverage Requirement, and the Primary Bond Coverage Ratio would remain subject to adjustment by the Authority as described above. See "Community Obligation and Revenue Enhancement Fund" and "Proposed Modifications to the General Resolution" below and "Summary of Certain Provisions of the General Resolution" in Appendix C.

Subordinated Combined Debt Service Coverage Ratio Covenant. In addition, under supplemental resolutions authorizing the issuance of Subordinated Bonds, including Subordinated Bonds issued to the Massachusetts Water Pollution Abatement Trust (the "SRF"), the Authority is required to fix and adjust Rates and Charges sufficient to provide Revenues Available for Bond Debt Service in each fiscal year at least equal to (a) 1.1 times debt service on the

Subordinated Bonds and all Outstanding Secured Bonds issued on a parity with or senior to the Subordinated Bonds (the “Subordinated Primary Bond Coverage Requirement”) plus (b) the amount necessary to fund the Community Obligation and Revenue Enhancement Fund to the Supplemental Bond Coverage Requirement (the “Subordinated Combined Debt Service Coverage Ratio Covenant”). For purposes of budgeting debt service deposits, calculating the Subordinated Combined Debt Service Coverage Ratio Covenant, and satisfying tests for the issuance of Additional Secured Bonds, the debt service requirements on the Subordinated Bonds issued to the SRF (the “SRF Bonds”) are based on the net debt service requirements determined after application of loan subsidies to be provided by the program and earnings on certain moneys.

The proposed modifications to the General Resolution would relocate the Subordinated Primary Bond Coverage Requirement from the applicable supplemental resolutions to the General Resolution and would remove the Supplemental Bond Coverage Requirement component of the Subordinated Combined Coverage Ratio Covenant. The effect would be to reduce the requirement of this covenant to the amount described in clause (a) of the preceding paragraph. See “Community Obligation and Revenue Enhancement Fund” and “Proposed Modifications to the General Resolution” below and “Summary of Certain Provisions of the General Resolution” in Appendix C.

Covenant as to Establishment of Rates; Failure to Comply with Covenants. Under the General Resolution the Authority covenants to adopt its Rates and Charges strictly in accordance with the Act as in effect on the original effective date of the General Resolution, which establishment shall be conclusive and final and not subject to supervision or regulation by the Commonwealth or any of its political subdivisions, at a level sufficient to satisfy the Coverage Covenants.

If in any fiscal year the Authority shall not comply with the Coverage Covenants, then the Authority shall not be deemed to be in default under the General Resolution so long as it shall specify to the Trustee the corrective steps which it has taken to ensure compliance with the Coverage Covenants for the then current fiscal year; retain the Consulting Engineer or Rate Consultant to review the adequacy of the Authority’s charges with respect to the Systems and to recommend changes necessary for the Authority to be in compliance with the Coverage Covenants; and use its best efforts to effect such changes as recommended by the Consulting Engineer or Rate Consultant. See “Summary of Certain Provisions of the General Resolution – Covenants of the Authority – Covenant as to Rates and Charges: Debt Service Coverage Ratio” in Appendix C.

Operating Reserve Fund and Rate Stabilization Fund Transfers. The Authority may include moneys transferred from the Operating Reserve Fund and the Rate Stabilization Fund as Revenues Available for Bond Debt Service in meeting the Coverage Covenants, subject to certain limitations. See the definition of “Revenues Available for Bond Debt Service” in the “Summary of Certain Provisions of the General Resolution” in Appendix C.

DEBT SERVICE RESERVE FUND

The General Resolution establishes a Debt Service Reserve Fund to be funded in an amount which equals the Debt Service Reserve Fund Requirement. The Debt Service Reserve Fund Requirement is equal to the aggregate of the Series Debt Service Reserve Fund Requirements for all Outstanding Series of Bonds. The Series Debt Service Reserve Fund Requirement means, for any Series of Bonds, an amount equal to the least of (i) 100% of the Average Annual Adjusted Debt Service for such Series of Bonds, (ii) 10% of the original net proceeds of such Series of Bonds, (iii) 125% of the average annual Debt Service for such Series of Bonds, or (iv) the maximum amount of Debt Service due on such Series of Bonds in any succeeding Bond Year. The General Resolution requires, as a condition to the issuance of a Series of Bonds thereunder, that the Debt Service Reserve Fund be fully funded in an amount equal to the Debt Service Reserve Fund Requirement. After the issuance of the Series A/B Bonds, the amount on deposit in the Debt Service Reserve Fund will be approximately \$240.7 million. In addition, there is approximately \$34.7 million in the Subordinated Debt Service Reserve Fund which is available only for Subordinated Bonds. See “Summary of Certain Provisions of the General Resolution” in Appendix C.

Moneys in the Debt Service Reserve Fund are available for the payment of principal and premium of and interest on all Bonds, but not Subordinated Bonds, equally and ratably. See “Financial Operations – Outstanding and Proposed Indebtedness” for a table setting forth the debt service requirements on the Authority’s Outstanding Bonds and Subordinated Bonds immediately prior to the issuance of the Series A/B Bonds. In the event that moneys are withdrawn from the Debt Service Reserve Fund, such withdrawal shall be replenished as nearly as practicable in twelve equal

monthly installments commencing in the fiscal year following such withdrawal. See “Summary of Certain Provisions of the General Resolution – Flow of Funds from the Revenue Fund” in Appendix C.

The proposed modifications to the General Resolution would eliminate the Series Debt Service Reserve Fund Requirements and amend the Debt Service Reserve Fund Requirement to mean, as of the first day in each Fiscal Year or the date of issuance of a Series of Bonds, the amount equal to the least of (i) 50% of the maximum amount of Adjusted Debt Service due in any succeeding Fiscal Year on all Bonds Outstanding on such date, (ii) 10% of the original net proceeds of such Bonds, (iii) 125% of the average annual Debt Service on such Bonds, or (iv) the maximum amount of Debt Service due on such Bonds in any succeeding Fiscal Year. See “Proposed Modifications to the General Resolution” below and “Summary of Certain Provisions of the General Resolution” in Appendix C.

COMMUNITY OBLIGATION AND REVENUE ENHANCEMENT FUND

The General Resolution establishes a Community Obligation and Revenue Enhancement Fund as security for Secured Bonds. The General Resolution requires that the Community Obligation and Revenue Enhancement Fund be funded in monthly installments over a fiscal year with respect to each Series of Bonds (but not Subordinated Bonds) in an aggregate amount necessary to bring the balance therein up to the Supplemental Bond Coverage Requirement. The Supplemental Bond Coverage Requirement is subject to adjustment from time to time by the Authority. See “Coverage Covenants” above. Moneys in the Community Obligation and Revenue Enhancement Fund are available only for the payment of principal of, premium, if any, and interest on all Secured Bonds in the event of a Local Body Default (as such term is defined in Appendix C).

In the event that a Local Body fails to pay any Rates and Charges, the Authority has covenanted to exercise its statutory power to certify to the State Treasurer the amount of such unpaid Rates and Charges. The Act provides that upon such certification, the State Treasurer shall promptly intercept any amounts then payable by the Commonwealth to such Local Body and pay them to the Authority in satisfaction of such unpaid Rates and Charges. See “Rates and Charges – Enforcement.” Should a Local Body’s default continue, the Authority is required, by no later than twelve months from the date of such failure, to declare such failure a Local Body Default. Upon such declaration the Authority must send to each Local Body receiving services from the Authority a notice specifying the default and the amount thereof, and stating that, unless such default is cured, Rates and Charges to each Local Body will be increased so as to cover the default. There have been no Local Body Defaults, although the Authority made use of the local aid intercept (described above) on six occasions between 1990 and 1993.

The proposed modifications to the General Resolution would terminate the Community Obligation and Revenue Enhancement Fund. See “Proposed Modifications to the General Resolution” below and “Summary of Certain Provisions of the General Resolution” in Appendix C.

OTHER RESERVES

The General Resolution also establishes an Operating Reserve Fund, an Insurance Reserve Fund and a Renewal and Replacement Reserve Fund. The annual requirement for each such reserve is funded in two installments on each December 31 and June 30. Under certain circumstances, moneys on deposit in each of these reserves are available to pay debt service on Secured Bonds. Additionally, other reserves and funds established under the General Resolution are generally available, with certain exceptions, to pay debt service on Secured Bonds in the event Revenues are insufficient. See “Summary of Certain Provisions of the General Resolution – Debt Service Fund” and “- Subordinated Debt Service Fund” and “- Priority of Funds in the Event of Debt Service Fund Shortfall” and “- Priority of Funds in the Event of Subordinated Debt Service Fund Shortfall” in Appendix C.

Operating Reserve Fund. The Operating Reserve Fund is funded from Revenues in the amount of the Operating Reserve Fund Requirement which must be at least one-sixth (1/6th) of the annual Operating Expenses set forth in the Operating Budget. Moneys in the Operating Reserve Fund may be transferred to the Operating Fund for the payment of Operating Expenses upon delivery of a Certificate of an Authorized Representative of the Authority. See “Summary of Certain Provisions of the General Resolution – Operating Reserve Fund” in Appendix C.

Insurance Reserve Fund. The Insurance Reserve Fund is funded from Revenues in the amount of the Insurance Reserve Fund Requirement. Moneys in the Insurance Reserve Fund may be applied by the Authority in the same manner as insurance proceeds, as provided in the General Resolution. See “Summary of Certain Provisions of the General Resolution – Insurance Reserve Fund” in Appendix C.

Renewal and Replacement Reserve Fund. The Renewal and Replacement Reserve Fund is funded from Revenues in the amount of the Renewal and Replacement Reserve Fund Requirement. Moneys in the Renewal and Replacement Reserve Fund shall be applied to the Cost of any Capital Improvement which is not provided for by moneys available in the Construction Fund or the Operating Fund in accordance with the procedures set forth in the General Resolution. See “Summary of Certain Provisions of the General Resolution – Renewal and Replacement Reserve Fund” in Appendix C.

The adequacy of each of the Operating Reserve Fund Requirement, the Insurance Reserve Fund Requirement and the Renewal and Replacement Reserve Fund Requirement is reviewed annually by the Authority and every third fiscal year by the Consulting Engineer or, in the case of the Insurance Reserve Fund Requirement, an insurance consultant. The adequacy of the funding requirements for the Operating Reserve Fund and the Renewal and Replacement Reserve Fund have been confirmed by the Consulting Engineer in its most recent triennial report dated December 2005 with respect to the Systems, prepared and delivered in accordance with the General Resolution.

The proposed modifications to the General Resolution would amend language relating to insurance requirements to explicitly permit insurance carried by the Authority to be subject to deductibles customary among water or sewer utility systems similar to the Authority and would amend language relating to the Renewal and Replacement Reserve Fund Requirement to specify that the purpose of such Requirement is to fund emergency repairs and replacements and other expenditures for repairs and replacements not provided for in the Operating Budget and the Capital Budget. In addition, the Consulting Engineer would evaluate the Renewal and Replacement Fund Requirement at five-year intervals instead of three-year intervals. See “Proposed Modifications to the General Resolution” below and “Summary of Certain Provisions of the General Resolution” in Appendix C.

OUTSTANDING INDEBTEDNESS

As of December 31, 2006, the Authority had Outstanding \$3.0 billion of Bonds, \$917 million of SRF Bonds, and \$1.5 billion of Multi-Modal Subordinated General Revenue Bonds and Subordinated General Revenue Bonds (which, together with the SRF Bonds, constitute Subordinated Bonds), and \$218 million of tax-exempt commercial paper notes (the “CP Notes”) (which constitute Subordinated Parity Bond Anticipation Notes). The interest on the CP Notes, but not the principal thereof, is secured by a lien on a parity with other Subordinated Bonds. For a further description of such Outstanding Indebtedness and a table setting forth the debt service requirements on the Authority’s Outstanding Secured Bonds prior to the issuance of the Series A/B Bonds, see “Financial Operations – Outstanding and Proposed Indebtedness.”

ADDITIONAL INDEBTEDNESS

The General Resolution contains certain conditions precedent to the issuance of additional Bonds, including that the Authority shall have met its Combined Debt Service Coverage Ratio Covenant for the most recent period of 12 consecutive months for which data is available and that the Consulting Engineer shall certify that for the fiscal year of issuance and the fiscal year thereafter either (i) projected Revenues Available for Bond Debt Service will be sufficient to satisfy the Combined Debt Service Coverage Ratio Covenant (taking into account the Series of Bonds to be issued and any other Series of Bonds to be issued in such Fiscal Year), or (ii) projected Revenues Available for Bond Debt Service, including only increases in Rates and Charges then approved and including increases in Operating Expenses to the extent required by the General Resolution, will be sufficient to pay debt service on all Bonds (taking into account the Series of Bonds to be issued) and certain required reserve deposits, including required deposits to the Community Obligation and Revenue Enhancement Fund. The foregoing requirements need not be met for Bonds issued to refund other Bonds so long as debt service is not increased in any fiscal year and the latest maturity date of Secured Bonds is not extended. The General Resolution requires that upon the issuance of Bonds, for refunding purposes or otherwise, the Debt Service Reserve Fund be fully funded to its applicable requirement. The General Resolution provides certain conditions precedent to the issuance of Secured Bonds secured on a parity with or senior to the SRF Bonds which are similar to the conditions in connection with the issuance of additional Bonds. In addition, the General Resolution permits the

Authority to issue other Indebtedness including, but not limited to, revenue, grant and bond anticipation notes, Indebtedness secured by the General Fund and certain non-recourse Indebtedness. See “Summary of Certain Provisions of the General Resolution – Additional Indebtedness” and “- Conditions Precedent to Delivery of a Series of Bonds” and “- Conditions Precedent to Delivery of a Series of Parity or Senior Secured Bonds” in Appendix C.

The proposed modifications to the General Resolution would amend the additional Bonds test described in the preceding paragraph to take account of the termination of the Community Obligation and Revenue Enhancement Fund by substituting for the Combined Debt Service Coverage Ratio Covenant the Primary Bond Coverage Requirement and by deleting from the test described in clause (ii) of such paragraph the reference to deposits to the Community Obligation and Revenue Enhancement Fund. Corresponding modifications would be made to the additional debt test relating to the issuance of additional Subordinated Bonds. See “Proposed Modifications to the General Resolution” below and “Summary of Certain Provisions of the General Resolution” in Appendix C.

PROPOSED MODIFICATIONS TO THE GENERAL RESOLUTION

The General Resolution provides that it may be amended by the Authority subject to certain conditions. With certain exceptions, an amendment of the General Resolution requires the consent of the holders of at least two-thirds of the aggregate outstanding principal amount of the Series of Secured Bonds that would be affected by such amendment, measured at the time such amendment becomes effective. Principal exceptions include the following: (a) certain specified amendments may be made by the Authority acting alone or by the Authority with the consent of the Trustee, (b) no amendment of the General Resolution may permit a reduction of principal or Redemption Price of or a change in the terms of redemption, maturity of principal or resolution of principal or Redemption Price of any Secured Bond, a reduction of the interest rate on any Secured Bond or a change in the terms of redemption or maturity of principal of any installment of interest on any Secured Bond, in each case without the consent of the holder of such Secured Bond, (c) no amendment of the General Resolution may reduce the percentages or otherwise affect the classes of Secured Bonds required to consent to modifications to the General Resolution without the consent of the holders of all the Secured Bonds and (d) no amendment of the General Resolution may change or modify any of the rights or obligations of the Trustee unless the Trustee assents thereto. For a more complete description of the amendment provisions of the General Resolution, see “Summary of Certain Provisions of the General Resolution — Supplemental Resolutions” and “— Amendments” in Appendix C. In addition, certain modifications to the General Resolution may also be subject to consent by other financial institutions, such as credit enhancers and liquidity providers, pursuant to the terms of contracts between such financial institutions and the Authority.

In the resolution authorizing the Series A/B Bonds, the Authority approved proposed modifications to the General Resolution. The principal effects of these modifications would include the following:

Reserve Requirements and Reserve Funds

- The Debt Service Reserve Fund Requirement for Bonds would be changed from a per-Series basis to an aggregate basis, and one of the standards of the test would be changed from 100% of Average Annual Adjusted Debt Service to 50% of Maximum Annual Adjusted Debt Service. See “Debt Service Reserve Fund” above.
- Investments permitted in the Debt Service Fund, Subordinated Debt Service Fund, Debt Service Reserve Fund and Subordinated Debt Service Reserve Fund would be expanded to include more permitted investments, including securities repurchase agreements (“repos”), and investments in the Debt Service Reserve Fund and the Subordinated Debt Service Reserve Fund would no longer be limited to 15 years. Amounts released from the Debt Service Reserve Fund or the Subordinated Debt Service Reserve Fund on account of the reduction in a debt service reserve requirement or the use of a financial guaranty in place of funding would be used to redeem Bonds or Subordinated Bonds, as applicable.
- The purpose of the Renewal and Replacement Reserve Fund would be redefined more narrowly as a fund for emergency needs, and other expenditures for repairs and replacements not provided for in the Operating Budget and the Capital Budget. In addition, any portion of the new Renewal and Replacement Reserve

Fund Requirement in excess of \$10 million may be covered by a line of credit (such as the Authority's current commercial paper programs) rather than having to be funded with cash and investments.

- The Supplemental Coverage Ratio Requirement and the Community Obligation and Revenue Enhancement Fund would be eliminated.

Rate Covenants and Additional Debt Tests

- The requirement that Rates and Charges cover deposits to the Community Obligation and Revenue Enhancement Fund would be eliminated.
- The calculation of debt service requirements for Bonds would take into account certain interest rate swap arrangements (as already provided in the General Resolution with respect to Subordinated Bonds).

Amendments

- The general bondholder consent requirement would be reduced from the holders of two-thirds of the outstanding principal amount of each Series of Secured Bonds affected by a proposed amendment to the holders of 51% of each such amount.
- Bond insurers and other providers of credit enhancement would be authorized to vote on amendments in place of the holders of the Secured Bonds which they insure or secure (excluding amendments that would require a unanimous consent or the consent of every holder of affected Secured Bonds).

Other

- The provision permitting removal of the Trustee at the option of the Authority would operate at two-year intervals instead of five-year intervals.
- Refunding and defeasance escrows would be permitted to be funded not only with obligations issued or guaranteed by the United States and pre-refunded municipal bonds, but also with obligations of the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation and other agencies established by the federal government.

For further details of the proposed modifications, see "Summary of Certain Provisions of the General Resolution" in Appendix C.

Most of the proposed amendments will require the consents of the holders of two-thirds of the Outstanding Secured Bonds of the Authority, but this general rule is subject to several exceptions. Amendments that affect the holders of Bonds but not the holders of Subordinated Bonds, such as the proposed modification of the Combined Debt Service Coverage Ratio Requirement with respect to Bonds, will not require the consent of any holders of Subordinated Bonds. Similarly, amendments which affect the holders of Subordinated Bonds but not the holders of Bonds, such as the proposed modifications of the tests permitting the issuance of additional Subordinated Bonds, will not require the consent of any holders of Bonds. In certain cases, issuers of municipal bond insurance policies may vote on amendments in place of the holders of the Subordinated Bonds insured by such policies. One amendment, that is, the reduction of the general bondholder consent requirement for future amendments of the General Resolution from holders of two-thirds of the Secured Bonds in applicable Series to the holders of 51% of the Secured Bonds in applicable Series, will require the consent of the holders of 100% of the Secured Bonds Outstanding at the time such amendment becomes effective.

In addition, third parties, including, for example, providers of credit enhancement and liquidity enhancement for Series of Subordinated Bonds of the Authority, pursuant to the terms of separate contracts between such providers and the Authority, are entitled to consent to certain of the proposed modifications to the General Resolution or have the benefit of contractual provisions which mirror provisions of the General Resolution that the Authority is seeking to modify. In either case, the Authority will have to obtain the consents of such providers (or its contracts with such

providers will have to expire or be terminated) before the Authority can effect or realize the benefits of certain of the proposed modifications to the General Resolution.

At the time of issuance of the Series A/B Bonds, the Underwriters, as the initial purchasers of all of the Series A/B Bonds, will consent to all of the proposed modifications on behalf of themselves and all subsequent holders of the Series A/B Bonds. Each of the proposed modifications will apply to the Series A/B Bonds only when and if such proposed modification becomes effective upon the consent of the requisite number of holders as described above. The Authority intends to request the initial purchasers of future Series of its Secured Bonds to consent to the proposed modifications at the time of original issue of each Series. As new issues of Secured Bonds are sold and as existing issues are retired, the Authority expects eventually to achieve the two-thirds consent of holders of Secured Bonds required to approve most of the proposed modifications. The Authority cannot be certain when this process will be completed. It expects it to take several years with respect to the Authority's Bonds. With respect to its Subordinated Bonds, this process will be supplemented by efforts to obtain consents from the Massachusetts Water Pollution Abatement Trust, which holds approximately 28% of the aggregate principal amount of Subordinated Bonds currently Outstanding, and from financial institutions which have insured Subordinated Bonds and are entitled to approve certain amendments of the General Resolution in place of the holders of such Subordinated Bonds. With this assistance, it may be possible to complete the bondholder approval process for amendments that affect only the Subordinated Bonds in a shorter period of time.

The Authority has not yet requested consents to the proposed modifications from the Massachusetts Water Pollution Abatement Trust or from any of the third parties which have consent rights. The Authority intends to initiate such requests on a timely basis following the issuance of the Series A/B Bonds.

By their acceptance of the Series A/B Bonds, the owners thereof (i) agree to all the terms of the General Resolution as currently in effect and all proposed modifications approved by the Authority in connection with the issuance of the Series A/B Bonds, (ii) waive the applicability of the provisions of the General Resolution affected by such modifications and (iii) agree to any amendments to the General Resolution which may be necessary, in the opinion of Bond Counsel, to effect such modifications.

THE AUTHORITY AND ITS SERVICE AREAS

PURPOSES AND POWERS

The Authority was created by the Act, effective January 1, 1985. Pursuant to the Act, the Authority has several main objectives: to construct and maintain sewage treatment facilities which ensure that the Sewer System's wastewater discharges meet federal and state pollution control requirements; to maintain, operate and improve an adequate water supply distribution system and provide water in conformance with all applicable state and federal regulations; to establish programs for leak detection and reduction of infiltration and inflow within its service areas; to repair, replace, rehabilitate and extend the Systems and to finance the capital and operating expenses arising from their operations on a self-sustaining basis; to provide professional management and Systems-wide planning; and to establish and administer charges on a basis which will foster the conservation of water and improve the quality of the environment.

Ownership, possession and control of all personal property constituting the MDC water and sewer systems were transferred to the Authority effective July 1, 1985. Real property formerly included in the MDC water and sewer systems, including all watersheds, reservoirs and other water rights, was retained by the Commonwealth, to be managed by the MDC Watershed Management Division. As of July 2003, the MDC became part of the DCR and the DCR's Division of Water Supply Protection is charged with the duties and responsibilities formerly performed by the MDC Watershed Management Division. The Authority is granted by the Act an exclusive right to utilize such quantities of water as may be safely yielded from the DCR Division of Water Supply Protection's watersheds, reservoirs and other water rights (the "DCR Watershed System") which are necessary to provide the Authority's water supply. The DCR Division of Water Supply Protection is responsible for the acquisition, construction and maintenance of the DCR Watershed System. See "The Systems." The Authority is obligated to pay the Commonwealth for the costs of the DCR Division of Water Supply Protection relating to watershed management.

The Authority is empowered by the Act to exercise the following powers in furtherance of its objectives: issue revenue bonds and notes (subject to the debt limitation contained in the Act) (see "Financial Operations – Debt

Limitation”); hire personnel and engage consultants and other experts; adopt budgets for its operations and capital improvement programs and establish, after it has held public hearings, rates and charges for its services; expand the service areas of the Waterworks System and the Sewer System subject to certain approvals and other conditions (see “The Systems”); acquire property by purchase, lease or, under certain limitations, eminent domain (other than water and water rights) and lease, sell, transfer or otherwise encumber its property (subject to legal restraints on the disposition of certain public property); and establish rates and charges for its services and commodities without supervision by other agencies of the Commonwealth or any other governmental body and enforce the collection thereof (see “Rates and Charges”).

The Act provides that the Authority’s existence shall continue until terminated by law, provided that no such law shall take effect so long as any bonds or notes of the Authority are outstanding unless adequate provision has been made for the payment or satisfaction of such obligations.

SERVICE AREAS AND MAP

The Authority currently provides wholesale water and sewer services in service areas encompassing, in whole or in part, 61 communities located primarily in eastern Massachusetts, including most of the cities and towns in the metropolitan Boston area. Approximately 2.6 million people, or approximately 42% of the total population of the Commonwealth, live in the Authority’s service areas. Under certain circumstances, the Authority’s service areas may be expanded to include additional communities. See “The Systems.”

The map on the following page shows the Authority’s current service areas for water and sewer services.

Map of the Authority's Service Areas

CHARGES TO LOCAL BODIES

Forty-nine Local Bodies are authorized to be served by the Waterworks System and 43 Local Bodies are authorized to be served by the Sewer System.

More than 80% of the Authority’s revenues historically have been derived from the rates and charges paid by the Local Bodies for the Authority’s wholesale water and sewer services. The Local Bodies in turn fund payment of the Authority’s rates and charges from a variety of local sources. The obligation to pay the Authority’s rates and charges is a general obligation of each Local Body, supported by its full faith and credit and payable from all revenue sources. See “Local Bodies.”

For water supply, 32 of the 49 Local Bodies named in the Act derive their entire municipal water supply from the Waterworks System. Eleven receive a portion of their water supply from the Waterworks System. Three – Dedham-Westwood Water District, Leominster and Worcester – historically have received virtually no water from the Authority (although Worcester did receive limited water from the Authority as a result of extremely dry weather in the summer of 1999 as did the Dedham-Westwood Water District during 2002, 2003, 2004 and 2006). In June 2002, the Board approved the application of the Town of Stoughton to become a member of the Waterworks System and began supplying water to the town in the first quarter of Fiscal Year 2004. In November 2005, the Board approved the application of the Town of Reading to become a member of the Waterworks System and the Town was authorized to start drawing water in May 2006. In December 2005, the Board approved the application of the Dedham-Westwood Water District to become a member of the Waterworks System. The allocation among Local Bodies of the Authority’s water charges for each fiscal year generally is based upon water consumption in the preceding calendar year. See “Rates and Charges – General.”

For the Sewer System, all 43 Local Bodies named in the Act currently receive service from the Authority. The Authority’s sewer charges are allocated on a proportional basis utilizing, among other factors, total metered flow, contributing population and census population. See “Rates and Charges – General.”

Five Local Bodies, of which the BWSC is the largest, are budgeted to account for approximately 47.4% of the aggregate rates and charges assessed in Fiscal Year 2007 as follows:

	<u>Percent of Total FY 2007 Authority Water Charges</u>	<u>Percent of Total FY 2007 Authority Sewer Charges</u>	<u>Percent of Total FY 2007 Authority Charges</u>
Boston Water & Sewer Commission	38.4%	28.3%	31.7%
City of Newton	4.7	4.6	4.6
City of Quincy	4.9	4.3	4.5
City of Cambridge	0.0	5.1	3.4
City of Waltham	<u>3.9</u>	<u>3.0</u>	<u>3.3</u>
Total	51.9%	45.2%	47.4%

The following table sets forth the Fiscal Year 2007 charges assessed by the Authority to each Local Body, except charges to certain Local Bodies and certain governmental users with special arrangements with the Authority. See Footnote 1 to the following table and “Local Bodies – Special Arrangements.”

FISCAL YEAR 2007 SYSTEMS CHARGES BY LOCAL BODY

<u>Local Body</u>	<u>Service Provided</u>		<u>Systems Charges</u>			<u>Percent of Total FY 2007 Charges</u>
	<u>Water</u>	<u>Sewer</u>	<u>Water</u>	<u>Sewer</u>	<u>Combined</u>	
Arlington	x	x	\$ 3,527,387	\$ 6,143,299	\$ 9,670,686	2.0%
Ashland		x	0	1,618,656	1,618,656	0.3
Bedford		x	0	2,565,613	2,565,613	0.5
Belmont	x	x	1,821,894	3,705,621	5,527,515	1.1
Boston Water and Sewer Commission ²	x	x	62,704,517	94,101,848	156,806,365	31.7
Braintree		x	0	6,234,886	6,234,886	1.3
Brookline	x	x	4,692,491	9,606,833	14,299,324	2.9
Burlington		x	0	3,650,224	3,650,224	0.7
Cambridge		x	0	16,822,068	16,822,068	3.4
Canton	x	x	1,622,912	3,073,080	4,695,992	0.9
Chelsea	x	x	2,657,451	4,439,053	7,096,504	1.4
Dedham		x	0	4,681,204	4,681,204	0.9
Dedham-Westwood Water District ³	x		0	0	0	0.0
Everett	x	x	3,668,354	5,815,528	9,483,882	1.9
Framingham	x	x	6,108,149	8,427,956	14,536,105	2.9
Hingham Sewer District		x	0	1,263,977	1,263,977	0.3
Holbrook		x	0	1,164,235	1,164,235	0.2
Lexington	x	x	4,032,517	5,633,833	9,666,350	2.0
Lynn Water and Sewer Commission ⁴	x		194,583	0	194,583	0.0
Lynnfield Water District ⁵	x		364,527	0	364,527	0.1
Malden	x	x	4,933,009	8,710,731	13,643,739	2.8
Marblehead	x		1,631,484	0	1,631,484	0.3
Marlborough	x		2,386,661	0	2,386,661	0.5
Medford	x	x	4,382,521	8,648,229	13,030,749	2.6
Melrose	x	x	2,017,068	4,515,809	6,532,877	1.3
Milton	x	x	2,263,683	4,154,293	6,417,976	1.3
Nahant	x		313,556	0	313,556	0.1
Natick		x	0	4,006,468	4,006,468	0.8
Needham	x	x	804,108	4,878,286	5,682,394	1.1
Newton	x	x	7,606,834	15,154,186	22,761,020	4.6
Northborough	x		762,171	0	762,171	0.2
Norwood	x	x	2,580,986	5,303,808	7,884,794	1.6
Peabody	x		928,069	0	928,069	0.2
Quincy	x	x	8,052,624	14,186,030	22,238,655	4.5
Randolph		x	0	4,268,513	4,268,513	0.9
Reading ⁶	x	x	0	3,171,403	3,171,403	0.6
Revere	x	x	3,497,276	6,922,399	10,419,675	2.1
Saugus	x		2,590,216	0	2,590,216	0.5
Somerville	x	x	5,179,472	10,830,035	16,009,508	3.2
Southborough	x		689,683	0	689,683	0.1
Stoneham	x	x	2,517,547	3,386,652	5,904,199	1.2
Stoughton	x	x	400,150	3,521,058	3,921,208	0.8
Swampscott	x		1,633,133	0	1,633,133	0.3
Wakefield	x	x	1,534,817	4,358,332	5,893,149	1.2
Walpole		x	0	2,586,581	2,586,581	0.5
Waltham	x	x	6,287,763	9,867,845	16,155,607	3.3
Watertown	x	x	2,448,358	4,412,383	6,860,741	1.4
Wellesley	x	x	678,369	4,341,937	5,020,306	1.0
Weston	x		1,377,593	0	1,377,593	0.3
Westwood		x	0	1,973,685	1,973,685	0.4
Weymouth		x	0	8,556,370	8,556,370	1.7
Wilmington		x	0	1,770,873	1,770,873	0.4
Winchester	x	x	890,279	3,071,919	3,962,198	0.8
Winthrop	x	x	1,249,283	2,261,781	3,511,064	0.7
Woburn	x	x	2,093,459	8,426,290	10,519,749	2.1
Total			<u>\$163,124,954</u>	<u>\$332,233,810</u>	<u>\$495,358,764</u>	<u>100.0%</u>

- ¹ This chart excludes six communities, the revenues received from which are accounted for by the Authority as other charges for services, rather than as rates and charges. These excluded communities include four of the 19 communities which receive water pursuant to contracts: Chicopee, South Hadley (served by South Hadley Fire District No. 1), Wilbraham and Worcester. Worcester currently only receives water services on an emergency basis and has not received water since the drought that occurred in the summer of 1999. The fifth excluded community is Clinton, which receives its first 800 million gallons of water per year at no charge pursuant to special act, and typically consumes less than 800 million gallons annually, but would be charged generally applicable rates for any amounts in excess thereof. Clinton also receives wastewater services provided by the Clinton Wastewater Treatment Plant and charges for this service are excluded from this chart. The sixth excluded community, Lancaster (served by the Lancaster Sewer District), receives wastewater services provided by the Clinton Wastewater Treatment Plant. The six excluded communities are budgeted to account for approximately \$4.3 million in Authority revenues for Fiscal Year 2007. The chart also excludes Leominster which, although named in the Act to be served by the Authority's Waterworks System, has taken no water from the Authority since January 1991.
- ² The Authority's services for the City of Boston are provided through and assessed to the BWSC. The BWSC is a body politic and corporate and independent political subdivision of the Commonwealth. The City of Boston is not liable for the rates and charges imposed on the BWSC by the Authority.
- ³ The Dedham-Westwood Water District did not use Authority water during 2005. Therefore, it did not incur an assessment for Fiscal Year 2007. The Towns of Dedham and Westwood are not liable for the rates and charges imposed on the Dedham-Westwood Water District by the Authority.
- ⁴ The Authority's services to a single large industrial user in Lynn are provided through and assessed to the Lynn Water and Sewer Commission (the "LWSC"). The LWSC provides service to the rest of Lynn from its own resources without obtaining service from the Authority. The LWSC is a body politic and corporate and independent political subdivision of the Commonwealth. Neither the City of Lynn nor the retail industrial user is liable for the rates and charges imposed on the LWSC by the Authority.
- ⁵ The Authority provides water services to approximately 45% of the population of Lynnfield through the Lynnfield Water District, a body corporate of the Commonwealth. The Town of Lynnfield is not liable for the rates and charges imposed on the Lynnfield Water District by the Authority.
- ⁶ Effective August 1, 2006, the Town of Reading is a fully-served water community of the Authority. The Town of Reading's Fiscal Year 2007 water charge will be based on applying the wholesale rate to actual water consumption.

Subject to applicable federal and state regulations and certain regulatory powers of the Authority, Local Bodies continue to exercise control over their respective retail water distribution and wastewater collection systems. Except in an emergency, written notice of any proposed local rules and regulations regarding use of the retail systems must be furnished to the Authority prior to adoption. Regulatory powers for monitoring and regulating Local Bodies conferred by the Act upon the Authority relate to matters such as water conservation and development of local water supply sources, implementation of federal and state toxic waste and pretreatment laws, reduction of infiltration and inflow of ground and surface waters into the Sewer System, and installation of water meters. See "The Systems."

Local Bodies currently served by the Authority could by state legislative action or with the Authority's approval seek to develop alternative water or wastewater delivery systems, although such systems would need to comply with all applicable federal and state environmental standards. The Authority and its Consulting Engineer believe that such alternatives are likely to be prohibitive in cost for most of the Local Bodies and, particularly in the case of alternative sewage treatment facilities, would take many years to implement.

RATES AND CHARGES

GENERAL

For Fiscal Year 2007, approximately 90% of the Authority's budgeted revenues are expected to be derived from wholesale rates and charges assessed to the Local Bodies. The remaining revenues are expected to be derived primarily from investment income and miscellaneous income, including assessments to certain Local Bodies not included as rates and charges. The Act requires that the Authority set its rates and charges at levels sufficient to pay, among other things, its current expenses and its debt service, and to provide the debt service coverage required by the General Resolution. See "Security for the Series A/B Bonds – Coverage Covenants." In addition to this revenue, the Authority expects to receive \$18.75 million in financial assistance from the Commonwealth ("state debt service assistance") in Fiscal Year 2007 that the Authority will account for as an offset to debt service deposits. See "Historical Rates and Charges," "Legislative and Other Developments" and Appendix B – "Supplemental Engineering and Financial Feasibility Report." There can be no assurance that the Authority will actually receive this amount.

In accordance with the Act, the Authority's rate setting is exercised independently by its Board of Directors without being subject to the approval of any department, agency or other instrumentality of the Commonwealth or any other governmental body. The Authority's rates and charges are adopted annually in June after notice and public hearing, and the review and receipt of non-binding recommendations by the Authority's Advisory Board. The level of the Authority's rates and charges assessed to Local Bodies is not subject to the limitations set forth in Proposition 2½. For a discussion of the effect of Proposition 2½ on the ability of Municipal Local Bodies to raise revenues to pay assessed rates and charges through property tax levies, see "Local Bodies – Municipal Sources of Revenue."

The Authority's charges for services are billed directly to Local Bodies on a wholesale basis. The Authority currently certifies annual charges to each Local Body on or about July 1 of each year. To assist Local Bodies with their respective annual budget or rate-setting processes, the Authority furnishes them with preliminary estimates of their respective rates and charges for the following fiscal year in February of each year. Authority charges are payable in ten equal installments due on or before the first business day of each month, excluding January and July, of each fiscal year. There is an interest charge of 1% per month for late payments.

As required by the Act, the Authority establishes charges of general application separately for the services provided by the Waterworks System and the Sewer System. Generally, charges for water services are computed by the Authority on the basis of metered water use for the immediately preceding calendar year. Accordingly, with certain exceptions, the Fiscal Year 2007 water charges are based on the Local Bodies' metered water use in calendar year 2005. In setting water rates, the Authority first identifies through its budgeting process the total amount of revenue which must be raised through water rates in a given fiscal year, net of other anticipated sources of revenue, such as investment income, receipts from water supply contracts and other special arrangements. Water charges are computed based on the proportional number of gallons consumed by each Local Body.

Sewer charges are computed on a proportional allocation basis utilizing, among other things, total flow, contributing population and census population for each Local Body. Consistent with the initial step in setting water rates, the Authority first determines the total amount of revenue to be raised from sewer charges. The total amount of required revenue for the Sewer System is allocated either to operating costs or capital costs. Operating costs are allocated to each Local Body based on the average of the prior three calendar years' total flow, with adjustments for strength of flow to take into account above-average concentrations of total suspended solids and biochemical oxygen demand. Capital costs, including debt service, are allocated to each Local Body based on a combination of (i) average of the prior three years' peak month wastewater flow and average concentrations of total suspended solids and biochemical oxygen demand, (ii) the proportion of the population of the Local Body which is served by the local sewer system (the "contributing population") to the total contributing population in the Sewer System, and (iii) the proportion of the Local Body's U.S. census population, based upon the Commonwealth's most recent bi-annual update (the "census population"), to the total census population in the Sewer System.

HISTORICAL RATES AND CHARGES

The Authority's rates and charges have increased at an average annual rate of approximately 4.2% for the period from Fiscal Year 2003 through Fiscal Year 2007. To date during this period, 100% of the Authority's rates and charges were collected within 30 days of their due dates, except for one instance in which the Authority made special arrangements with a town to extend its due date. The following table sets forth the aggregate budgeted charges of the Authority from Fiscal Year 2003 through Fiscal Year 2007, but does not include state debt service assistance allocated and received after the Authority's adoption of its Current Expense Budgets for Fiscal Years 2004 and 2005. The table also sets forth the percentage increase in charges in each fiscal year over those of the prior fiscal year.

**HISTORICAL RATE REVENUE
AND PERCENTAGE INCREASES¹**
(dollar amounts in millions)

Fiscal Year	<u>Water</u>		<u>Sewer</u>		<u>Combined</u>	
	<u>Amount</u>	<u>Increase</u>	<u>Amount</u>	<u>Increase</u>	<u>Amount</u>	<u>Increase</u>
2003	\$112.5	--	\$304.2	--	\$416.7	--
2004 ²	123.8	7.33%	312.0	2.60%	435.8	3.89 ³ %
2005 ⁴	134.3	8.52	318.7	2.12	453.0	3.94
2006 ⁵	156.5	16.54	315.7	(0.94)	472.2	4.24
2007 ⁶	163.1	4.21	332.2	5.24	495.4	4.90

¹ Does not include revenues received by the Authority from Local Bodies pursuant to contracts or special act which are accounted for as other charges for service rather than as rates and charges.

² Based upon the FY04 CEB; does not reflect the receipt of \$4.1 million of state debt service assistance.

³ In Fiscal Year 2004, the towns of Marlborough and Southborough became part of the rate revenue base, resulting in the Fiscal Year 2004 rate revenue requirement being \$3.1 million higher than it would have been. In order to provide an accurate basis for comparison, the rate revenue change from Fiscal Year 2003 to Fiscal Year 2004 is based on the final Fiscal Year 2003 rate revenue requirement plus \$2.8 million in Fiscal Year 2003 of other user charges revenue from Marlborough and Southborough.

⁴ Based upon the FY05 CEB; does not reflect the receipt of \$8 million of state debt service assistance.

⁵ Fiscal Year 2006 rate increase reflected the then-anticipated receipt of \$10 million of state debt service assistance. The Authority subsequently received \$9.6 million of state debt service assistance in Fiscal Year 2006.

⁶ Reflects the anticipated receipt of \$18.75 million of state debt service assistance, although there can be no assurance that the Authority will receive this amount. See "Legislative and Other Developments" herein.

The Authority has completed the majority of the projects in its CIP, including the Deer Island Wastewater Treatment Plant (the "Deer Island Treatment Plant," and, together with related facilities, the "Deer Island Project"), the MetroWest Water Supply Tunnel and the John J. Carroll Water Treatment Plant and has turned its focus to the construction and completion of remaining court-mandated projects, most notably its long-term CSO Control Plan, and the rehabilitation, repair and maintenance of its infrastructure. In recent years, the Authority has managed rate increases through the use of commercial paper, refinancing existing debt at lower interest rates, issuance of variable rate debt, additional borrowing at subsidized interest rates from the SRF, use of reserves to defease debt and various efficiency and cost control strategies, including significant reductions in staffing levels. Notwithstanding its success in mitigating rate increases, due to its debt service requirements, the Authority currently projects that, absent unanticipated new sources of revenue or other unexpected changes to its programs, its future rates and charges will experience larger annual increases than in the most recent fiscal years.

Beginning in Fiscal Year 1994, the Authority received funding through the Commonwealth's Water and Sewer Rate Relief Fund (the "Fund"). The Fund provides state debt service assistance to issuers of eligible indebtedness, such as the Authority, for qualified projects in order to mitigate increases in rates. The Commonwealth appropriated to the Fund \$38.7 million for Fiscal Year 2003, \$5 million for Fiscal Year 2004, \$10 million for Fiscal Year 2005, \$12.5 million in Fiscal Year 2006 and \$25 million in Fiscal Year 2007. Of these amounts, the Authority received state debt service assistance for Fiscal Years 2004, 2005, and 2006 in the amounts of \$4.1 million, \$8 million, and \$9.6 million, respectively. The Authority's FY07 CEB includes \$18.75 million in state debt service assistance, although there can be no assurance that the Authority will receive this amount. See "Legislative and Other Developments" herein. Due to Commonwealth budget constraints, the Authority did not receive any state debt service assistance in Fiscal Year 2003.

FUTURE RATES AND CHARGES

While the Authority expects to continue to seek and adopt measures to moderate its rate increases in the future, the Authority's rates and charges must continue to be increased to meet the increased debt service costs necessary to finance the facilities included in the CIP, and to fund increased operating expenses resulting from the operation of such facilities. The Authority has developed planning estimates of its future rate revenue requirements and the related percentage rate increases for Fiscal Years 2007 through 2012. These estimates assume the receipt of debt service

assistance in the amount of \$18.75 million each year, although there can be no assurance that the Authority will receive such amounts. See “Legislative and Other Developments” herein and Appendix B – “Supplemental Engineering and Financial Feasibility Report” hereto.

The Authority’s planning estimates assume an inflation rate of 2.5% for capital projects which are not yet under contract, an annual capital budget expenditure rate of 85%, with two-thirds of the remaining 15% assumed to be spent three years later; and that the costs of the capital program will be as currently set forth in the FY07 CIP, which was approved by the Authority’s Board on June 28, 2006. The planning estimates and the FY07 CIP do not reflect the addition of new capital projects included in the Authority’s Master Plan. High priority projects identified in the Master Plan have been included in the Proposed FY08 CIP and are expected to be incorporated into the planning estimates in future years. The planning estimates assume that all of the Authority’s future long-term bond financings will consist of 40-year debt with an interest rate of 6% in Fiscal Years 2008 through 2012. To reflect current economic conditions, operating expenses for Fiscal Year 2008 are inflated at rates higher than 2.5%. These inflated rates include assumed increased expenses related to labor, chemicals and maintenance of 5.0%, 8.3% and 9.5%, respectively. For Fiscal Year 2009 and afterward, operating expense inflation rates for facilities currently in operation are assumed to be 2.5%. The Authority has assumed, for the purposes of estimating future rates and charges, that state debt service assistance will be provided in the amount of \$18.75 million annually. Although not binding on future legislatures, based upon recent experience and other factors, the Authority believes that it is reasonable to assume that the Commonwealth will continue to appropriate debt service assistance in future years. The Authority cannot predict the amount of debt service assistance that will actually be appropriated in future years. If debt service assistance is not appropriated or is appropriated in lesser amounts than the Authority has assumed, rates and charges will be increased as necessary. The planning estimates do not take into account any debt service savings resulting from the issuance of the Series B Bonds and the defeasance of the Refunded Bonds.

The table below sets forth the Authority’s estimates of its rate revenue requirements for Fiscal Years 2007 through 2012 based on the FY07 CEB. The Authority believes that the estimates are based upon realistic cost estimates and other assumptions, including the annual receipt of debt service assistance, and include adequate provision for contingencies. However, as discussed below, there can be no assurance that actual revenue requirements or expenditures will not vary from current estimates and cause actual rates and charges to be different from current estimates. For a discussion of risk factors that could lead to higher costs in the CIP, see “Capital Improvement Program – Factors Affecting the Capital Projects.”

**ESTIMATED FUTURE RATE REVENUE REQUIREMENTS
AND PERCENTAGE INCREASES**
(dollar amounts in millions)

<u>Fiscal Year</u>	<u>Rate Revenue</u> ¹	<u>Percentage Increase</u>
2007	\$495.4 ²	--
2008	539.3	8.9%
2009	587.2	8.9
2010	639.3	8.9
2011	684.9	7.1
2012	714.6	4.3

¹ Based on the FY07 CEB; assumes the annual receipt of \$18.75 million of state debt service assistance, although there can be no assurance that the Authority will receive such amounts. See “Legislative and Other Developments” herein and Appendix B – “Supplemental Engineering and Financial Feasibility Report” hereto.

² Actual rate revenue requirement for Fiscal Year 2007.

See Appendix B for a discussion of the Consulting Engineer’s rate projections through Fiscal Year 2012.

Actual retail rate increases of specific Local Bodies vary considerably because of different practices among Local Bodies to the extent to which the Authority's rates and charges are incorporated into retail user charges and the disparity in levels of the local water and sewer costs of the Local Bodies. Based upon a 2006 survey conducted by the Authority's Advisory Board of Local Bodies' rates and charges (the "2006 Survey") and the Authority's budgeted rates and charges for Fiscal Year 2007, and assuming annual household water usage of 90,000 gallons, the annual average household combined water and sewer bill in those Local Bodies that receive full water and/or sewer services from the Authority is estimated to be \$979. Actual annual bills vary from this average, in part due to the fact that there are certain Local Bodies which in the past raised their own retail rates at paces different from the Authority's rate increases.

The Local Bodies fund their payment of the Authority's rates and charges in a variety of ways so that it is difficult to generalize about the effect of the Authority's future rate increases on retail ratepayers, including households and businesses in the service area. However, for illustrative purposes, based upon data provided by the Authority, the Consulting Engineer has calculated the impact of the projected rate increases on an average household in a hypothetical Local Body, as described in the Supplemental Feasibility Report included as Appendix B hereto. The average household in the circumstances assumed by the Consulting Engineer would pay an estimated retail user charge for combined water and sewer service of approximately \$979 in Fiscal Year 2007. This estimate is based on the Authority's FY07 CEB, Fiscal Year 2007 rates and charges, and the 2006 Survey. The Consulting Engineer's assumptions include: (1) that the Local Body which provides retail services to such household receives full water and sewer service from the Authority; (2) that the Local Body passes on to each household it serves 100% of the increase in the Authority's charges and of local charges in the form of retail user charges; (3) that such costs of the Local Body, other than Authority charges, will increase by 5% per year in each of the fiscal years up to and including Fiscal Year 2012; (4) that the Authority charges in Fiscal Year 2007 constituted approximately 72% of the Local Body's total costs; and (5) that the household consumes 90,000 gallons of water annually. Provision for and payment of these increases will depend on a number of factors, including the Local Bodies' methods of funding Authority charges and the availability of local sources of revenue.

Actual future experience with respect to both the Authority's aggregate rates and charges and the Local Bodies' retail charges, as well as actual usage, is likely to vary from the estimates set forth above, although the Authority cannot predict what those variations will be.

From time to time, public concern is expressed regarding the increasing level of the Authority's rates and charges. The Authority believes that public awareness of several factors will assist to mitigate public opposition. These factors include: (i) the federal and state legal and regulatory mandates (including legal enforcement orders issued by courts or administrative agencies) to which much of the CIP responds, (ii) the importance of improvements to the Systems to support future regional economic growth, (iii) public support for meeting environmental protection and public health goals, and (iv) the Authority's success in mitigating rate increases during the past five Fiscal Years, resulting in an average annual increase of approximately 4.2% from Fiscal Year 2003 through Fiscal Year 2007.

The Authority believes that the considerations described above have contributed to the Authority receiving substantial financial assistance, from both the federal and state governments, to help finance the CIP. This financial assistance – in the form of capital grants, SRF loans at subsidized interest rates, and state debt service assistance – helped in the past to mitigate rate increases. The Authority believes that SRF loans and state debt service assistance will continue to be necessary in order to mitigate future rate increases and to assure that revenue requirements continue to be met. Accordingly, the Authority will continue to pursue such financial assistance for its programs through legislative and other avenues. There can be no assurance, however, as to the continuation of state and federal support.

ENFORCEMENT

The Authority has adopted, and is authorized by the Act to enforce, billing and collection procedures and regulations, including requirements for the submission to the Authority of relevant information regarding the provision of retail services by Local Bodies. In the event any charge to a Local Body is not paid when due, the Act authorizes the Authority to recover the amount due, together with interest and other actual damages, by action in the state superior court.

Without suit, the Authority may use an intercept mechanism (the "local aid intercept") established by the Act to recover amounts unpaid by a Local Body. To trigger this mechanism, the Authority must certify to the State Treasurer the amount of any unpaid charge, whereupon the State Treasurer is required by the Act to deduct such unpaid charge

from all amounts payable to the Local Body by the Commonwealth, if any, regardless of their intended use (including state reimbursements, grants and general local aid funds) and to pay such amount over to the Authority. For a description of general local aid funds as a source of revenue available to Local Bodies to pay Authority charges, see “Local Bodies – Municipal Sources of Revenue.” The Authority has covenanted in the General Resolution to use this enforcement mechanism in the event that a Local Body fails to make timely payment. See “Security for the Series A/B Bonds – Community Obligation and Revenue Enhancement Fund” and Appendix C “Summary of Certain Provisions of the General Resolution – Community Obligation and Revenue Enhancement Fund.” The Authority has successfully used the local aid intercept six times since 1990, including, in one case, following a Local Body’s protesting of the Authority’s rates and charges. The amounts intercepted represented less than one-tenth of one percent of all rates and charges assessed and collected in the applicable fiscal year. The Authority has not used the local aid intercept since Fiscal Year 1993.

Distributions of local aid payable to the municipalities served by Special Purpose Local Bodies, including the BWSC, would not be available to meet unpaid charges due the Authority through the local aid intercept. Municipalities served by such Special Purpose Local Bodies account for approximately 32% of the Authority’s combined rates and charges assessed for Fiscal Year 2007.

Under the laws of the Commonwealth, there are currently several other similar local aid intercept mechanisms that may affect the amount available for intercept on behalf of the Authority. The State Treasurer is authorized to deduct from a Local Body’s local aid distributions amounts owed by such Local Body to the Commonwealth for certain assessments and charge-backs. In addition, under the so-called Qualified Bond Act, cities and towns in the Commonwealth, including certain Local Bodies, may secure their bonds and notes by authorizing the State Treasurer to intercept from their respective local aid distributions the amount necessary to pay principal and interest on such debt. Under state law, the amount available for intercept on behalf of the Authority also may be affected by actions taken by or on behalf of the state Department of Revenue, the Department of Education, any public transportation authority or a regional transit authority, among others, with respect to amounts owed to or by a Local Body. Finally, under the Commonwealth legislation establishing the SRF, the State Treasurer may, under certain circumstances, deduct from a community’s local aid distribution (i) the amount of charges owed by the community to the SRF, (ii) the amount of charges owed by the community to any entity which provides wastewater or drinking water service to the community and has a repayment obligation to the SRF (a “Regional Unit”) which the Regional Unit has not fulfilled by reason of the default of such community in its payment obligations to the Regional Unit, and (iii) the community’s pro rata share of any payment obligation of a Regional Unit to the SRF which has not been fulfilled but not due to the default of any particular community or communities served by the Regional Unit. Since the Authority is a Regional Unit under the SRF statute, failure by the Authority to pay debt service on its loans from the SRF would permit the SRF to exercise its intercept against the Local Bodies. As of December 31, 2006, the Authority had outstanding \$917 million in aggregate principal amount of loans from the SRF. The SRF also has made loans to or purchased local governmental obligations from 36 Local Bodies in an approximate aggregate principal amount of \$208.5 million outstanding as of November 1, 2006, the debt service on which also is subject to intercept.

In addition to the possibility of a Municipal Local Body’s local aid being accessed by another offset mechanism prior to the Authority’s attempt to intercept it, the availability of local aid in the future to satisfy unpaid charges imposed by the Authority will be dependent upon, among other things, the aggregate amount actually appropriated by the state legislature and distributed by the Governor in a fiscal year. For a discussion of these and other factors affecting local aid, see “Local Bodies – Municipal Sources of Revenue” and “Local Bodies – Economic Factors.”

OTHER SOURCES OF REVENUE

The Authority receives revenues from other sources, including water supply contracts and other arrangements between the Authority and certain Local Bodies under which amounts paid to the Authority are not accounted for by the Authority as rates and charges (although such contract revenues are included in the definition of Rates and Charges for purposes of the General Resolution). See “Local Bodies – Special Arrangements.” Revenue under such contracts is budgeted to be approximately \$6.9 million in Fiscal Year 2007, including water supply revenues from three Local Bodies (Chicopee, South Hadley Fire District No. 1 and Wilbraham). The Authority also receives investment earnings on various funds which it holds. Such earnings are budgeted to total approximately \$37 million in Fiscal Year 2007. Revenues from permits, fines, fees and other miscellaneous sources are budgeted to total approximately \$5.3 million in Fiscal Year 2007.

LOCAL BODIES

GENERAL

The Authority provides services to Local Bodies on a wholesale basis. The obligation of the Local Bodies to pay for these services is a general obligation payable from any and all sources of revenue available to the Local Bodies. The legal structure of a Local Body determines which revenue sources are available to it under state law. The revenues available to Special Purpose Local Bodies, each a retail system operator, are limited primarily to retail user fees and charges and investment income. Such entities have no taxing power and do not ordinarily receive distributions of local aid. Revenues of Municipal Local Bodies used to pay the Authority's rates and charges are derived primarily from retail user charges, property taxes, and local aid. All Municipal Local Bodies have instituted retail user charges, although there are substantial differences in the proportion of its full costs that each Municipal Local Body recovers through its retail user charges.

BOSTON WATER AND SEWER COMMISSION

The BWSC is budgeted to account for approximately 31.7% of the Authority's combined rates and charges assessed for Fiscal Year 2007. Established in 1977 as a public instrumentality, a body politic and corporate and a political subdivision of the Commonwealth, the BWSC is responsible for the retail operation of the water distribution and wastewater collection and storm water drainage systems of the City of Boston (the "City") and for the maintenance and improvement of such systems. The BWSC purchases its water in bulk from the Authority. Such water is delivered through 29 active metered connections located at various points throughout the BWSC's water distribution system. The BWSC's sewer system transports the City's wastewater to the Authority's interceptor sewers which convey the wastewater to the Authority's Deer Island Treatment Plant for treatment and disposal.

The Authority's charges to the BWSC constitute general obligations of the BWSC. The BWSC has no taxing power but funds its operations through the collection of user fees and charges. Chapter 436 of the Acts of 1977 of the Commonwealth (the "BWSC Act") requires the BWSC to establish its rates and charges at levels sufficient to (i) pay the current expenses of the BWSC (including the Authority's rates and charges), (ii) pay all BWSC debt service, (iii) create and maintain reasonable reserves required by any bond resolution, (iv) provide funds for paying the cost of all necessary repairs, replacements and renewals of the BWSC's systems, and (v) pay or provide for any and all amounts which the BWSC may be obligated to pay or provide for by law or contract. The BWSC's rates and charges are independently set by the BWSC and are not subject to regulation or approval by any other governmental body. However, the BWSC is required to give written notice to the Authority of its proposed rules and regulations, including its rates, relating to its water and sewer services prior to adoption.

The BWSC serves approximately 86,000 accounts. Its 20 largest users as of June 30, 2006 are estimated to account for approximately 16.7% of the BWSC's aggregate retail user charges. Its customers include many large commercial entities, governmental agencies and not-for-profit institutions including its five largest customers: the Boston Housing Authority, the City of Boston, Harvard University, Boston University and the Massachusetts Port Authority. The BWSC has realized surpluses from its operations in each year since its inception.

The BWSC has issued revenue bonds to finance improvements to its water distribution and wastewater collection systems. As of January 1, 2007, the BWSC had approximately \$319.7 million aggregate principal amount of revenue bonds outstanding. In addition, the BWSC has received loans from the SRF and combined loans/grants from the Authority's Infiltration/Inflow, Local Water Infrastructure Rehabilitation Financial Assistance Program and Pipeline Assistance Program. As of January 1, 2007, the BWSC had \$16.4 million of its SRF loans and \$37.9 million of its loans from the Authority outstanding. In the resolutions providing for the issuances of its revenue bonds, the BWSC has granted a security interest on its revenues as security for its revenue bonds. The BWSC bond resolutions also provide that debt service on the BWSC's revenue bonds and operating expenses of the BWSC shall be paid prior to the Authority's rates and charges.

The single largest component of the BWSC's expenses has been assessments to the BWSC by the Authority. Authority assessments for the costs of water supply and wastewater treatment services provided to the BWSC have continued and, based on BWSC projections, will continue to increase as a percentage of the BWSC's total expenses. BWSC financial statements show the Authority's assessments to the BWSC to be 62.4% of the total costs of operation of

the BWSC in calendar year 2006. As of January 1, 2007, the BWSC projected that this percentage would be 62.3% in 2007, 62.7% in 2008, 65.7% in 2009, 65.6% in 2010 and 65.44% in 2011.

For calendar years 1994 through 2001, there had been no increase in the BWSC's combined water and sewer rates. In calendar year 2002, the BWSC's combined water and sewer rate increased 8.9%. In January 2003, such rate increased 8.9%, and there was an additional increase of 3.9% in April 2003. The combined water and sewer rate increase for calendar year 2004 was 5.8%. There was no increase for calendar year 2005. In 2006, the BWSC's combined water and sewer rate increased 9.85%. Effective January 1, 2007, the BWSC's combined water and sewer rate increased 9.25%. As of January 1, 2007, the BWSC estimated that over the period from calendar years 2008 through 2011, the Authority's assessments to the BWSC will increase at an average annual rate of 7.71% and the BWSC's rates will increase at an average annual rate of 7.75%. The BWSC's estimates are based upon the Authority's Fiscal Year 2007 Current Expense Budget ("FY07 CEB") planning estimates. See "Rates and Charges – General" above. The BWSC is able to mitigate the impact of the Authority's assessments on its rates and charges to its retail customers through the funding of its rate stabilization fund, which has increased over the past several years. The BWSC expects to use the fund in the coming years to continue to mitigate increases in the BWSC's retail rates and charges.

From 1986 to 2005, the BWSC used a ten-block inclining rate structure in order to promote water conservation. In 2005, the BWSC completed a rate structure study in which it was determined that the rate structure should be reduced to six blocks. The 2007 rate schedule calculates charges based on a six-block inclining rate structure. The BWSC's staff believes that this structure provides conservation incentives to all users, increased stability of the BWSC's revenues, and some relief to those customers least able to pay rising water and sewer rates, and ensures the efficient allocation of the costs of providing water, wastewater and stormwater drainage services.

MUNICIPAL SOURCES OF REVENUE

General. Cities and towns in the Commonwealth are limited by state law as to the types of revenues that they can raise to support local spending, including for the rates and charges of the Authority. Under current state law, the Municipal Local Bodies may derive their revenues from several sources, including water and sewer user charges, property taxes, local aid distributions, certain excise receipts (including motor vehicle excises, local option excises on hotel and motel room occupancy and aircraft fuel), departmental revenues (including parking fines and building permit fees), and investment income. Some of the revenue sources discussed in this subsection are not available to Special Purpose Local Bodies, including the BWSC.

User Fees and Charges. Each Municipal Local Body owns and operates a distribution system of pipes for water and a collection system for sewage. Each Municipal Local Body is authorized by state law to charge just and equitable retail user charges to cover the respective costs of providing these municipal services, including operation and maintenance of the Municipal Local Body's system, replacement of capital components of the system over time, and the Authority's annual charges to such Municipal Local Body. These retail user charges are not subject to the limitations of Proposition 2½. Under the Act, Local Bodies may establish rates and charges for retail services on a flat rate basis or on an ascending unit rate based on quantity, and may permit adjustments in their local rates for the age, infirmity or poverty of their retail customers.

The Act also permits the Authority, subject to federal and state constitutional restrictions on the impairment of contracts in effect on the effective date of the Act, to require Local Bodies to adopt systems of rates and charges which comply with applicable federal and state law and with Authority policies designed to promote water conservation, full local cost recovery, the elimination of infiltration and inflow of ground and surface waters, and the pretreatment of industrial wastes.

The revenues received by a Municipal Local Body through its retail user charges are not pledged to the payment of any costs of the local systems, including the payment of the rates and charges of the Authority. A Municipal Local Body may elect, however, to segregate such retail user charges and apply them only to the costs of the respective local systems.

Enforcement remedies are available under state law to Municipal Local Bodies to collect unpaid retail user charges. A Municipal Local Body may terminate water and sewer service to any retail user who has not paid the respective charges. In addition, if a Municipal Local Body accepts the applicable statutory sections, unpaid water and

sewer charges become a lien upon the associated real estate by operation of law and are added to the property tax bill for such real estate. In general, the laws relating to the imposition of interest on unpaid real estate taxes and the foreclosure of title to real estate for nonpayment of taxes apply equally to unpaid water and sewer charges.

Among the Municipal Local Bodies, different local policies, including each Municipal Local Body's decision about the extent to which the costs of operating its local system are recovered through its retail rates, and the complexity of its rate structure and its accounting methodologies, result in divergent retail user charges. Currently, while all Municipal Local Bodies have instituted retail user charges, certain Municipal Local Bodies may not recover the entire cost of providing retail services through user charges. The Authority is able to offer technical assistance to the Municipal Local Bodies to help them establish systems of retail user charges and identify costs that can be recovered through such charges.

Property Taxes. Property taxes are raised through assessments against real and personal property in a municipality. State law mandates a revaluation of all taxable property every three years. These revaluations are reviewed and certified by the Commonwealth. In the years between the revaluation, the Commonwealth permits municipalities to establish new values for year-to-year increases in assessments on the basis of market trends, using the most recent revaluation as a basis. These new values, together with the municipalities' proposed tax rate, are subject to annual certification by the Commonwealth. The property tax levy generally is certified by the Commonwealth in the fall. Most municipalities adopt a quarterly payment schedule for property taxes, with installments due on August 1, November 1, February 1 and May 1.

Proposition 2½ generally constrains levels of property taxation, one of the primary sources of revenue for cities and towns in the Commonwealth, and limits the charges and fees imposed on cities and towns by certain governmental entities. The law is not a constitutional provision and accordingly is subject to amendment or repeal by the legislature. Proposition 2½ contains limitations on the revenues which may be collected by certain governmental entities, including a limitation on the property taxes which may be levied by any city or town in any fiscal year to the lesser of (i) 2.5% of the full and fair cash valuation of the real estate and personal property therein, and (ii) 2.5% over the previous year's levy limit plus any growth in the tax base from certain new construction and parcel subdivisions. Proposition 2½ also limits any increase in the charges and fees assessed by certain governmental entities on cities and towns to the sum of (i) 2.5% of the total charges and fees imposed in the preceding fiscal year, and (ii) any increase in charges for services customarily provided locally or services obtained by the city or town at its option.

Any property tax increase in excess of the limits imposed by Proposition 2½ must be approved by a vote of the municipality. However, amendments to Proposition 2½ enacted in 1994 permit a Municipal Local Body, and a Special Purpose Local Body through agreement with the municipalities it serves, to offset increases in user charges resulting from increases in water and sewer debt service costs (including increases in the Authority's debt service costs incorporated into the Authority's rates and charges to such Local Body) through the assessment of property taxes in excess of the limits imposed by Proposition 2½, subject to certain conditions, without requiring a vote of the municipality.

Local Aid. Local aid is the generic term used to describe all distributions made by the Commonwealth to cities and towns, some of which are earmarked for specific programs, the bulk of which are available to the municipality to be applied to any authorized expenditures. Except for amounts distributed to municipalities pursuant to state law from state lottery receipts, all local aid is subject to annual appropriation by the state legislature. The major formula used by the legislature in determining the payment level to each city and town tends to provide proportionately more local aid to communities with relatively lower per capita income and with higher service cost levels in order to compensate for the gap between certain fixed costs incurred by a municipality and its revenue-raising capacity. The bulk of the local aid distributions are, by state law, made quarterly.

From 1999 through 2003, the Commonwealth's direct local aid increased from \$4.3 billion to \$5.1 billion and then decreased to \$4.1 billion in Fiscal Year 2004. The appropriations for direct local aid in the Commonwealth budget for Fiscal Years 2005, 2006 and 2007 were \$4.2 billion, \$4.2 billion, and \$4.6 billion, respectively.

From time to time legislation and voter initiative petitions are approved which affect the amount of local aid to be distributed by the Commonwealth. These include legislation approved by the Governor in October 1986 (which legislation was repealed as of July 1, 1999) and an initiative petition approved by the voters in November 1986. These

two measures, by limiting the annual rate of state tax revenue growth to the average rate of growth in total wages and salaries in the Commonwealth, placed limits on the amount of funds available to be distributed as local aid. Since the Commonwealth's 1989 fiscal year, state tax revenues have been below the allowable limits imposed by law and are expected to be below the limits for the Commonwealth's fiscal year. Additionally, a large portion of local aid has been earmarked for public education to provide more aid to the Commonwealth's poorer communities.

Under the Massachusetts constitution and state finance law, the State Treasurer and the Governor have the authority to withhold or delay local aid payments under certain circumstances. Any available moneys in the state treasury, including amounts appropriated for local aid, may be used as a matter of last resort by the State Treasurer if required to pay Commonwealth notes. Moreover, the statute governing the Commonwealth distribution of school aid (which constitutes a portion of the local aid distribution) provides that such payments are due only to the extent that sufficient funds are available therefor.

Although there can be no assurance that local aid will continue to be available at current levels and not reduced in the future, the Authority believes that the availability of its various enforcement mechanisms, including its statutory authority to intercept local aid distributions, will adequately provide for the payment of its rates and charges. For a comparison of the Authority's rates and charges with respect to each Municipal Local Body, see "The Authority and its Service Areas – Charges to Local Bodies." For a discussion of the Authority's enforcement mechanisms and the possible limits on the availability of the local aid intercept, see "Rates and Charges – Enforcement."

ECONOMIC FACTORS

The Authority's service areas are located primarily in eastern Massachusetts and include most of the metropolitan Boston area. Recent economic data specifically with respect to the service areas is not available, as it is for the Commonwealth and the City of Boston. The state of the Massachusetts economy is reflected in, among other things, income and employment statistics. Massachusetts per capita personal income is among the highest in the nation and income levels in Massachusetts as of September 30, 2006 were well above the national average: \$43,702 compared to \$34,495. The Commonwealth unemployment rate for November 2006 (seasonally adjusted) was 5.0%, which was slightly higher than the unemployment rate for the nation as a whole of 4.5%.

This data has been presented for informational purposes and does not purport to present all factors which may have a bearing on the fiscal and economic affairs of the Local Bodies or the Commonwealth. The Authority cannot assure that they accurately or completely mirror current economic conditions, and the Authority cannot predict general economic trends on the basis of the information available to it. The Authority expects, however, that the Commonwealth's diversified economic base and its position as the transportation and commercial center for New England will continue to provide sources of economic strength to the service area. See also "Rates and Charges – Future Rates and Charges" herein.

SPECIAL ARRANGEMENTS

Twenty Local Bodies are charged for water services pursuant to contracts between the Local Bodies and the Authority. Of these Local Bodies, 14 pay for water services at the full water rates under contracts renegotiated by the Authority with such Local Bodies. Of the remaining six, various arrangements are in effect. Bedford pays at the full water rates through an arrangement with a neighboring Local Body. Southborough receives the first 10.95 million gallons provided at no charge. The three communities which purchase water via the Chicopee Valley Aqueduct – Chicopee, South Hadley, and Wilbraham – pay for water at a rate established by the Board (the "CVA Rate"). These three communities together accounted for 3.5% of calendar year 2005 total consumption. The CVA Rate is set at a level designed to recover all direct operating and debt service costs related to providing service to these communities, as well as a proportional share of the Authority's administrative costs. In addition, Clinton, which accounted for 0.7% of calendar year 2005 total consumption, receives its first 800 million gallons of water per year free of charge pursuant to a special act.

Pursuant to Authority Regulations, continuation of water supply services to any Local Body under special acts or contracts shall be made on such reasonable terms and charges as the Authority shall determine, provided in each instance the Authority determines that (i) the safe yield of the DCR Watershed System, on advice of the DCR Division of Water Supply Protection, is sufficient to meet the projected demand (provided that any Local Body previously

receiving water supply services on a contract basis shall not be denied continuation of service if it has no other local water supply capable of being developed), (ii) no existing or potential local water supply has been abandoned, (iii) the Local Body has adopted a water management plan approved by the state Water Resources Commission, (iv) the Local Body has adopted effective demand management, leak detection and water system rehabilitation measures, (v) a local water source feasible for development has not been identified by the Local Body or the Massachusetts Department of Environmental Protection (“DEP”), and (vi) a water use survey has been completed identifying all local users in the Local Body consuming in excess of 20 million gallons per year.

The provision of sewer services by the Sewer System, in contrast to the special acts and contractual arrangements governing a portion of the services provided by the Waterworks System, is governed solely by the Act and other applicable federal and state environmental quality laws and regulations.

MANAGEMENT AND ORGANIZATION OF THE AUTHORITY

BOARD MEMBERSHIP

The Authority is governed by an eleven-member Board of Directors (the “Board”) chaired by the Secretary of Environmental Affairs for the Commonwealth. The Secretary and four other members are appointed by the Governor – one resident of a Connecticut River basin community and one resident of a Merrimack River basin community who represent water resources protection interests (terms coterminous with the Governor), one upon recommendation of the Mayor of Quincy and one upon recommendation of the Board of Selectmen of Winthrop (each of the latter two memberships are for four-year terms). At least one of the five gubernatorial appointments must be a representative of a minority group. Three members of the Board are appointed by the Mayor of Boston (terms coterminous with the Mayor), and three are appointed by the Advisory Board (staggered three-year terms). See “Advisory Board” below. Six members of the Board constitute a quorum, and the affirmative vote of six members is required to approve any matter put to a vote of the Board. The members of the Board continue to serve until a successor is appointed.

The present members of the Board, their occupations, appointment categories, the dates of their original appointment and the dates of expiration of their terms as members of the Board are set forth on the following table.

BOARD OF DIRECTORS

<u>Member</u>	<u>Occupation</u>	<u>Date and Source of Original Appointment</u>	<u>Current Term Expires</u>
Ian Bowles, <i>Chairman</i>	Secretary of Environmental Affairs	January 4, 2007 Ex Officio	Coterminous with term as Secretary of Environmental Affairs
John J. Carroll, <i>Vice Chairman</i>	General Manager, Town of Norwood	February 27, 1985; Advisory Board	July 1, 2008
Joseph A. MacRitchie, <i>Secretary</i>	Executive Director Quincy Housing Authority	March 8, 1989; Governor (upon recommendation of Quincy)	January 28, 2005*
Rudolph H. Banks	Retired Plumber, Teacher	January 26, 2005 Governor	Coterminous with Governor*
Kevin L. Cotter	Business Manager/Treasurer, Plumbers and Gasfitters Local 12	September 3, 2002; Mayor of Boston	Coterminous with Mayor
Joseph C. Foti	Director of Public Works, City of Chelsea	June 21, 2001; Advisory Board	June 30, 2007
Lucile P. Hicks	Environmental Activist	November 3, 1997; Governor	Coterminous with Governor*
James W. Hunt, III	Chief, Environmental/Energy Services, City of Boston	May 10, 2005; Mayor of Boston	Coterminous with Mayor
Vincent G. Mannering	Executive Director, Boston Water and Sewer Commission	June 19, 1995; Mayor of Boston	Coterminous with Mayor
Andrew M. Pappastergion	Director, Town of Brookline Water and Sewer Division	June 25, 1997; Advisory Board	July 1, 2009
Marie T. Turner	Former Chairperson, Town of Winthrop Board of Selectmen	December 6, 1996; Governor (upon recommendation of Winthrop)	January 28, 2009

* Continues to serve until reappointed or until a successor is appointed.

ORGANIZATION, MANAGEMENT AND STAFF

The staff of the Authority is headed by an Executive Director who is responsible for the implementation of Authority programs, policies and procedures at the direction of the Board. There are several departments which report directly to the Executive Director, including the Office of Emergency Preparedness, the Affirmative Action Compliance Unit, the Internal Audit Department, Public Affairs and the Planning Department.

The Operations Division comprises six departments: Operations Administration, Wastewater Treatment, Environmental Quality, Field Operations, Laboratory Services and Engineering and Construction. In November 2005, the Authority consolidated three engineering and construction groups into one department with subunits for wastewater engineering, water engineering and construction. The Chief Operating Officer (“COO”) heads the Operations Division. Although the Operations Division provides some services on a consolidated basis to more efficiently support both Water and Sewer Systems, the costs for providing water and sewer services are separately tracked in order to comply with the Act.

The Finance Division contains a Treasury Department, a Budget Department, a Controller Department, and a Risk Management Department.

The Law Division addresses legal and regulatory issues involving the Authority.

The Support Services Division is responsible for supervision and coordination of the functions which serve the program divisions, and specifically for the operations of Human Resources, Management Information Systems, Procurement, Real Property and Environmental Management, Fleet Services and Facilities Management.

Brief resumes of the Authority’s senior management appear below:

Frederick A. Laskey, *Executive Director*

Mr. Laskey was appointed Executive Director in May 2001. Before joining the Authority in June 2001, Mr. Laskey served as Commissioner of the Massachusetts Department of Revenue from 1999 to 2001, managing the Commonwealth’s tax administration, child support enforcement and local services. He served as Secretary of Administration and Finance from 1998 to 1999. As Secretary, he was the Governor’s chief fiscal advisor, with oversight of the state’s \$20 billion annual budget and managed the Cabinet Secretariat that oversees the entire state workforce. Before joining the Cabinet, Mr. Laskey served as Senior Deputy Commissioner of the Massachusetts Department of Revenue from 1994 to 1998, and was designated by the Commissioner to serve on the Board of Bank Incorporation. From 1993 to 1994, he served as Assistant Secretary in the Executive Office for Administration and Finance. Mr. Laskey holds a Bachelor of Arts degree in political science and history from University of Massachusetts, Boston. Mr. Laskey has a contract with the Authority that expires in 2009.

Michael J. Hornbrook, *Chief Operating Officer*

Mr. Hornbrook was appointed the first Chief Operating Officer of the Authority in June 2000. Prior to this appointment, from 1995 to 2000, Mr. Hornbrook was responsible for the overall management of the Authority’s CSO, Infiltration/Inflow, and Wastewater System planning programs. Previously, he directed the development and administration of the Sewerage Division’s capital projects (1994-1995), and was responsible for the management of individual wastewater capital projects (1989-1994). From 1980 to 1989, Mr. Hornbrook held various engineering positions within the Massachusetts Department of Environmental Protection, Divisions of Waterways, Water Supply and Water Pollution Control. Mr. Hornbrook received a Bachelor’s degree in civil engineering from the University of Massachusetts, Amherst. Mr. Hornbrook has a contract with the Authority that expires in 2009.

Patricia A. Filippone, Chief Financial Officer

Ms. Filippone was appointed Chief Financial Officer in May 2006. She served as Treasurer of the Authority from June 2004 to September 2006. Prior to her appointment as Treasurer, Ms. Filippone served as Controller from August 2002 through June 2004, responsible for managing the accounting, accounts payable, payroll and rates departments. Ms. Filippone also served as the Accounting Manager and Accounting and Financial Systems Manager from February 1995 to August 2002, responsible for managing the accounting department and project management of financial system implementation. Prior to joining the Authority, Ms. Filippone was an Audit Manager with Coopers & Lybrand LLP and worked there from June 1988 to February 1995. Ms. Filippone is a Certified Public Accountant and holds a Bachelor of Science degree in business administration, with a major in accounting, from Babson College.

Ralph M. Wallace, Treasurer

Mr. Wallace was appointed Treasurer of the Authority in September 2006. Prior to his appointment as Treasurer, Mr. Wallace was the Director of the Authority's CSO program from October 2003 to September 2006, and was responsible for managing the regulatory approval, planning, design, and permitting of the Authority's long-term CSO control program. From September 1994 until October 2003, he held several senior management positions within the Authority's Program Management Division, including Director of Program Management, and was responsible for directing the design, construction and start-up of the Boston Harbor Project. Prior to joining the Authority, Mr. Wallace was a consultant engaged in economic feasibility analysis, financing, design and implementation of transportation infrastructure and industrial development projects. Mr. Wallace began his career working in several capacities for the City of New York, managing economic development projects. Mr. Wallace holds a Bachelor of Science degree in sociology and economics from Florida State University and a Master of Regional Planning degree from the University of North Carolina at Chapel Hill.

Steven A. Remsberg, General Counsel

Mr. Remsberg was appointed General Counsel in May 2004. Prior to joining the Authority, Mr. Remsberg served in the position of Acting General Counsel with the Massachusetts Department of Revenue from March 2003 to May 2004. Between April 2000 and March 2003, Mr. Remsberg served as the Associate General Counsel and from January 1997 to April 2000, as Chief of the Litigation Bureau at the Department of Revenue. Between 1989 and 1997, Mr. Remsberg practiced law with the Boston firm of Hinckley, Allen & Snyder and between 1979 and 1989 with the Boston firm of Snyder, Tepper & Comen. Mr. Remsberg holds a law degree from the University of Pittsburgh Law School and a bachelor's degree in economics from Dickinson College.

Kevin P. Feeley, Managing Director

Mr. Feeley was appointed Managing Director in February 2006. Prior to his appointment, from 1985 to 2006, Mr. Feeley served as Director of Procurement. Prior to joining the Authority Mr. Feeley served as a consultant to the Town of Arlington responsible for the development and reuse of surplus school buildings and surplus space from 1983 to 1986. Between 1980 and 1983, Mr. Feeley was engaged in a private law practice with specific emphasis on real estate and commercial law. From 1963 to 1983, Mr. Feeley held various positions including General Counsel for the Boston Housing Authority, Assistant Deputy Commissioner for Legal Affairs for the City of Boston and Assistant General Counsel to the Secretary of State for the Commonwealth of Massachusetts. Mr. Feeley holds a law degree from the New England School of Law and a Bachelor's degree in business administration from The College of the Holy Cross.

EMPLOYEES

As of December 1, 2006, the Authority had 1,254 employees, including persons with professional qualifications in the fields of construction, engineering, environmental science, accounting, finance, law and management. The Authority believes that future staffing needs to support facilities constructed under the CIP are adequately reflected in the projected revenue requirements established by the Consulting Engineer.

Under Massachusetts law, employees of the Authority have certain organizational and representational rights which include the right to organize, to bargain collectively by representatives of their choosing on questions of wages, hours and other terms and conditions of employment and to engage in lawful concerted activities for bargaining or other mutual aid or protection. The law prohibits strikes by Authority employees.

As of December 1, 2006, 1,166 of the Authority's employees were organized into five collective bargaining units represented by four different unions: two units are represented by an alliance between the National Association of Government Employees ("NAGE") and the United Steelworkers of America (Units 1 and 6); one by the Massachusetts Organization of Engineers and Scientists (Unit 9); one by NAGE (Unit 3); and one by the American Federation of State, County and Municipal Employees (Unit 2). The Authority has collective bargaining agreements with all of its unions. With the exception of the contract with Unit 2, which expires on March 29, 2007, all the other union contracts expire on June 30, 2007. Negotiations with respect to successor agreements are ongoing.

The Act provides that no collective bargaining agreement entered into by the Authority shall limit inherent management rights including (i) employment, assignment and promotion of employees, (ii) termination and discharge of employees on reasonable grounds, (iii) determination of the Authority's levels of service and staffing and the methods, means and personnel for performing operations, (iv) supervision, evaluation and establishment of productivity standards, and (v) use of part-time regular employees and independent contractors and vendors.

The Authority believes that its relationships with its employees and their representatives are generally good.

ADVISORY BOARD

The Advisory Board to the Authority was established by the Act to serve as a liaison between the Authority and the Local Bodies. It is composed of one representative from 60 of the 61 Local Bodies (Lancaster is not represented on the Advisory Board), one from the Metropolitan Area Planning Council (a legislatively-created, comprehensive regional planning organization), and six persons appointed by the Governor to include an expert in environmental protection, one representative each from the Connecticut River basin, the Quabbin/Ware watershed areas and the Wachusett watershed area, and two persons qualified by membership or affiliation in organizations directly concerned with the recreational or commercial uses of Boston Harbor.

The Advisory Board, whose staff is headed by an executive director and includes a budget analyst and other professionals, is empowered by the Act to do the following:

- Name three members to the Authority's Board;
- Approve, subject to other requirements of the Act, extension of service to additional communities;
- Make recommendations to the Authority on annual expense budgets, capital facility programs and expenditure budgets and user charges;
- Hold hearings on matters relating to the Authority; and
- Make recommendations to the Governor and the legislature regarding the Authority.

The Advisory Board actively monitors the Authority's programs from the perspective of the Authority's rate payers. In addition to participating in the process of formulating the Authority's current expense budgets and capital improvement programs, the Advisory Board has actively pursued legislative support for state debt service assistance, watershed protection and other measures of interest to the Local Bodies. The Advisory Board works with the Authority to enhance community assistance programs and share technical information and resources. In addition, pursuant to the Commonwealth's 1994 fiscal year budget act, the Advisory Board developed a sewer rate methodology to allocate Authority sewer costs among the Local Bodies, which was incorporated by the Authority into the establishment of its rates and charges commencing in Fiscal Year 1996. See "Rates and Charges – General."

The Authority and Advisory Board share the goals of improved service to the Local Bodies and additional financial assistance for the Authority's programs.

RETIREMENT SYSTEMS

All employees of the Authority are members of a contributory retirement system for public employees. The Act provides that all employees transferred to the Authority from the MDC on July 1, 1985 who were members of the State Employees' Retirement System (the "State System") shall remain members of the State System. All other employees of the Authority are members of a separate retirement system established in the Act known as the Massachusetts Water Resources Authority Retirement System (the "Authority System"). The Authority System is managed by a three-member board consisting of the Secretary of the Authority, *ex officio*, a second member elected for a three-year term by the present and retired members of the Authority System and a third member appointed by the Authority for a three-year term. On August 22, 2006, the Governor signed legislation increasing the number of members on the Authority System Board of Directors from three to five. The Authority System has scheduled an election for January 3, 2007 to elect the fourth member and the fifth member will be selected by the other four members in early calendar year 2007.

Neither the Authority nor the Authority System has any liability for retirement benefits paid to those employees who remain members of the State System. For these employees, the total cost of benefits earned while employed by the Authority are paid by the Commonwealth and by the employees' own contributions. As of December 1, 2006, 134 employees of the Authority were members of the State System. While employees of the DCR Division of Water Supply Protection are not members of the Authority System and the Authority is not directly responsible for the payment of benefits, the cost of such benefits can be included in the computation of the expenses of the Division which are reimbursable in part by the Authority. See "The Systems – The Waterworks System."

The retirement benefits of employees of the Authority System are funded in part by employee contributions, investment returns and in part by the Authority. As of December 1, 2006, there were 1,164 active members, 127 inactive members and 271 retirees in the Authority System. The Act requires the Authority to pay annually to the Authority System any amounts needed to finance any pension benefits earned by its members. In Fiscal Year 2006, the Authority contributed \$3.6 million to the System. The Authority has budgeted \$4.1 million for its contribution due to the Authority System in Fiscal Year 2007. The Authority System completed an actuarial study on January 1, 2005.

Employee contributions to both the State and Authority Systems range from 5% of salary to not more than 11% of salary depending upon salary and the initial date of becoming a member of a system. Employees of the Authority do not participate in the federal Social Security Administration System.

The Authority plans to implement GASB Statement Nos. 43 and 45, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans* and *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* for the fiscal years ending June 30, 2007 and June 30, 2008, respectively.

PUBLIC AFFAIRS

The Authority maintains strong relationships with the various constituencies it serves, including the Local Bodies, the Advisory Board, elected and appointed officials, interest groups, and the public at-large. To these constituencies the Authority communicates its goal to improve, maintain, and operate, in a manner which is cost effective and fully accountable to the public, the Authority's water and sewer infrastructure that is vital to enhancing the quality of life and economic well-being of the region.

Public outreach and education – critical to building support for the Authority's operational and environmental objectives – are accomplished through a wide variety of activities. These efforts include community assistance programs, technical assistance to industrial customers, the Authority's web site, rapid response to public inquiries, facility tours, informational publications, school education programs, intergovernmental and media liaisons, and targeted programs for communities impacted by Authority facilities.

FINANCIAL OPERATIONS

GENERAL

As required by the Act, the Authority's operations for sewage collection, treatment and disposal and for delivery of water are treated separately for accounting and billing purposes, and revenues, expenses, assets and funds pertaining to these two operations are segregated by function. Indirect administrative costs and capital costs are allocated to water or sewer operations, as appropriate. The Authority's fiscal year commences on July 1.

The Authority uses a budgetary system of accounting in setting its rates and charges and preparing its annual budget (the "Current Expense Budget") for its current expenses, including operating costs and direct and indirect administrative costs (collectively, "Current Expenses"). United States of America generally accepted accounting principles ("GAAP") are used by the Authority in preparing its monthly internal and annual audited financial statements.

Current and Capital Expense Budgets. In accordance with the Act, the Authority adopts annually a Current Expense Budget, which may be amended from time to time. While the Authority's Current Expense Budget must be submitted to the Advisory Board for comment and recommendation not less than 60 days prior to its adoption, and amendments to the budget must be submitted to the Advisory Board no less than 30 days prior to their adoption, the Authority's Current Expense Budget is not subject to approval by any board (including the Advisory Board), department, agency or other instrumentality of the Commonwealth or any other governmental body.

The Act requires that the Authority adopt and update capital facilities programs for the Systems and capital expense budgets to implement and finance such programs. See "Capital Improvement Program."

MANAGEMENT AND FINANCIAL CONTROLS

The Authority uses a performance-based budgeting format for its Current Expense Budget which provides a basis for measuring operating activities, strengthens managerial accountability for each of the departments and provides a framework for the apportionment of resources. The Authority also uses a system of monthly and quarterly reports on key management indicators. Presentation formats allow for month-to-month, year-to-date, and year-to-year comparisons.

The Authority uses a variety of fiscal management systems to monitor and control Current Expenses. In addition to weekly cash reports, the Authority monitors its spending through monthly variance reports for each of its cost centers. Variance explanations are prepared at the end of the first three quarters of the fiscal year. At the end of the second and third fiscal quarters, the budget variance report includes updated forecasts of year-end expenditures.

The Authority has instituted a set of fiscal controls for the CIP. The Authority prepares monthly and quarterly reports on capital budget performance and semi-annual variance analysis reports on the capital budget. From time-to-time, as necessary, the Authority follows its established budget amendment policy to make adjustments to the capital budget. In addition, procurements are processed by a central department to ensure uniform contract language, standard safeguards and competitive bids for the Authority. Contract amendments and construction change orders are subject to critical review and evaluation by field and budget staff, procurement officers, and legal counsel. The Authority also has instituted audit procedures to examine wage, overhead and profit rates on professional service contracts. Resident inspectors monitor all construction in progress to ensure quality of material and workmanship. Claims by contractors are reviewed and negotiated by the Authority's inspection and legal staff.

The Authority has an integrated management information system for its financial functions, including general ledger, budget, accounts receivable, debt management, cash management, procurement, accounts payable, and payroll systems. The Authority regularly upgrades and enhances this system to ensure the ongoing efficiency of its operation.

The Authority's business plan defines critical operational goals and objectives, as well as related activities and improvements in support of these objectives. The Authority also has developed annual performance targets that provide a quantifiable standard against which to measure progress towards achieving these objectives.

OUTSTANDING AND PROPOSED INDEBTEDNESS

The following table sets forth debt service on the Authority's Outstanding Secured Bonds, including the Series A/B Bonds, for each fiscal year in which such Secured Bonds will be Outstanding.

SECURED BOND DEBT SERVICE¹ (in thousands of dollars)

Fiscal Year	Debt Service On General Revenue Bonds ²		Debt Service On Subordinated Bonds ³		Total Secured Bond Debt Service
	Principal	Interest	Principal	Interest	
2007	\$ 35,580	\$ 151,914	\$ 29,931	\$ 80,300	\$ 297,726
2008	25,020	153,736	37,228	80,861	296,846
2009	60,160	150,685	53,052	78,952	342,849
2010	60,820	147,350	59,826	77,157	345,154
2011	69,795	143,624	87,794	73,811	375,024
2012	79,740	139,386	95,602	70,425	385,153
2013	90,335	134,784	103,186	67,340	395,645
2014	109,880	129,219	108,100	65,323	412,522
2015	102,260	123,089	111,651	62,159	399,159
2016	114,105	116,878	116,175	57,662	404,820
2017	142,570	109,648	92,765	54,764	399,747
2018	167,785	101,088	118,044	50,551	437,467
2019	144,115	92,514	89,308	47,128	373,065
2020	158,775	84,399	92,645	48,211	384,030
2021	105,990	77,508	215,511	43,153	442,162
2022	157,475	70,751	100,808	37,081	366,114
2023	151,975	62,997	138,160	31,629	384,761
2024	119,705	56,255	87,112	28,244	291,316
2025	107,675	50,550	83,392	23,116	264,733
2026	91,750	45,522	82,597	19,976	239,845
2027	90,110	40,957	104,341	16,092	251,500
2028	90,615	36,439	71,327	11,847	210,227
2029	80,315	32,221	54,903	9,288	176,727
2030	64,620	28,661	29,588	7,865	130,734
2031	50,460	25,814	25,213	6,992	108,479
2032	65,675	22,941	25,920	6,132	120,668
2033	60,615	19,806	20,618	5,482	106,521
2034	41,700	17,255	21,714	4,621	85,289
2035	43,805	15,117	21,097	3,658	83,677
2036	46,025	12,871	18,450	2,633	79,979
2037	19,575	11,231	16,491	1,579	48,876
2038	31,680	10,008	14,800	523	57,011
2039	33,190	8,504	-	-	41,694
2040	34,750	6,928	-	-	41,678
2041	36,400	5,278	-	-	41,678
2042	24,545	3,819	-	-	28,364
2043	25,730	2,620	-	-	28,350
2044	11,960	1,795	-	-	13,755
2045	12,445	1,307	-	-	13,752
2046	12,955	799	-	-	13,754
2047	13,485	270	-	-	13,755
Total	\$2,986,165	\$2,446,538	\$2,327,347	\$1,174,554	\$8,934,605

¹ Includes debt service on bonds issued to the SRF, but does not include debt service on commercial paper. SRF debt service is net of subsidy amounts. Totals may not add due to rounding.

² Does not include debt service on defeased bonds or the Refunded Bonds.

³ Variable rate debt was budgeted with an assumed interest rate of 4.75% in Fiscal Year 2007, with the exception of the 1999 Series A and 1999 Series B Bonds, in connection with which the Authority had entered into interest rate swap agreements, and for which the Authority budgeted the fixed interest rates payable pursuant to the respective swap agreements. Such swap agreements expired August 1, 2006. The table assumes a 4% interest rate for the remaining years' interest rate for the Multi-Modal Subordinated General Revenue Bonds, 1997 Series A, 1997 Series B, 1999 Series A, 1999 Series B, 1999 Series C, 1999 Series D, 2001 Series A and 2001 Series B, and the Multi-Modal Subordinated General Revenue Refunding Bonds, 2002 Series C. The Authority has entered into interest rate swap contracts in connection with its Multi-Modal Subordinated General Revenue Refunding Bonds, 1998 Series D, 2000 Series B, 2000 Series C, 2002 Series D, 2002 Series E, 2002 Series F, and 2002 Series G, pursuant to which the Authority pays interest to the swap counterparty at a fixed rate and receives interest at a variable rate. The Authority's current payment obligations under its swap agreements are secured on a parity basis with its Subordinated Bonds; however, any termination obligations would be payable only from amounts in the Commonwealth Obligation Fund. For these series, the table assumes the fixed rate of interest pursuant to the applicable swap contract for the period in which the swap contract is in effect and assumes a 4% interest rate for the period, if any, in which there is no swap contract in effect.

The Authority's Consulting Engineer currently projects that the Authority will issue approximately \$1.014 billion of additional Secured Bonds from Fiscal Year 2007 through Fiscal Year 2012 to finance the FY07 CIP. This projection has not been updated to reflect the Proposed FY08 CIP or the Authority's updated planning estimates. The Consulting Engineer's projection incorporates various assumptions, including assumptions as to interest rates on indebtedness and investments, inflation rates and the size and timing of capital expenditures. For a discussion of these assumptions, see Appendix B. The projection also assumes approval by the state legislature and Governor of adequate and timely increases in the Authority's debt limit. See "Debt Limitation" below. Although this Official Statement does not contain rate projections beyond Fiscal Year 2012, the Authority expects to issue additional Secured Bonds beyond Fiscal Year 2012.

Additionally, the Commonwealth has issued bonds to finance certain watershed preservation projects. The debt service on such bonds is payable annually by the Authority to the Commonwealth as a charge for the costs of the DCR Division of Water Supply Protection. Such charges would constitute Commonwealth Obligations under the General Resolution. These charges are included in the Authority's estimates of its future rates and charges.

DEBT LIMITATION

As enacted in 1984, the Act contained a \$600 million limit on the total amount of unrefunded bonds and notes of the Authority which may be outstanding at any one time. The Authority periodically has requested and received increases in its debt limit as necessary to allow for issuance of bonds in amounts required to finance the CIP. Since 1989, the state legislature has increased the debt limit 14 times, most recently increasing the debt limit to \$6.1 billion in June 2006. Following the issuance of the Series A/B Bonds, the Authority will have outstanding approximately \$5.8 billion of bonds and notes. The Authority plans to seek and expects to obtain additional increases in the limit as necessary to issue debt in order to finance its CIP. All such increases will be subject to the approval of the state legislature and the Governor. If the state legislature and Governor fail to approve sufficient increases, the Authority will be unable to finance the CIP as planned and will be required to adjust its construction plans and schedules and seek alternative sources of funding.

REPORTS

In accordance with the Act, the Authority submits annual reports and five-year progress reports to the Governor, the President of the state Senate, the Speaker of the state House of Representatives, the Advisory Board and the Chairpersons of the state Senate and House Committees on Ways and Means. The annual reports contain financial statements relating to its operations maintained in accordance with GAAP and audited by independent certified public accountants. The five-year progress report is prepared with the participation of an independent citizen panel, documenting activities of the prior period, and anticipated challenges for the future. The most recent five-year report was prepared in December 2005. The Authority retained KPMG LLP, formerly KPMG Peat Marwick LLP, independent auditors, to audit the financial statements of the Authority for each of the ten fiscal years through and including June 30, 2004 and for the fiscal year ended June 30, 2006. Deloitte & Touche LLP, independent accountants, audited the financial statements of the Authority for the fiscal year ending June 30, 2005. Included in Appendix A are the audited financial statements of the Authority at June 30, 2006, and 2005 and for the fiscal years then ended.

Pursuant to the General Resolution, in December 2005, the Authority filed with the Trustee the most recent triennial report of its Consulting Engineer, setting forth a detailed analysis of the Authority's Systems, Current Expense Budget and CIP, including recommendations as to reserve requirements and other matters. The next triennial report is

expected to be filed in December 2008.

MANAGEMENT'S REVIEW OF OPERATING RESULTS

HISTORICAL REVENUES, EXPENSES AND FUND DEPOSITS

The following table is prepared in accordance with the General Resolution and sets forth a summary of the Authority's historical revenues, expenses and fund deposits for Fiscal Years 2002 through 2006. For financial statements prepared in accordance with GAAP regarding Fiscal Years 2006 and 2005, see Appendix A.

HISTORICAL REVENUES, EXPENSES AND FUND DEPOSITS (in thousands of dollars)

	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>	<u>FY 2005</u>	<u>FY 2006</u>
Revenues					
Rates and Charges	\$ 389,518	\$ 416,659	\$ 431,767	\$ 444,269	\$ 472,220
Investment Income ¹	34,967	31,390	29,422	34,925	43,762
Transfer from Rate Stabilization Fund	11,600	14,691	-	-	10,740
Other Income	<u>13,964</u>	<u>12,388</u>	<u>15,110</u>	<u>12,326</u>	<u>18,764</u>
Total Revenues	450,049	475,128	476,299	491,520	545,486
Operating Expenses ²	210,167	208,698	203,318	209,038	223,955
Capital Lease	<u>268</u>	<u>3,217</u>	<u>3,217</u>	<u>3,217</u>	<u>3,217</u>
Net Operating Revenues	239,614	263,213	269,764	279,265	318,314
Debt Service on Bonds ³	149,724	171,332	169,256	158,264	166,412
Other Debt Service ⁴	<u>82,398</u>	<u>85,163</u>	<u>93,587</u>	<u>109,435</u>	<u>119,745</u>
Amount Available After Operations and Debt Service	<u>\$ 7,492</u>	<u>\$ 6,718</u>	<u>\$ 6,921</u>	<u>\$ 11,566</u>	<u>\$ 32,157</u>
Fund Deposits					
Reserve Funds	\$ 0	\$ 0	\$ (20,000) ⁵	\$ 1,000 ⁶	\$ 866 ⁷
Construction Fund ⁸	2,819	4,600	5,468	5,234	5,384

¹ Unrealized gains or losses recorded on investments are also excluded. Fiscal Year 2006 includes the receipt of \$7.5 million from the termination of a swap agreement relating to the Authority's Subordinated General Revenue Bonds, 2000 Series D.

² Includes payment of certain Commonwealth Obligations which are paid after Debt Service on Secured Bonds and which are not included in Operating Expenses for purposes of calculating certain Coverage Covenants; excludes depreciation.

³ State debt service assistance is treated as a reduction of debt service on Bonds for purposes of calculating debt service coverage. Fiscal Year 2004 includes \$15.8 million of deposits to escrow debt maturing in future years.

⁴ Includes debt service on Commonwealth debt, variable rate Subordinated Bonds, and bonds issued to the SRF. Excludes amortized issuance expenses, refinanced principal payments and interest on commercial paper, except that in Fiscal Year 2006, the Authority expensed \$2.9 million of interest on a portion of its commercial paper program prior to the issuance of long-term debt.

⁵ Transferred to Bond Redemption Fund.

⁶ Addition to Insurance Reserve Fund.

⁷ Addition to Operating Reserve Fund.

⁸ Includes deposits from current revenue to fund capital projects.

For Fiscal Years 2003, 2004 and 2006, the Authority ended each such fiscal year with a favorable variance between budgeted revenues and actual revenues of 0.5%, 0.1% and 3.3%, respectively. In Fiscal Years 2003, 2004, and 2006 the positive revenue variances resulted from higher than budgeted revenues for investment income and other revenue. For Fiscal Year 2002 and Fiscal Year 2005, the Authority ended each such fiscal year with an unfavorable

variance between budgeted revenues and actual revenues of 0.8% and 0.2%, respectively. In Fiscal Year 2002, the negative variance resulted from lower than budgeted revenues for investment income. In Fiscal Year 2005, the negative variance resulted from lower than budgeted rate revenue. The Authority ended each of the Fiscal Years 2002 through 2006 with favorable variances between actual and budgeted expenditures, ranging from 0.2% to 1.8%.

FISCAL YEAR 2005

In June 2004, the Board of Directors approved the Fiscal Year 2005 CEB ("FY05 CEB"), which included net expenses of \$492.6 million. Of the amounts budgeted, capital financing expenses accounted for 57%; annual operating and maintenance expenses accounted for 36%; and indirect expenses accounted for the remaining 7%.

The Authority's FY05 CEB, adopted in June 2004, did not assume the receipt of any state debt service assistance from the Commonwealth. Subsequent to the Authority's adoption of the FY05 CEB, the Commonwealth included \$10 million of state debt service assistance in the Commonwealth's budget. On September 1, 2004, the Authority reduced the rate revenue installment that was due from the Local Bodies based on its then-current estimate of state debt service assistance in the amount of \$8.7 million. Taking the then-current debt service assistance estimate into consideration, the increase in the rate revenue requirement as compared to the Fiscal Year 2004 CEB rate revenue requirement was 1.9%. The Authority actually received \$8 million of state debt service assistance in the spring of 2005.

In Fiscal Year 2005 total expenses were \$486.2 million, \$6.4 million less than budgeted. Direct expenses of \$176.8 million were \$770,692 or 0.44% more than budgeted, and capital financing expenses of \$276.1 million were \$5.8 million less than budgeted. Total revenues in Fiscal Year 2005 were \$491.5 million or 0.2% lower than budgeted and \$5.3 million greater than expenses.

FISCAL YEAR 2006

The Fiscal Year 2006 CEB ("FY06 CEB") was adopted by the Board of Directors in June 2005 after Advisory Board comment and adjustments by staff to the proposed budget. The FY06 CEB as originally adopted totaled \$524.9 million. Non-rate revenue totaled \$52.7 million, resulting in a rate revenue requirement of \$472.2 million, an increase of 4.2% compared to the FY05 CEB. The FY06 CEB included \$10 million of state debt service assistance, which was included in the budget as an offset to debt service, and which resulted in a lower rate revenue requirement.

During the first half of Fiscal Year 2006, the Authority anticipated a budget shortfall. In September, and subsequently in November and December 2005, total expenses exceeded the amount budgeted, primarily due to greater than anticipated utilities costs. In January 2006, the Authority's Board of Directors voted to transmit a proposed amendment to the FY06 CEB to the Advisory Board for its review and comment, pursuant to the Authority's Current Expense Budget Management Policies and Procedures. The amendment increased revenue and expenditures in the FY06 CEB by approximately \$5.4 million. Although the amendment was approved by the Board of Directors in May 2006, events and economic trends by that time had essentially eliminated the need for budget increases.

Total expenses during Fiscal Year 2006 were \$519.6 million, \$8.3 million or 1.6% less than the amended budget. Direct expenses of \$189.7 million were \$1.8 million or 1% less than the amended budget, debt service expenses of \$294.8 million were \$4.8 million or 1.6% lower than the amended budget and indirect expenses were \$1.8 million or 4.8% lower than the amended budget.

Total revenues in Fiscal Year 2006 were \$545.5 million, \$17.6 million or 1.9% more than budgeted.

FISCAL YEAR 2007 CURRENT EXPENSE BUDGET

The FY07 CEB was adopted by the Board of Directors on June 28, 2006 after Advisory Board comment and adjustments by staff to the proposed budget. The FY07 CEB totals \$557.1 million. Non-rate revenue totals \$61.8 million, resulting in a rate revenue requirement of \$495.3 million, an increase of 4.9% compared to the FY06 CEB. The Authority expects to receive approximately \$18.75 million in state debt service assistance in Fiscal Year 2007. The Authority has reduced the rate revenue requirement for Fiscal Year 2007 by this amount. See "Legislative and Other Developments."

The \$557.1 million in current expenses for Fiscal Year 2007 consist of approximately \$203.7 million in direct expenses, \$39.2 million of indirect expenses and \$314.2 million of capital financing expenses after offset.

FISCAL YEAR 2007 FIRST QUARTER RESULTS

Total expenses during the first quarter of Fiscal Year 2007 were \$132.2 million, \$5.8 million or 4.2% less than budgeted. Direct expenses of \$45 million were \$4.6 million or 9.3% less than budgeted, debt service expenses of \$77.6 million were \$1 million or 1.2% less than budgeted and indirect expenses of \$9.5 million were \$0.2 million or 2.1% less than budgeted. Direct expenses are under budget primarily due to lower than budgeted electricity pricing, delays in deliveries for diesel fuel and timing of maintenance projects.

Revenues during the first quarter of Fiscal Year 2007 were \$141.1 million, \$1.1 million or 0.8% more than budgeted. This variance is primarily due to greater than budgeted investment income.

DEBT SERVICE COVERAGE

The Authority has met or exceeded the Coverage Covenants, as required by the General Resolution, in each of the last five fiscal years, as shown in the following table.

HISTORICAL COVERAGE
(in thousands of dollars)

	<u>FY2002</u>	<u>FY2003</u>	<u>FY2004</u>	<u>FY2005</u>	<u>FY2006</u>
Operating Revenues	\$403,482	\$429,047	\$446,877	\$456,595	\$490,984
Interest Income	34,967	31,390	29,422	34,925	43,762
Swap Income	3,629	5,318	0 ¹	0	0
Transfers from Rate Stabilization Fund ²	<u>11,600</u>	<u>14,691</u>	<u>0</u>	<u>0</u>	<u>10,740</u>
Total Revenues	453,678	480,446	476,299	491,520	545,486
Operating Expenses	(210,167)	(208,698)	(203,318)	(209,038)	(223,953)
Commonwealth Obligations ³	20,481	19,944	17,678	20,577	21,816
Capital Lease	<u>(268)</u>	<u>(3,217)</u>	<u>(3,217)</u>	<u>(3,217)</u>	<u>(3,217)</u>
Net Revenues	\$263,724	\$288,475	\$287,442	\$299,842	\$340,132
CORE Fund Deposits	0	0	0	0	0
Revenues Available for Primary and SRF Primary Coverage (Before Provision for Transfer to Rate Stabilization Fund)(A)	<u>\$263,724</u>	<u>\$288,475</u>	<u>\$287,442</u>	<u>\$299,842</u>	<u>\$340,132</u>
Provision for Transfer to Rate Stabilization Fund ²	<u>(4,673)</u>	<u>0</u>	<u>0</u>	<u>(2,000)</u>	<u>(8,840)</u>
Revenues Available for Primary and SRF Primary Coverage (After Provision for Transfer to Rate Stabilization Fund)(B)	<u>\$259,051</u>	<u>\$288,475</u>	<u>\$287,442</u>	<u>\$297,842</u>	<u>\$331,292</u>
Required Senior Debt Service Fund Deposits(C) ⁴	<u>\$149,695</u>	<u>\$171,764</u>	<u>\$150,563</u>	<u>\$155,564</u>	<u>\$184,751</u>
Required Subordinated Debt Service Deposits(D)	<u>\$85,790</u>	<u>\$90,482</u>	<u>\$99,080</u>	<u>\$108,474</u>	<u>\$116,423</u>
Coverage:					
Before Provision for Transfer to Rate Stabilization Fund:					
Primary ⁵	176%	168%	191%	193%	184%
SRF Primary ⁶	112%	110%	115%	114%	113%
After Provision for Transfer to Rate Stabilization Fund:					
Primary ⁷	173%	168%	191%	191%	179%
SRF Primary ⁸	110%	110%	115%	113%	110%
Required CORE Fund Deposits ⁹	0.00	0.00	0.00	0.00	0.00
CORE Fund Deposits	0.00	0.00	0.00	0.00	0.00

¹ Beginning in Fiscal Year 2004, Swap Income is included in Interest Income.

² Amounts transferred from the Rate Stabilization Fund to the Revenue Fund are included as Revenues for coverage purposes in the year of such transfer up to an amount equal to .1 times Required Debt Service Fund Deposits for such year. Consistent with this treatment, in calculating coverage for a fiscal year, moneys transferred to the Rate Stabilization Fund are not included as Revenues.

³ Commonwealth Obligations are paid after debt service on Bonds and are, therefore, excluded from Operating Expenses in calculating coverage.

⁴ Fiscal Year 2004 does not include \$15.8 million of deposits to escrow debt maturing in future years. Fiscal Year 2006 includes \$17.2 million of debt service deposits for the 1990 Series A Capital Appreciation Bond.

⁵ A divided by C.

⁶ A divided by the sum of C and D.

⁷ B divided by C.

⁸ B divided by sum of C and D.

⁹ The CORE Fund is required to be funded at the end of each fiscal year in the amount of at least 10% of the Required Debt Service Fund Deposits for all Bonds Outstanding as of the beginning of such fiscal year.

PROJECTED REVENUES, EXPENSES AND FUND DEPOSITS

The following table sets forth a summary of the Consulting Engineer's projection of revenues, expenses and fund deposits for Fiscal Years 2007 through 2012. The Coverage Covenants are projected to be satisfied in each such fiscal year. For a discussion of the assumptions and methodology underlying these projections and projected coverage levels, see Appendix B. The Consulting Engineer's projections do not take into account any debt service savings resulting from the issuance of the Series B Bonds and the defeasance of the Refunded Bonds.

PROJECTED REVENUES, EXPENSES AND FUND DEPOSITS¹

(in thousands of dollars)

	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>
Revenues						
Rates & Charges	\$495,359	\$539,338	\$587,221	\$639,341	\$684,943	\$714,643
Investment Income	32,261	27,500	28,129	28,993	29,606	30,272
Transfers from Rate Stabilization Fund	12,577	16,102	6,359	6,507	0	0
Other Income	<u>16,943</u>	<u>13,716</u>	<u>12,959</u>	<u>13,088</u>	<u>13,311</u>	<u>13,205</u>
Total Revenues	557,140	596,656	634,668	687,929	727,861	758,121
Operating Expenses ²	239,673	257,171	260,851	267,133	276,043	284,854
Capital Lease	3,217	3,217	3,217	3,217	3,217	3,217
Net Operating Revenues	314,250	336,268	370,600	417,579	448,601	470,050
Debt Service on Bonds ³	194,560	223,106	235,282	251,456	266,219	279,402
Bond Redemption ⁴	(18,750)	(38,889)	(25,470)	(27,301)	(18,750)	(18,750)
Debt Service on Subordinated Bonds ⁵	<u>131,127</u>	<u>139,834</u>	<u>146,893</u>	<u>177,772</u>	<u>183,584</u>	<u>191,861</u>
Amount Available After Operations and Debt Service	\$7,313	\$12,217	\$13,895	\$15,652	\$17,548	\$17,537
Fund Deposits						
CORE Fund	\$ 0	\$ 0	\$679	\$1,434	\$2,331	\$1,318
Reserve Funds	3,119	4,596	1,117	990	1,084	1,337
Construction Fund	7,820	13,200	14,700	16,300	17,400	18,400
Commonwealth Obligations	23,461	23,908	24,365	24,834	27,148	27,686
Bond Early Redemption Account	0	0	0	0	0	0

¹ Totals may not add due to rounding.

² Excludes depreciation.

³ Assumes issuance of several series of additional Bonds. See Appendix B.

⁴ Fiscal Years 2007 through 2012 each include \$18.75 million of anticipated state debt service assistance; there can be no assurance that the Authority will receive such amounts. See "Legislative and Other Developments" and Appendix B.

⁵ Debt service on current and projected SRF Bonds and other Subordinated Bonds. See Appendix B.

THE SYSTEMS

THE WATERWORKS SYSTEM

History. Boston and surrounding communities have one of the oldest public water supply systems in the United States, dating to 1652 when the "Water Works Company" was incorporated to construct Boston's first waterworks facility. Facilities were added over the years to meet increasing demand, and by the mid-1800s, a large scale water supply system utilizing cast iron pipes from a series of area reservoirs had been fully developed. In 1895, after a major study of the existing Boston metropolitan water supply and demand forecasts, work was begun on a major expansion project, the Wachusett Reservoir and Aqueduct. Construction of the Wachusett Reservoir, finished in 1908, more than doubled the System's yield. In 1919, after the state legislature commissioned a second major water supply study, planning was begun for the Quabbin Reservoir. Construction of the Quabbin Reservoir, completed in 1939 and filled to capacity by 1946, represented the last major expansion of the System's water supply, increasing the reservoirs'

total storage capacity from 78 billion gallons to approximately 490 billion gallons, and the watershed area from approximately 185 square miles to approximately 467 square miles.

Water Supply. The right to use, improve and manage the Waterworks System was granted to the Authority by the Act. The Act also granted to the Authority the exclusive right to utilize for water supply purposes all of the water from the existing DCR Watershed System as may be safely yielded. The safe yield is defined to be the average quantity of water that can be supplied on a continuous basis through a drought period. Under present operating rules the Authority's water sources can supply a safe yield of approximately 300 million gallons per day ("mgd"). The Authority's statutory right to utilize water derived from the DCR Watershed System includes the delivery, distribution and sale of water and the receipt by the Authority of revenues from charges relating to such delivery, distribution and sale.

The Act establishes responsibility for management of the Watershed System by the MDC which is now the Department of Conservation and Recreation ("DCR"). DCR continues to have the mandate to construct, maintain and operate a system of watersheds, reservoirs, water rights and rights in sources of water supply, and to supply a sufficient supply of pure water to the Authority. Other DCR responsibilities include forestry and wildlife management; conservation of water, land and other natural resources; preservation of the environment; operation of a visitor's center at the Quabbin Reservoir; and regulation of hydroelectric generation.

The Authority is required by statute to pay to the Commonwealth a charge for the costs of the DCR's Division of Water Supply Protection. Such costs include the cost of debt service on certain bonds that were issued by the Commonwealth to finance the acquisition of development rights or other interests in land within the Division's watershed. In July 2004, legislation was passed creating a Watershed Supply Pilot Program to be administered by and through a separate trust called the "Water Supply Protection Trust." A Board of Trustees was established to approve an annual budget developed by the Authority and DCR and a separate trust account was established for the receipt of revenues (including the Authority's contribution) and expenditures pursuant to the approved budget. Originally scheduled to expire in January 2007, the Water Supply Protection Trust was extended by legislation until January 2009.

The present major sources of water to the Waterworks System are the watersheds of the Quabbin Reservoir, the Ware River and the Wachusett Reservoir. Other standby sources include the Sudbury Reservoir and the Framingham Reservoir No. 3. The Quabbin Reservoir, located approximately 65 miles west of Boston, is one of the largest reservoirs in the world built exclusively for water supply purposes, covering 39 square miles with a capacity of 412 billion gallons. Water for the Quabbin Reservoir is derived from the impounded Swift River, a tributary of the Connecticut River, with a runoff from 186 square miles of watershed. In addition, a limited quantity of the runoff from 98 square miles of the Ware River watershed is diverted to the Quabbin Reservoir.

The Wachusett Reservoir is located in central Massachusetts, approximately 35 miles west of Boston. The Wachusett Reservoir has a capacity of 65 billion gallons and covers 6.5 square miles. The Sudbury Reservoir, in the Sudbury River watershed, has a 8.4 billion gallon capacity and surface area of two square miles. Framingham Reservoir No. 3, also in the Sudbury River watershed, has a capacity of 1.2 billion gallons and an area of approximately one half of a square mile. The Sudbury and Framingham Reservoirs are currently maintained off-line for emergency use only.

In close conjunction with the Authority, the DCR has developed and implemented Watershed Protection Plans for the Quabbin, Wachusett and Ware watershed areas to protect water quality in the reservoirs. Components of this program include an on-going land acquisition program funded by the Authority targeting critical lands over 15 years, a recently completed \$85 million sewer project to improve tributary water quality, public access controls around the reservoir, state regulations on development in critical areas along tributaries, and a substantial water quality monitoring and research program. The FY07 CIP includes \$19 million for watershed land acquisition, including \$8 million budgeted to be spent in Fiscal Year 2007. The Authority and the DCR closely coordinate watershed protection, reservoir operations, and water quality monitoring efforts between the two agencies. An updated five-year protection program for the Wachusett watershed, covering the 2005-2009 period, was approved by DEP in 2004. The plan focuses on continuing protection efforts to minimize the level of pathogens entering the reservoir.

Water Transmission and Distribution. Because of the variety of local conditions and elevations, six water pressure zones are required for the Authority's waterworks service area. These six zones are supplied through tunnels and aqueducts from the two active source water reservoirs and water is distributed through pumping and major

transmission and storage facilities, all of which are owned and maintained by the Authority. Major system components include approximately 350 miles of aqueducts, tunnels and mains, eleven active distribution storage reservoirs and standpipes, ten active pumping stations, and two active hydro-electric power stations.

Water from the Quabbin Reservoir, which has an elevation 530 feet above the base elevation of Boston, is delivered to the Wachusett Reservoir by the Quabbin Aqueduct, a 24.6-mile tunnel. From the Wachusett Reservoir, water is delivered through the eight-mile Cosgrove Tunnel, built in the 1960s, and the Wachusett Aqueduct, first used in 1898, to the Hultman Aqueduct intake structure in Marlborough and to the Weston Reservoir via the Weston Aqueduct. The Hultman Aqueduct, in service since the 1940s, connects with the Cosgrove Tunnel and continues the delivery of water 17.8 miles into the Boston area. Water from the Wachusett Reservoir and the back-up Sudbury Reservoir can be delivered in an emergency through the 17.5-mile Sudbury Aqueduct, built in 1878, to the Chestnut Hill Reservoir which is now off-line.

The Hultman Aqueduct is a major component in the water distribution system. In the past the lack of redundancy for the Hultman Aqueduct meant that a significant failure would have resulted in the inability to deliver water in sufficient volume to meet the needs of Authority customers and could have seriously disrupted residential life and ordinary commerce in the service area while repairs were made. In order to provide an appropriate level of redundancy, the Authority constructed and placed in service in November 2003 the 17.6-mile MetroWest Water Supply Tunnel. The tunnel provides full redundancy for the Hultman Aqueduct during either maintenance or emergency situations and is an integral component in the design and engineering of the Authority's proposed capital program to improve the reliability and quality of its water supply services discussed below. In addition to the redundancy offered by the MetroWest Water Supply Tunnel, the Authority has a contingency plan to expedite repairs and provide emergency water services to the best of its water supply capabilities in the event of a failure of the Hultman Aqueduct. See "Capital Improvement Program – Major Capital Projects – Waterworks Projects."

The major links of the water supply distribution system in the Boston area are the Authority's 5.4-mile City Tunnel, a 7.1 mile City Tunnel Extension serving communities north of Boston, and the Dorchester Tunnel, a 6.4-mile tunnel providing distribution to communities south of Boston. The Authority provides water supply to each Local Body through one or more metered connections and through certain non-metered connections which are used on an emergency basis only. Less than 5% of monthly water consumption is estimated, rather than metered, due to the necessary use of an emergency connection or to a faulty meter or other system malfunction. The water distribution system has a total of 185 metered connections and approximately 70 non-metered emergency connections. The Authority is responsible for the maintenance of the water distribution system to and including the metered connection or, in the case of an emergency connection, the emergency valve. Local communities served by the Authority distribute water to their retail customers through approximately 6,000 miles of community-maintained water pipelines.

Water Quality. The Authority has substantially completed measures to ensure both the level and consistency of water quality throughout the Waterworks System through a ten-year Integrated Water Supply Improvement Program (1995-2005), that consists of comprehensive watershed protection, construction of covered storage, modern treatment facilities to meet current engineering and regulatory standards, and improvements to the distribution system. See "Capital Improvement Program – Major Capital Projects – Waterworks Projects."

The Authority has received a waiver from DEP of filtration requirements for water supplied from Wachusett Reservoir to the metropolitan Boston area. To meet the waiver requirements and to comply with the applicable SDWA regulations, the Authority constructed and placed into service in July 2005 the new John J. Carroll Water Treatment Plant (previously referred to as the Walnut Hill Water Treatment Plant) in Marlborough. The John J. Carroll Water Treatment Plant meets all current SDWA requirements. Disinfection byproducts are down over 80% while the plan meets stringent giardella standards. Because existing uncovered distribution reservoirs are vulnerable to airborne contaminants and allow the growth of bacteria, plants and algae, the Authority has eliminated the use of open distribution reservoirs by constructing covered storage facilities.

These projects, which have been completed, replaced active distribution storage of approximately 2.4 billion gallons of open reservoirs with more than 200 million gallons of covered storage downstream of the John J. Carroll Water Treatment Plant.

The Authority has received a conditional waiver from DEP of filtration requirements for water supplied to three communities in western Massachusetts by the Chicopee Valley Aqueduct from the Ware River/Quabbin Reservoir supply system. To meet the waiver conditions and improve disinfection and corrosion control to assure water quality and SDWA compliance, the Authority constructed a disinfection facility at Ware, and two 12.5 million gallon concrete water storage tanks to replace the open Nash Hill Reservoir. See “Environmental Regulation and Litigation – Water Supply – Drinking Water Regulation.”

In addition, the Authority also is expanding financial and technical assistance to member communities for rehabilitation of local water systems. Beginning in 1997, the Authority established a \$30 million Local Water Infrastructure Rehabilitation Assistance Program which provided grant and loan packages (a combined 25% grant and 75% interest-free loan) to eligible water communities to replace, rehabilitate, and maintain components of their waterworks systems. Through this two-year revolving fund program which covered Fiscal Years 1997 to 1999, the Authority distributed financial assistance for water distribution system improvements to 42 communities. Effective July 1, 2000, the Authority implemented a longer-term program that provides for \$25 million per year in ten-year interest free loans to assist member communities with pipeline rehabilitation. As of December 1, 2006, loans totaling \$118.6 million have been approved.

The Authority also is working with state and local officials to increase awareness of water quality issues affecting the water distribution systems operated by the Authority and the Local Bodies. In addition, the Authority continues to work in collaboration with Local Bodies to deal with local water quality problems as they arise.

Water Demand. At the time the Authority assumed responsibility for the Waterworks System in 1985, the average daily withdrawal of water from the system had exceeded the safe yield of 300 mgd in each year since 1969, and a long-range water supply study, begun in 1980, was underway to assess the options for addressing projected shortfalls. To address the problem, the Authority established more than 20 related programs for detecting and repairing leaks, encouraging conservation and reduced water use, preserving and developing local supply sources, and implementing a drought response plan. In large part as a result of the Authority’s programs, water use declined steadily from 1987 to 1996, and since 1989 average daily withdrawals have been well within the safe yield. In the opinion of the Authority, barring a drought more severe than any on record and assuming continuing conservation efforts and proper maintenance of the transmission and distribution system, the Authority’s existing supplies will be more than sufficient for its water supply needs through at least the year 2020. The Authority currently has no plans to develop any new sources of water. For a description of certain of the environmental and regulatory constraints involved in the process of augmenting the Authority’s water supply, see “Environmental Regulation and Litigation – Water Supply – Expansion of Water Supplies.”

Extension and Contraction of Waterworks Service Area. Under the Act, the Authority may extend the Waterworks System to additional communities not currently served on such reasonable terms as the Authority may determine. Such an extension of service requires that the Authority first make certain findings similar to those required to be made in connection with the continuation of water supply services to communities currently served under special acts or contracts. See “Local Bodies – Special Arrangements.” Any extension of the Waterworks System is subject to the approval of the Governor, the state legislature, the Advisory Board, and the regulatory bodies within the Commonwealth’s Executive Office of Environmental Affairs (“EOEA”) having jurisdiction. Extension of the Waterworks System to any community not currently served by the Authority also requires the approval by majority vote of its city council or town meeting, as the case may be. The Authority also is authorized to enter into arrangements not involving an extension of the Waterworks System to provide water supply services to any community or any agency or facility of the Commonwealth or the United States not currently served, provided (i) no such arrangement shall extend for a period greater than six months without the approval of the Advisory Board and (ii) the Authority finds that the arrangement will not jeopardize its ability to service its existing statutory and contractual supply agreements. In cases of water supply emergency, as determined by DEP, the Authority may approve a connection to an adjoining community.

The Authority is aware that certain other communities are considering requesting admission to the Waterworks System’s service area in order to receive supplemental water from the Authority for seasonal, occasional, or emergency use of water from the Waterworks System. The Authority does not expect that admission to the service area of any of these communities would result in a substantial increase in the use of water.

The Authority has adopted a policy for the review of requests for water supply which requires a community requesting admission to the Waterworks System to pay an entrance fee for its proportional share of historic investments in the system, a connection fee to cover all costs associated with establishing a connection to the Waterworks System, and the prevailing water rate for all annual water consumption. The policy further requires a community that requests a temporary connection to the Waterworks System to pay a cost per million gallons which includes the prevailing water rate, a proportional asset value contribution, and, in certain recurring cases, a surcharge on the then-prevailing water rate (as well as the asset value contribution), of up to 10%. Should such a community ultimately seek admission to the Waterworks System, any asset value contribution would be credited to its entrance fee, but the surcharge would be non-refundable and would not be credited to other costs.

A Local Body specified in the Act as eligible for receiving water supply services could seek to withdraw from the Waterworks System by state legislative action or with the Authority's approval. However, in the opinion of the Authority and its Consulting Engineer, the cost and time required to implement adequate alternative water supply sources in accordance with existing and anticipated state and federal environmental laws and regulations generally would preclude this course of action as a practical matter for any substantial portion of the Waterworks System's service area.

THE SEWER SYSTEM

History. The Authority's existing wastewater facilities include certain components constructed as early as 1884, when the Boston Main Drainage System was originally placed in operation. At that time, combined sewage was pumped by a pump station constructed in 1884 to Moon Island in Boston Harbor, where sewage was held in storage tanks before being released on the outgoing tides. In 1898, the Neponset Valley Sewer System was completed, with flows sent to Moon Island through the Boston Main Drainage System. Also in 1898, a pump station was constructed on Deer Island in Boston Harbor to pump sewage from the metropolitan area north of Boston to Deer Island, where it was held in storage tanks before being released on the outgoing tides. In 1904, the original South Sewerage System was completed, conveying flow from the Charles River Watershed, the Neponset River Watershed and areas south of the Boston Main Drainage System. After screening at Nut Island, flows from the South Sewerage System were discharged into Boston Harbor. Some flow from the Boston Main Drainage System also was redirected to Nut Island. In response to concerns about water pollution, a primary wastewater treatment plant was constructed on Nut Island in 1952 to treat the discharge from the South Sewerage System and, in 1968, a second primary wastewater treatment plant at Deer Island was completed and flow from the Boston Main Drainage System began to be diverted to Deer Island.

Wastewater Collection. The 43 communities within the Authority's sewer service area own and operate approximately 5,400 miles of local sewers which connect to the Authority's approximately 240 miles of large interceptor sewers located to parallel the natural drainage patterns of the Mystic, Charles and Neponset River Watersheds. Approximately one-third of the sewage treated by the Authority originates in the BWSC's wastewater conveyance system. The Authority operates and maintains the wastewater transport and treatment system, including the interceptor sewer, 11 pumping stations, five headworks, five CSO facilities and the treatment plants at Deer Island and Clinton. The Local Bodies' sewer collection systems, some of which are combined sanitary and storm sewers, connect to the Authority's wastewater transport system through more than 1,800 connections.

The Sewer System is divided into a northern system and southern system. The northern system serves 26 communities with a total population of approximately 1.3 million, of which all but 40,000 contribute to the Sewer System. The four pumping stations in the northern system serve to pump wastewater into interceptors which carry the wastewater to four headworks where large debris is screened out and grit is removed. From the headworks, the wastewater flows down vertical shafts into one of two deep rock tunnels 300 feet under Boston Harbor, through which the wastewater is carried to Deer Island. Flow also is conveyed to Deer Island by means of a 10-foot diameter interceptor through Winthrop. At Deer Island a large pumping station, substantially rehabilitated in 1995, lifts the flow from the tunnels into the treatment plant.

The southern system serves communities with a total population of approximately 775,000, of which 700,000 contribute to the Sewer System. The wastewater is pumped by seven pumping stations into interceptors which carry the wastewater to the High Level Sewer and ultimately to the Nut Island Headworks. At Nut Island, the headworks facility removes grit and screenings before the flow enters the Inter-Island Tunnel for transport to Deer Island, where it is lifted by pumps at the South System Pump Station to the treatment plant.

Wastewater Treatment. The Deer Island Treatment Plant includes, at Deer Island, pumping, headworks, odor control, disinfection, primary and secondary treatment and residual facilities and utilities (including a hydropower plant), a 4.8-mile deep rock inter-island tunnel that brings south system flows from Nut Island to Deer Island for treatment, a 9.5-mile deep rock outfall tunnel that carries treated effluent from Deer Island to Massachusetts Bay. Primary treatment design capacity at the Deer Island Treatment Plant allows for an average daily flow of approximately 361 mgd and a peak hourly flow of 1,270 mgd. Since February 1996, following startup of the new primary treatment facilities at Deer Island, the Authority has consistently been in compliance with the discharge limitations specified in its National Pollutant Discharge Elimination System (“NPDES”) permit issued under the Clean Water Act. Effluent wastewater is disinfected and discharged into Massachusetts Bay through a series of diffusers located at the end of the 9.5 mile effluent outfall tunnel. The maximum discharge capacity of the effluent outfall tunnel is 1,270 mgd. Sludge resulting from the treatment process is anaerobically digested and then piped to and processed at the dewatering and pelletization facility located at the Fore River Shipyard in Quincy. See “Residuals Management,” below.

The Authority’s Toxics Reduction and Control (“TRAC”) Department administers a permitting and inspection effort that allows for control and limitation of the volume and type of industrial waste discharged into the Sewer System so that both sludge and effluent from the treatment plants meet applicable environmental standards. This program serves as the enforcement mechanism for federal, state and Authority wastewater discharge regulations. Through strict limitations and prohibitions, the TRAC program requires the control of pollutants at their sources through industrial process modifications, pretreatment of contaminated wastewater, measurements and sampling of wastes, certification of industrial waste treatment operators and strict management controls. TRAC also is initiating programs to minimize the discharge of toxic pollutants at the source.

The Authority’s sewer use regulations, which give the Authority the ability to assess civil and financial penalties directly against violators of its regulations and permits, have been coupled with vigorous enforcement measures. Through December 1, 2006, the Authority has assessed penalties against industrial dischargers to its Sewer System in an aggregate amount of approximately \$10.1 million. In many instances, following a penalty assessment, the Authority and the violator have entered into a settlement agreement which contains a payment schedule for the penalty. As of December 1, 2006, the Authority had collected approximately \$6.2 million in penalties.

Clinton. Legislation enacted in 1987 transferred the ownership of the wastewater treatment plant in Clinton to the Authority from the MDC. The plant serves an area adjoining the Wachusett Reservoir watershed lands in central Massachusetts made up of the towns of Clinton and Lancaster (served by the Lancaster Sewer District). The Authority constructed an advanced secondary treatment facility at Clinton with a design capacity for an average flow of 3 mgd. The new plant commenced operations in Fiscal Year 1992.

Residuals Management. The Authority operates sludge dewatering and pelletization facilities located on a portion of the site of the former Fore River Shipyard in Quincy, constructed as part of the Deer Island Project. Digested liquid sludge is piped to the site from Deer Island and is processed for use as fertilizer in agriculture, horticulture and turf management. Sludge cake or pellets that are not used as fertilizer are landfilled. The Authority has entered into a contract with New England Fertilizer Company (“NEFCo”) for both the operation and management of the plant and the disposition, through sale or otherwise, of the sludge. NEFCo also has a subcontract with a landfill operator for use in the event of emergencies. The current NEFCo contract expires in 2015.

The Authority maintains on an on-going basis an emergency preparedness plan that identifies out-of-state landfills which could be utilized in the event that New England Fertilizer Company is not able to dispose of the wastewater residuals. The Authority also has retained ownership of a site in Walpole to construct an in-state landfill in the event that capacity or other issues emerged with the other landfills.

Combined Sewer Overflows; Infiltration and Inflow. Many areas in Boston, Cambridge, Chelsea and Somerville are served by combined sewers, which are pipes that carry both sanitary flow and storm water runoff. These sewers, built for the most part prior to 1910, were designed to discharge CSOs into nearby waterways during heavy rainstorms to protect the system, as well as homes and businesses connected to it, from flooding. The Authority’s and communities’ interceptors, trunk sewers, and pumping systems serving the combined sewer areas are not capable of fully handling wet weather flows generated by large storm events. Combined flows in excess of the Sewer System’s capacity are currently diverted and discharged through overflow conduits into Boston Harbor, Dorchester Bay, Mystic River, Charles River Basin, and Alewife Brook. At many outfalls, overflow events result in the discharge of diluted, but

untreated, sewage, although the Authority operates facilities that provide screening and disinfection to the majority of CSO discharge volumes. These overflows are a source of pollution in Boston Harbor and its tributary rivers. Since 1987, the Authority's investments in the Sewer System have reduced the average annual volume of CSO discharges by approximately 76%, from 3.3 billion gallons to 0.8 billion gallons in a typical year. The Authority is designing and implementing remedial actions for CSOs in connection with the federal enforcement action brought against the Authority and others under the federal Clean Water Act (the "Clean Water Act Case"). See "Capital Improvement Program – Major Capital Projects – Wastewater Projects."

Further increasing the burden on the Sewer System are infiltration of groundwater into the Sewer System through leaks in pipes, joints and connections, and inflow of storm water from a number of sources into otherwise separate, local sewer systems ("infiltration and inflow"). The Authority has developed programs, including an Infiltration/Inflow Local Financial Assistance Program (a combined grant and interest-free loan program) that can provide more than \$180 million in funding for local sewer improvements, to encourage and assist efforts to reduce infiltration and inflow within the local collection systems of the Local Bodies. As of December 1, 2006, the Authority has entered into loan and grant agreements with 43 Local Bodies, representing \$138.6 million in loans and grants.

Extension and Contraction of Wastewater Service Area. The Act authorizes the Authority to provide sewer service for a limited term to any person within or outside its service area not currently connected to the Sewer System, provided any such arrangement does not entail an extension of the Sewer System or have a term in excess of six months (unless a longer term is approved by the Advisory Board). The Act authorizes the Authority to extend the Sewer System to additional local bodies, provided such extension is approved by the Governor, the state legislature, the Advisory Board and DEP. Extension of the Sewer System to any community not currently served by the Authority also requires the approval by majority vote of its city council or town meeting, as the case may be. Prior to extending the Sewer System to any new local body, the Authority must determine that (i) the safe capacity of the Sewer System as so extended will be sufficient to meet ordinary wet weather demand, (ii) all feasible measures have been taken by the local body to limit infiltration and inflow of surface and ground waters into the Sewer System, and (iii) the local body has adopted an industrial pretreatment program in accordance with applicable law. At the present time, the Authority does not anticipate adding any communities to the Sewer System.

Although a Local Body could withdraw from the Sewer System by state legislative action or with the Authority's approval, in the opinion of the Authority and its Consulting Engineer, existing and anticipated state and federal environmental laws and regulations would cause any alternative to the Authority's wastewater collection services for a Local Body to be prohibitively expensive as a practical matter since it would require the construction of new treatment facilities in accordance with state and federal environmental laws.

SECURITY

In response to the events of September 11, 2001, the Authority immediately took action to increase protection of potentially vulnerable water and wastewater facilities and sites. In November 2005, the Authority consolidated its security and emergency preparedness from three departments into one Office of Emergency Preparedness. The Office of Emergency Preparedness is designed to streamline the organizational structure to allow the Authority to act quickly and decisively across departments in the event of an emergency. The Director of Emergency Preparedness, in conjunction with a Task Force on Security and Emergency Preparedness comprising senior managers from all Authority disciplines, directs and coordinates critical infrastructure protection, security and emergency response efforts and emergency and contingency plans. The Authority has completed a Water Systems Terrorism Vulnerability Assessment (conducted in part by the U.S. Department of Energy's Sandia National Laboratories) and Emergency Response Plan, both mandated by the Bioterrorism Act of 2002. An Emergency Services Unit was established and funded through a Homeland Security grant to provide rapid response to incidents of water system contamination. This unit is being augmented with additional equipment through another grant to increase its ability to respond to incidents of contamination at the Authority's open storage reservoirs. The Authority is continuing its efforts to improve surveillance and physical security. The Authority's facilities are patrolled by the Massachusetts State Police, and a private security service provides additional protection at the Deer Island Treatment Plant, Chelsea and Charlestown facilities and the John J. Carroll Water Treatment Plant. Guards also monitor cameras, intrusion alarms, key card access and fire alarms for major waterworks facilities at a central security monitoring point in Chelsea.

CAPITAL IMPROVEMENT PROGRAM

CAPITAL IMPROVEMENT PLANNING

The Act requires the Authority to adopt and update capital facilities programs for the Systems and capital expense budgets to implement and finance such programs. In June 2003, the Board of Directors adopted a five-year capital spending cap that limits total expenditures for Fiscal Years 2004 through 2008 to \$1.13 billion. The cap policy requires that a new cap for Fiscal Years 2009 through 2013 be set by the Board before the end of the current cap period. The Authority annually prepares and updates its CIP, and in June 2006 the Board of Directors approved the FY07 CIP. The FY07 CIP includes spending for Fiscal Years 2004 through 2008, the current cap period, and projections through Fiscal Year 2016 and beyond. As a result of the Authority's ongoing efforts to manage rate increases to its member communities, while continuing to upgrade and maintain the Systems, the CIP adopted by the Authority for Fiscal Year 2006 (the "FY06 CIP") reflected a spending reduction of approximately \$420 million as compared to the CIP adopted for Fiscal Year 2005, but is equal to the spending level approved in Fiscal Year 2004. This reduction reflected a proposed shift forward of CSO spending and a reduction in infrastructure improvements to the System largely in Fiscal Years 2009 through 2013. The FY07 CIP, with the exception of three new CSO projects, comprises the same projects with the same relative priorities as the FY06 CIP. In December 2006, the Board approved the transmittal of the Proposed FY08 CIP to the Advisory Board, which recommends a spending cap for the five Fiscal Years 2009 through 2013 of \$1 billion. The Proposed FY08 CIP and the spending cap reflect the Authority's effort to align its project prioritization process with the Master Plan and the inclusion of new projects for the future years accordingly.

The CIP describes all capital projects ongoing at the time of its adoption and new projects to be initiated during a ten-year planning period. The costs shown for each project in the CIP include any payments made on such project prior to the commencement of the ten-year planning period, the expected costs for such project for each year of the CIP budget period, and the expected balance of such costs through completion of the project. Capital project spending is forecast annually over the ten-year planning period. The scope and anticipated cost of the projects included in the CIP are reviewed periodically during the course of the fiscal year by the Authority, and revised as necessary. In addition, the CIP has been updated and readopted on an annual basis and rolled forward for an additional year each time.

During the course of the fiscal year, the Authority's financial information system produces monthly statements of capital spending compared to the budget plan. The Authority reports on capital program progress in its monthly management indicators report and dollar variances in its monthly financial update. At mid-year and at year-end progress, project schedules and variances are summarized and reported.

SUMMARY OF CAPITAL INVESTMENT

The Authority has completed or substantially completed several major capital projects, including the Deer Island Project and the major components of its Integrated Water Supply Improvement Program. The results of the Authority's efforts to date are apparent in improvements to the environment as well as in better delivery of services. Significant steps taken in the environmental restoration of Boston Harbor include the end of sludge discharges into Boston Harbor in December 1991, the commencement of operations of the new primary treatment facilities at Deer Island in January 1995, the start-up of operations of the first, second and third batteries of the new secondary treatment facilities at Deer Island in July 1997, January 1998 and January 2001, respectively, the transfer of flows from the south portion of the Sewer System to Deer Island for treatment in July 1998 and the commencement of operation of the effluent outfall tunnel in September 2000. In addition, the final contract with respect to the Deer Island Project was declared substantially complete in November 2001. Together with the operation of CSO screening and disinfection facilities and improvements to the Sewer System and certain of the Local Bodies' local systems, reductions have been achieved in the frequency, volume and severity of CSOs with corresponding substantial reductions in the bacterial contamination to Boston Harbor. According to information developed by or available to the Authority, the Authority believes that measurements of bacterial contamination in Boston Harbor since 1990, on average, have been the lowest on record since the 1930s; most beaches have experienced fewer closings in recent summers; fish living in Boston Harbor are less contaminated and healthier; and the appearance of Boston Harbor has improved. The Authority also has completed several sewer interceptor projects, including projects at New Neponset, Wellesley and Framingham, which have further improved the performance of the Sewer System.

The Authority placed into service the MetroWest Water Supply Tunnel, a major component of its integrated water supply improvement program, in November 2003. This 17.6-mile long deep rock tunnel from Marlborough to Weston connects to the new John J. Carroll Water Treatment Plant at Walnut Hill, placed in service in July 2005, and

aqueducts from the Wachusett and Quabbin Reservoirs to the greater Boston area. The tunnel was completed on schedule and under its \$700 million budget.

In addition, the Authority has completed certain other capital projects within the Waterworks System, including a water meter modernization program, a domestic device retrofit program, a leak detection survey, a local source of supply analysis and protection program, and a long-range water supply study, which have enabled the Authority to eliminate the near-term prospect for very expensive and potentially controversial projects for large-scale water supply augmentation. The Authority has completed projects that have enhanced pumping and pipe capacity, including a pump station and storage tanks at the Spot Pond Reservoir.

MAJOR CAPITAL PROJECTS

Proposed Fiscal Year 2008 CIP

The Proposed FY08 CIP includes 99 ongoing and new projects. Total costs of the projects are \$4.7 billion in Fiscal Year 2008 dollars (“FY08 Dollars”), including contingency, of which \$2.5 billion has been spent through Fiscal Year 2006. The Proposed FY08 CIP projects spending, including contingency and inflation in FY08 Dollars, of \$944.8 million for Fiscal Years 2004-2008, \$970.0 million for Fiscal Years 2009-2013 and net projected spending of \$819.6 million for Fiscal Years 2014 and beyond.

Waterworks Projects

Capital projects for the Waterworks System are designed to upgrade and extend the useful life of the water supply, transmission and distribution system in order to assure a satisfactory and consistent level of water quality and distribution throughout the Waterworks System. Certain of these projects also are mandated by federal regulatory requirements. The total estimated expenditures for the Waterworks projects for Fiscal Years 2004 through 2008, as contained in the Proposed FY08 CIP, are approximately \$353 million. Approximately \$415.2 million in additional expenditures is forecast through Fiscal Year 2013, reflecting significant capital investment in the Waterworks System. The major projects in the program are summarized below.

Drinking Water Quality Improvements. The Authority continues to implement its Integrated Water Supply Improvement Program for drinking water improvement. This program consists of aggressive watershed protection, modernized treatment facilities, and distribution system improvements including construction of covered storage facilities and pipeline rehabilitation. This program is based on current engineering practices, up-to-date technology and drinking water standards resulting from state and federal laws. See “Environmental Regulation and Litigation – Water Supply.” Pursuant to an administrative consent order entered into with DEP and DCR with respect to the enforcement of the SDWA and the rules promulgated thereunder, the Authority constructed the John J. Carroll Water Treatment Plant. The plant treats water delivered from the Wachusett Reservoir (including water transferred to the Wachusett Reservoir from the Quabbin Reservoir) through ozonation and chloramination. Construction of the treatment plant began in November 2000 and the facility went on line in July 2005. The John J. Carroll Water Treatment Plant is able to treat 405 mgd of drinking water.

Total estimated costs of the projects in the Proposed FY08 CIP related to drinking water quality improvement projects are approximately \$640.1 million, of which \$453.4 million is for water treatment, and \$186.7 million is for covered storage facilities and watershed protection. Approximately \$490.2 million was expended through Fiscal Year 2006 for these projects.

Transmission. Critical needs of the Authority’s aqueduct system include correction of structural conditions to reduce leakage and provision of redundancy for critical sections of the transmission system, such as the Hultman Aqueduct and the Southborough Tunnel, where transmission has depended on a single conduit. The estimated costs for transmission projects included in the Proposed FY08 CIP total \$972.7 million, of which approximately \$644.2 million was expended through Fiscal Year 2006.

The most significant of the Authority’s transmission projects is the construction of the MetroWest Water Supply Tunnel, a 17.6-mile long, 14-foot diameter deep rock tunnel running from Marlborough to Weston. The

MetroWest Water Supply Tunnel is critical to provide an appropriate level of transmission redundancy and is a key element of the planning, design, and operation of the John J. Carroll Water Treatment Plant and covered distribution storage project described above. Construction of the tunnel was completed in November 2003.

Distribution and Pumping. The Proposed FY08 CIP identifies 23 separate projects for rehabilitation, upgrade or new construction of pipelines, pumping facilities, valves and meters. These projects total approximately \$629.1 million, of which approximately \$262.6 million was expended through Fiscal Year 2006. Pursuant to the Authority's business plan, over the next 30 years, approximately 200 miles of unlined pipe will be rehabilitated or replaced at a rate of approximately seven miles of pipe each year. These projects will provide improved reliability and safety of water delivery.

Other Waterworks Projects. These projects include expansion of the Waterworks System's central monitoring system, various system rehabilitation projects and two local community waterworks assistance programs. The total cost of these projects as contained in the Proposed FY08 CIP is approximately \$30 million.

Wastewater Projects

Combined Sewer Overflows. Discharges of combined wastewater and stormwater runoff from 63 remaining CSO outfalls in the Authority's system and four of the service area community systems (Boston, Cambridge, Chelsea and Somerville) can impact water quality in Boston Harbor, Dorchester Bay, the Charles and Mystic Rivers and Alewife Brook. Pursuant to a 1987 stipulation entered in the Clean Water Act Case, the Authority has responsibility for developing and implementing a long-term plan for CSO control at all locations. The Authority first proposed the current long-term plan in its CSO Conceptual Plan and Sewer System Master Plan (the "CSO Conceptual Plan") in 1994. The CSO Conceptual Plan incorporated then-current information about the volume of CSO flows and water quality impacts, and was developed in accordance with the U.S. Environmental Protection Agency's ("EPA") National CSO Policy (April 1994).

In 1997, the Authority completed its CSO Facilities Plan based on the CSO Conceptual Plan. The CSO Facilities Plan comprised 26 site-specific projects, including such measures as sewer separation, interceptor improvements, upgrades of existing CSO treatment facilities, new CSO facilities and storage. Since 1997, several projects have changed, although the project locations and site-specific CSO control goals have not changed significantly. In 2004 and 2005, respectively, the Authority added the Morrissey Boulevard Storm Drain project to its new plan for controlling CSO and stormwater discharges to the South Boston beaches and a Charles River CSO Controls project that involves a set of sewer separation projects and system optimization measures to further reduce CSO discharges to the Charles River, including at the Authority's Cottage Farm CSO treatment facility.

In April 2006, the Federal District Court approved a joint motion filed by the DOJ and the Authority which reflected changes to the Authority's CSO Control Plan agreed to by EPA, DEP and the Authority on the appropriate level of CSO control and recommended plans for the Charles River, the Alewife Brook/Upper Mystic River, and East Boston and on its overall CSO Control Plan. With this agreement, the Authority now has an approved CSO Control Plan for all receiving waters, which includes 35 projects. The Federal District Court subsequently issued Schedule Seven in the court order for the Clean Water Act Case ("Schedule Seven"), which includes additional milestones related to this comprehensive agreement. Schedule Seven incorporates all the current milestones including directing the design and construction of these additional projects. With this agreement the Authority now has an approved CSO Control Plan for all receiving waters where CSO outfalls connected to its system discharge through 2020. The Authority's Proposed FY08 CIP includes \$803.5 million for the planning, design and construction costs of the CSO projects.

Sixteen of the 35 projects contained in the Authority's CSO Control Plan are complete, and eight additional projects are in construction. In July 2006, the Authority awarded the first of two construction contracts comprising the North Dorchester Bay CSO Storage Tunnel and Related Facilities. This contract, valued at \$145.7 million, is the single largest component of the Authority's CSO Control Plan and involves constructing a 2.1-mile soft-ground tunnel to capture CSO and stormwater flows which currently discharge along the swimming beaches of South Boston. Of the remaining 11 projects, seven are in design. Design of the final four projects will commence in accordance with the milestones in Schedule Seven.

Interceptor Sewers and Pumping. The Authority is undertaking, and in some cases has completed, several major projects to extend, enlarge and rehabilitate large sewer interceptors. These projects are necessitated by the age of the systems and their inadequate capacity to serve existing or projected populations. As they are completed, the new facilities alleviate sewer surcharging and overflow problems. The interceptor sewer and pumping projects total approximately \$676.7 million, of which approximately \$429.1 million was expended through Fiscal Year 2006. The most significant project is the Braintree-Weymouth Relief Facilities project, which includes a deep rock tunnel, two new pump stations, new interceptors and siphon river crossings. The tunnel is complete and overall the project is 94% complete as of December 1, 2006. The major portion of the project, which provides the required hydraulic relief, was completed in Fiscal Year 2005, providing capacity for peak flows from Braintree, Hingham, Holbrook, Randolph, Weymouth and sections of Quincy. The final portion of the project, replacement of the existing Braintree-Weymouth Pump Station, is expected to be completed in Fiscal Year 2008.

Treatment and Residuals. At the Deer Island Treatment Plant, plant staff have assumed responsibility for maintenance and ongoing capital improvements. The Proposed FY08 CIP includes \$631.4 million for these improvements, including \$348.3 million for equipment and system replacement and upgrades over the next ten years through the Deer Island Treatment Plant Asset Protection project and \$148.3 million for the Residuals Asset Protection project. The \$348.3 million amount is an estimate that is refined annually, as additional operational and maintenance information becomes available. As part of the Proposed FY08 CIP, Residuals Asset Protection was added as a new project. This project consists of 13 individual contracts to maintain and improve the operations and infrastructure of the residual plant. Planned spending includes \$0.5 million in Fiscal Year 2008, \$6.5 million in the Fiscal Year 2009-2013 period and the balance of \$141.3 million in Fiscal Year 2014 and beyond.

Business and Operations Support and Contingency

Business and Operations Support. Business and operations support projects are generally directed to improvement of the Authority's centralized services. The Proposed FY08 CIP includes funds for leasehold improvements to the new Chelsea facility, which houses personnel and equipment servicing the metropolitan Boston portion of the Systems. Total capital costs for this project are estimated at \$10.2 million, of which \$9.9 million has been expended. The FY07 CIP also includes funds for technical assistance contracts and for the upgrade of the Authority's Management Information Systems to meet the changing needs of planning and managing the Systems to respond to new regulatory requirements. Security improvements to protect Authority facilities are also funded through business and operations support. Total business and operations support costs in the Proposed FY08 CIP are approximately \$68.1 million.

Contingencies. The Proposed FY08 CIP provides for contingencies for the ten-year period in the amount of approximately \$156.2 million. The contingency is established as a percentage of the expected capital expenditure cash outlays in each of the fiscal years: 15% for tunnel construction for the North Dorchester Bay CSO Tunnel project, and approximately 10% for all other projects. According to the Consulting Engineer, these contingency levels are prudent and well proportioned and properly recognize that many large scale construction projects are now underway that have potential for significant cost changes due to unanticipated circumstances.

FACTORS AFFECTING THE CAPITAL PROJECTS

The following is not intended as a complete summary, but describes some of the uncertainties which may affect the Authority's capital programs. Unforeseen circumstances affecting the projects may result in delays or cost escalations not currently provided for in the Authority's projections.

The Authority must complete its capital projects in a complex legal and political environment. For example, performing large and complicated projects under court-ordered and administrative deadlines has required special coordination among engineering, legal, and regulatory activities. Many of the Authority's projects also involve impacts on surrounding communities and important concerns for environmental mitigation. Political sensitivities arising in these community contexts cannot be fully foreseen. Another consideration is the highly regulated public construction process in Massachusetts. A further important concern is the complexity of applying for and processing environmental construction and occupancy permits required for facility construction and operation. Many aspects of the permitting process require the assistance and cooperation of other federal, state and local governmental agencies. If the Authority's

permit needs are not expeditiously handled by these other federal, state and local governmental agencies, critical project delays may result.

The scope and complexity of many of the Authority's capital projects makes the timetable and expenditure forecasts for the CIP subject to change. Such factors as future environmental mandates, as well as traditional construction risks such as unknown site conditions could alter the Authority's forecasts. In preparing estimates of future revenue requirements for the CIP, the Authority has included inflation assumptions for the purposes of projecting the level of project expenditures when expected to be made or contracted for in accordance with each project's cash flow projections. Actual future inflation rates which are lower than the assumed rate could permit the Authority to proceed with portions of the CIP at costs lower than those used in developing its current revenue requirements projections. Actual future inflation rates higher than the assumed rate would require upward adjustment of construction cost and revenue requirement projections.

SOURCES AND USES OF CAPITAL FUNDS

The Authority expects to finance its capital expenditures principally from the proceeds of revenue bonds issued under the General Resolution. Certain capital improvements are eligible for federal grants and loans under the Clean Water Act and the Authority expects that certain waterworks projects will be eligible for loans under the SDWA's revolving fund program. The Authority also plans a gradual increase in the use of current revenues to fund certain capital projects.

ENVIRONMENTAL REGULATION AND LITIGATION

The Authority's Waterworks System and Sewer System are subject to significant regulation under federal and state environmental laws.

WATER SUPPLY

In the maintenance and expansion of water supply, the Authority is subject to environmental and regulatory oversight chiefly in the following respects:

Drinking Water Regulation. Under the SDWA, amended in 1986 and reauthorized and amended in 1996, EPA regulates the level of contaminants allowed in drinking water of most water supply systems in the United States by establishing national drinking water standards so that drinking water will be protected against microbiological or chemical contaminants. Standards include maximum levels for contaminants or treatment techniques and other performance standards. Enforcement of drinking water standards in Massachusetts under the SDWA has been delegated to DEP which also acts under authority of state law and has adopted Massachusetts Drinking Water Standards. The state and federal rules implementing the 1986 amendments to the SDWA impose additional treatment requirements for surface water sources, including criteria, procedures and timetables for state determinations of whether filtration measures are required, maximum permissible levels of coliform bacteria occurrence in distribution systems, and the testing and control of lead and copper in water at the customers' taps.

When the SDWA was amended and reauthorized in 1996, the water quality standard setting process was revised, a revolving loan fund for drinking water projects was established, water suppliers were required to issue consumer confidence reports and a timetable was established for further regulation of microbial pathogens in drinking water and potentially harmful disinfection by-products. As part of such further regulation, the first set of rules, the Interim Enhanced Surface Water Treatment Rule ("ESWTR") and Stage 1 Disinfectants and Disinfection By-products Rule ("DBPR") were issued in December 1998, and became effective in November 2001. These rules specify further treatment requirements for filtered systems to protect against pathogens and revise the maximum contaminant levels for potentially harmful disinfection by-products.

Between June 1993 and October 2005, the Authority worked under an administrative consent order entered into with MDC and DEP to comply with the SDWA's 1989 Surface Water Treatment Rule ("SWTR") and other rules under the 1986 amendments which included obligations to construct a new water treatment plant and covered storage to replace

Norumbega Reservoir. The Authority reported quarterly to DEP in accordance with the administrative consent order. The order also required the Authority to eliminate uncovered distribution storage at Weston Reservoir, Spot Pond and Fells Reservoir. The Authority has eliminated all uncovered distribution storage. Based on an annual review, DEP continues to find that the Authority's water supply meets federal criteria for unfiltered sources.

In 1992, DEP issued a conditional waiver of filtration for the Quabbin Reservoir, which directly serves three Local Bodies located in western Massachusetts. The conditions of the waiver required the Authority to develop a schedule for selecting and implementing a treatment technology to achieve current drinking water standards for the water provided to the three Local Bodies and for providing covered storage of the Nash Hill Reservoir. The Authority has completed the construction of covered storage facilities at Nash Hill and a primary disinfection facility at Ware. The Authority has established a separate water rate to recover the costs of constructing and operating these facilities. See "Local Bodies – Special Arrangements."

The John J. Carroll Water Treatment Plant and the Ware facilities comply with the ESWTR and DBPR. Future regulations issued in draft form in August 2003, and finalized in January 2006, have imposed additional requirements. A staged compliance schedule for capital improvements ending in 2014 is planned. The Authority believes that the treatment processes at the John J. Carroll Water Treatment Plant and the Ware facilities can be modified by the addition of ultraviolet light disinfection to meet the anticipated new regulatory requirements. All expected necessary additions and modifications to the water treatment plants for the Quabbin and Wachusett Reservoirs are included in the Proposed FY08 CIP.

Under the Lead and Copper Rule, the Authority is required to conduct sampling in conjunction with the Local Bodies to detect the presence of lead in their customers' tap water. In 2002, the samples collected by the Local Bodies were below the action levels set by the rule. As a result of the sampling in September 2003, it was determined that the Authority's water system exceeded the lead action level. This triggered a series of required actions under the Lead and Copper Rule, including conducting a public education program and the implementation of a lead service replacement program which exceeded the action level locally. These programs are underway. Results of five rounds of sampling in 2004, 2005 and 2006 were below the lead action level, as they have been in eight of the most recent ten rounds. The Authority's system continues to be in compliance with all requirements of the Lead and Copper Rule. Certain individual communities with higher local sample results also have independent public education and lead service line replacement program requirements from DEP.

Water Resources Management. Pursuant to the state Water Management Act (the "WM Act"), water users whose withdrawals from a particular ground or surface water source exceed 100,000 gallons per day must file a registration statement with DEP. In 1997, the Authority applied for and received a renewal of its registered withdrawals for each river basin from which its water is delivered through 2008.

Expansion of Water Supplies. In addition to the provisions of the WM Act, other state laws and regulations would govern any substantial structural augmentations to the Waterworks System's water supply. These include legislative approval for diversion of any river or stream for water supply purposes outside its own basin or for any structural action by the Authority in any water donor basin, including any capital improvement, which is expected to create a new interbasin transfer or increase the rate of any existing interbasin transfer. Approval by the state Water Resources Commission, an interagency policy management group within the EOE, is also required for any increase over the present rate of interbasin transfers of surface or groundwater. The Commonwealth's existing policies regarding water supply and management mandate that all economically feasible local sources of supply be developed before diversion of a major river source be considered. Environmental impact assessment and mitigation requirements under the Massachusetts Environmental Policy Act ("MEPA") and, in certain circumstances, the National Environmental Policy Act ("NEPA"), also must be met. The Authority does not foresee any circumstances requiring expansion or augmentation of the Authority's water supply.

WASTEWATER MANAGEMENT

Sewage Collection, Treatment and Disposal. The Clean Water Act imposes several permit and regulatory requirements on wastewater treatment systems. Public sewage treatment plant owners and operators such as the Authority are required to provide secondary treatment as established by federal regulation for all wastewater discharge from treatment plants into waters of the United States. Under the Clean Water Act, states also establish water quality standards classifying water body uses and pollutant control criteria to protect those uses. All sewage system discharges require NPDES permits specifying applicable technology based requirements, as well as any more stringent controls required to achieve the water quality standards established by the state pursuant to federal regulations. Under state law, the Commonwealth also requires treatment plants to hold state surface water discharge permits, which, in the discretion of EPA and DEP, may be issued jointly with the NPDES permit. Major wastewater treatment systems also must adopt and enforce pretreatment regulations for industries and other non-domestic sources discharging into sewers. Treatment plants are also subject to the Clean Water Act and state regulations governing sludge use and disposal.

The Clean Water Act is enforced by EPA and DEP through administrative orders and procedures. Violations also may be the basis for federal law suits brought on EPA's behalf by the DOJ or by private citizens. DOJ brought such an action against the Authority and others, referred to herein as the Clean Water Act Case, as described below.

Boston Harbor: NPDES Permit. The Authority operates its sewage system, including the Deer Island Treatment Plant and CSO outfalls, under a NPDES permit (the "Permit"), which became effective in August 2000. The Permit incorporates federal secondary treatment requirements, other technology based requirements, and other limits necessary for discharges to meet water quality standards established by the Commonwealth. The Permit includes extensive water quality monitoring, a contingency plan (the "Contingency Plan") to identify and respond to water quality changes that could potentially be related to effluent discharges from the new outfall, and numerous other requirements for pollution prevention, facility best management practices, management of infiltration/inflow, and restrictions on dry day flow.

The quality of wastewater effluent discharged from the treatment plant is continuously monitored by the Authority to assess compliance with water quality standards and pollutant limits set forth in the Permit. The Deer Island Treatment Plant generally operates reliably in compliance with the requirements of the Permit. Reliable compliance with water quality standards applicable to CSO discharges depends on completion of the CSO Facilities Plan. Because of the intermittent operation of CSO treatment facilities, and ongoing upgrades and improvements in the collection system, from time to time excursions from effluent limits applicable to treated CSO discharges under the Permit have occurred.

In September 2000, when the Authority placed the effluent outfall tunnel at Deer Island on-line, the Contingency Plan went into effect. The Contingency Plan and an Ambient Monitoring Plan are attached to the Permit. The Contingency Plan had been developed as a result of the Authority's agreement with the National Marine Fisheries Service ("NMFS") and EPA to implement certain recommendations regarding activities that will provide additional information to help to ensure that there are no adverse impacts to endangered species or critical habitats under NMFS jurisdiction. The Contingency Plan relies on data obtained through the Authority's extensive Ambient Monitoring Plan. Both the Contingency Plan and the Ambient Monitoring Plan are subject to recommendations made by an Outfall Monitoring Scientific Advisory Panel, advisory to EPA and DEP, and are to be reviewed annually and revised as necessary based upon information from the monitoring program and new scientific information.

The Authority submitted its renewal application for its NPDES Permit in February 2006. The current Permit expired in August 2005, but will remain in effect until the new Permit becomes final. EPA is currently working on a draft permit.

Boston Harbor: Clean Water Act Case. The Authority continues to be a defendant, along with BWSC and the Commonwealth, in the Clean Water Act Case, a consolidated lawsuit brought by the United States, acting at the request of EPA, and certain citizen groups, suing the Authority and other defendants for violations of NPDES permit conditions and certain terms of outstanding administrative orders previously issued by EPA. With the completion of the last battery of secondary treatment at the Deer Island Treatment Plant, the Court allowed the Authority's motion to reduce Court oversight, for the most part, to CSO related requirements under a CSO compliance schedule requiring the Authority to undertake CSO controls by specified dates, which has been modified from time to time as the CSO Control Plan has developed. See "Capital Improvement Program – Major Capital Projects – Wastewater Projects – Combined

Sewer Overflows.” In 1987, the Authority stipulated to accept responsibility to undertake corrective actions necessary to meet wastewater treatment discharge and CSO control requirements, with Court oversight. In April 2006, the 1987 stipulation was replaced with a new stipulation which limits the Authority’s responsibility and legal liability for CSO outfalls owned and operated by its four CSO communities following completion of the Authority’s long term CSO Control Plan. At that time, the Federal District Court allowed a joint motion of the DOJ and the Authority amending the Authority’s CSO Control Plan and adding new milestones for CSO control projects related to the Charles River, Alewife Brook/Upper Mystic River and East Boston. This motion was the result of a comprehensive agreement between the United States, DEP, and the Authority on the appropriate level of control for the Authority’s overall CSO Control Plan. With this agreement the Authority now has an approved CSO Control Plan for all receiving waters where CSO outfalls connected to its system discharge through 2020. In July 2006, the Federal District Court adopted Schedule Seven, which replaces Schedule Six and incorporates all of the additional milestones related to the comprehensive agreement.

Since 1988, no penalties have been assessed against the Authority and there are no pending requests for assessments of penalties against the Authority with respect to the Clean Water Act Case.

Related Litigation. The Authority’s activities as operator of the Sewer System, and in connection with the construction of the Deer Island Treatment Plant and related facilities, have given rise to several other lawsuits in federal and state courts. To date, none of these actions have led to a judicial determination adverse to the Authority or materially affecting the Authority’s programs or its ability to proceed in accordance with schedules mandated in the Clean Water Act Case. The Authority believes that actions of this nature may continue to arise from time to time and cannot predict the outcome of future proceedings, if any.

In April 1998, the Authority received a Notice of Enforcement Action from DEP regarding the Braintree-Weymouth Relief Facilities project. This project, now over 90% complete, provides increased capacity for transporting sewage flows from six communities south of Boston to remedy overflows that occur during wet weather. See “Major Capital Projects – Wastewater Projects – Interceptor Sewer and Pumping.” In February 1999, the Authority reached agreement with DEP on the terms of an administrative consent order which established a schedule for the project from 1999 to 2004 and required certain additional measures to manage and reduce overflows. In December 2004, the Authority commenced operation of the Intermediate Pump Station and is now providing the required relief to the Braintree-Weymouth Sewer System. The Authority has advised DEP that it will be seeking to amend the administrative consent order by deleting a rehabilitation contract not related to the relief project and by extending the completion date of the final construction contract to 2007.

Other Clean Water Act Requirements and Administrative Regulation of Sewage Sludge Reuse. In addition to program requirements of the Clean Water Act already reflected in the Permit and the Clean Water Act Case, other regulatory requirements under federal and state law may impose additional operating requirements on the Authority.

EPA has promulgated regulations covering the treatment and handling of sewage sludge, which provide aggressive protection of the environment and public health while permitting beneficial sludge reuse. In addition to the federal standards, the Authority’s sewage sludge products must comply with regulations applicable in each jurisdiction in which such products are used, including Massachusetts. Sewage sludge regulations adopted by DEP also govern permissible application and distribution of sludge as fertilizer in Massachusetts. The Authority has signed a memorandum of understanding with the Commonwealth to promote the beneficial reuse of its sludge within Massachusetts.

Other Regulatory and Compliance Matters. In common with most water and wastewater operating agencies, the Authority’s operations and improvements for its Systems are subject to numerous environmental regulatory requirements in addition to the SDWA and the Clean Water Act. These include environmental impact assessment requirements under NEPA and MEPA, permitting requirements under various federal and state laws for construction projects, and various requirements affecting the Authority’s properties and operations under the Federal Resource Conservation and Recovery Act of 1976 and the Federal Comprehensive Environmental Response, Compensation and Liabilities Act of 1980, the Clean Air Act, federal and related state laws and regulations regarding the handling, treatment and storage of oil, hazardous materials and other waste, water quality standards, and air pollution control requirements.

On January 5, 2007, the Authority received a letter from DOJ sent at the request of the EPA, notifying the Authority that the United States is prepared to bring a federal court enforcement action against the Authority for alleged violations of its Permit and the Clean Water Act and to seek the recovery of a monetary penalty of an unstated amount. While no specific violations were raised in that letter, the Authority believes that the focus of EPA's concerns is with past blending practices of the Authority. EPA raised issues with the Authority's blending practices in the spring of 2005 and the Authority has cooperated with EPA's information requests since that time. DOJ has offered the Authority the opportunity to discuss and resolve the alleged violations without the need for a federal court filing. DOJ has requested the execution of a Tolling Agreement, which the Authority's Board of Directors authorized on January 10, 2007.

Blending is a process whereby some of the wastewater effluent stream, having first received primary treatment, is directed around secondary treatment, in most cases, but not all, during wet weather events, and then "blended" with wastewater which has received both primary and secondary treatment, after which the wastewater effluent stream is disinfected and discharged. In the period from Fiscal Year 2002 through Fiscal Year 2006, 92.9% of flows discharged from the Authority's Deer Island Treatment Plant received secondary treatment. In Fiscal Year 2006, 95.4% of all discharged flows received secondary treatment. The Authority has consistently met water quality-based Permit limits, including during blending periods, since the Authority's current Permit was issued in August 2000.

LEGISLATIVE AND OTHER DEVELOPMENTS

From time to time legislation has been introduced in the Massachusetts legislature proposing to affect the Authority, including adding to its responsibility certain capital projects, increasing the Authority's debt authorization, providing financial assistance for its programs, and requiring it to make payments to other governmental entities in the Commonwealth. Some of these legislative proposals have been enacted, but it is not possible to predict whether any such legislative proposals will be enacted in the future.

On November 10, 2006, then-Governor Mitt Romney, using his authority under Section 9C of Chapter 29 of the Massachusetts General Laws, made budget cuts eliminating all funding for the Water and Sewer Rate Relief Fund from the Commonwealth's Fiscal Year 2007 budget. Prior to this cut, the Authority expected to receive approximately \$18.75 million in state debt service assistance from the Fund for Fiscal Year 2007, which amount was reflected in the FY07 CEB. On January 5, 2007, Governor Deval Patrick restored the full amount of debt service assistance funding of approximately \$18.75 million in the Commonwealth's Fiscal Year 2007 budget. The \$18.75 million figure is reflected in the Authority's FY07 CEB and in its rate revenue requirement for Fiscal Year 2007. The Authority cannot predict whether or what amounts will be appropriated by the Commonwealth to the Fund in the future. See "Rates and Charges" and "Management's Review of Operating Results – Fiscal Year 2007 Current Expense Budget" and "– Projected Revenues, Expenses and Fund Deposits."

LITIGATION

There is no threatened or pending litigation against or affecting the Authority that, to the knowledge of the Authority, seeks to restrain or enjoin the issuance, sale or delivery of the Series A/B Bonds, or to in any way contest or affect the validity of the Series A/B Bonds, the General Resolution, or any proceedings of the Authority taken with respect to the issuance or sale of the Series A/B Bonds or with respect to the General Resolution, or in any way contesting the existence or powers of the Authority.

The Authority is a defendant in a number of suits arising out of its operations and activities. These actions include contract claims arising from the Authority's capital projects as well as personal injury and property damage claims. To the best knowledge of the Authority's General Counsel, no litigation is pending or threatened which, in the opinion of the Authority's General Counsel, if decided adversely to the Authority, would be likely to result, either individually or in the aggregate, in final judgments against the Authority which would materially adversely affect its ability to meet debt service payments on the Series A/B Bonds, when due, or its obligations under the General Resolution, or materially adversely affect its financial condition.

In addition, due to the nature and scope of the CIP, the substantial number of Authority construction projects may result from time to time in the bringing of material claims for damages in tort or contract against the Authority. While the outcome of such litigation cannot be predicted, the Authority believes that it has made adequate provision through insurance, indemnification, performance bonds, construction monitoring, contingencies and reserves, among other measures, to limit its exposure to liability as a result of such claims.

TAX EXEMPTION

Bond Counsel is of the opinion that, under existing law, except as described below, interest on the Series A/B Bonds is not included in gross income for federal income tax purposes. Interest on obligations such as the Series A/B Bonds is not an item of tax preference for the purpose of computing the alternative minimum tax imposed on individuals and corporations under the Internal Revenue Code of 1986, as amended (the "Code"), but such interest is taken into account in determining adjusted current earnings for the purpose of computing the alternative minimum tax imposed upon certain corporations. See Appendix D – "Proposed Form of Opinion of Bond Counsel."

The Code imposes certain requirements and restrictions on the use and investment of proceeds of state and local governmental obligations, including the Series A/B Bonds, and a requirement for payment to the federal government (called a "rebate") of certain proceeds derived from the investment thereof. Failure to comply with the Code's requirements subsequent to the issuance of the Series A/B Bonds could cause interest on the Series A/B Bonds to become subject to federal income taxation, retroactive to the date of their issuance. On or before delivery of the Series A/B Bonds to the original purchasers, the Authority will provide covenants or certificates evidencing that it will take all lawful action necessary to comply with those provisions of the Code that, except for such compliance, would affect adversely the excludability of interest on the Series A/B Bonds from gross income for federal income tax purposes. Bond Counsel has not opined as to the other federal tax consequences resulting from holding the Series A/B Bonds.

Potential purchasers should be aware, however, of other collateral consequences that may result under the federal tax law for certain holders of the Series A/B Bonds. Interest on the Series A/B Bonds is included in the measure of the foreign branch profits tax imposed upon corporations and may be included in passive investment income subject to federal income taxation under provisions of the Code applicable to certain S corporations. The Code further provides that interest on the Series A/B Bonds may be includable in the modified adjusted gross income of certain recipients of Social Security and Railroad Retirement benefits for the purpose of determining whether a portion of such benefits shall be included in the taxable income of such recipients. In addition, certain otherwise deductible underwriting losses of property and casualty insurance companies will be reduced by a portion of the interest received by such companies on the Series A/B Bonds, and no deduction will be allowed for interest on indebtedness incurred or continued to purchase or carry the Series A/B Bonds or, in the case of a financial institution, that portion of such institution's interest expense that is allocated to interest on the Series A/B Bonds.

In the opinion of Bond Counsel, the Series A/B Bonds, their transfer and the income therefrom, including any profit made on the sale thereof, are exempt from Massachusetts personal income taxes and the Series A/B Bonds are exempt from Massachusetts personal property tax, although the Series A/B Bonds and the interest thereon are included in the measure of estate and inheritance taxes and of certain corporation excise and franchise taxes. Bond Counsel has not opined as to other Massachusetts tax consequences or as to the taxability of the Series A/B Bonds, their transfer and the income therefrom, including any profit made on the sale thereof, under the laws of jurisdictions other than The Commonwealth of Massachusetts.

For federal and Massachusetts tax purposes, interest includes original issue discount, which with respect to a Series A/B Bond is equal to the excess, if any, of the stated redemption price at maturity of such Series A/B Bond over the initial offering price thereof to the public, excluding underwriters and other intermediaries, at which price a substantial amount of all Series A/B Bonds with the same series and maturity was sold. Original issue discount accrues actuarially over the term of a Series A/B Bond. Holders should consult their own tax advisers with respect to the computations of original issue discount on such accruals of interest during the period in which any such Series A/B Bond is held.

The excess, if any, of the tax basis of the Series A/B Bonds to a purchaser (other than a purchaser who holds such Series A/B Bonds as inventory, stock in trade or for sale to customers in the ordinary course of business) over the

amount payable at maturity is “bond premium.” For federal income tax purposes, bond premium is amortized over the term of such Series A/B Bonds, is not deductible and reduces the purchaser’s adjusted tax basis. Bond purchasers should consult their tax advisers with respect to the consequences of such bond premium.

On the date of delivery of the Series A/B Bonds, the Underwriters will be furnished with an opinion of Bond Counsel substantially in the form attached hereto as Appendix D – “Proposed Form of Opinion of Bond Counsel.”

FINANCIAL ADVISORS

Public Financial Management, Inc. (“PFM”) and Lamont Financial Services Corporation serve as financial advisors to the Authority for issuance of the Series A/B Bonds, debt management and other financial matters. PFM has acted as independent financial advisor to the Authority with respect to the Series A/B Bonds. PFM is not obligated to undertake, and has not undertaken, either to make an independent verification of or to assume responsibility for, the accuracy, completeness, or fairness of the information contained in this Official Statement and the appendices hereto. PFM is an independent financial advisory firm and is not engaged in the business of underwriting, trading or distributing securities.

INDEPENDENT ACCOUNTANTS

The financial statements of the Authority as of June 30, 2006 and for the Fiscal Year then ended, included in Appendix A of the Official Statement have been audited by KPMG LLP, independent accountants, as stated in their report included in Appendix A. KPMG LLP has not performed any procedures relating to the Series A/B Bonds. The financial statements of the Authority as of June 30, 2005, and for the Fiscal Year then ended, were audited by Deloitte & Touche LLP, independent accountants, as set forth in their report, dated October 21, 2005.

CONSULTING ENGINEER

Camp Dresser & McKee Inc. serves as the Authority’s engineering consultant in connection with the issuance of the Series A/B Bonds. The Supplemental Feasibility Report prepared by Camp Dresser & McKee Inc. is attached hereto as Appendix B. The Engineering and Financial Feasibility Report, which is incorporated herein by reference, as supplemented by the Supplemental Feasibility Report included as Appendix B hereto, provides an independent engineering analysis of the Authority’s Systems and a financial feasibility analysis of the Authority’s current operations and CIP.

CERTAIN LEGAL MATTERS

All legal matters incident to the authorization, issuance, sale and delivery of the Series A/B Bonds are subject to the approval of Ropes & Gray LLP, Boston, Massachusetts, Bond Counsel to the Authority. Certain legal matters will be passed upon for the Authority by its Disclosure Counsel, Edwards Angell Palmer & Dodge LLP, Boston, Massachusetts, and for the Underwriters by their counsel, Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C., Boston, Massachusetts.

UNDERWRITING

The Series A/B Bonds are being purchased by the Underwriters, for whom Bear, Stearns & Co. Inc. is acting as Representative. The Underwriters have agreed, subject to certain conditions, to purchase all of the Series A/B Bonds from the Authority at an aggregate underwriters’ discount from the initial public offering prices or yields set forth on the inside cover page of this Official Statement equal to \$4,598,735.25 and to reoffer such Series A/B Bonds at public offering prices not higher than or at yields not lower than those set forth on the inside cover page of this Official Statement. The Underwriters are obligated to purchase all such Series A/B Bonds, if any are purchased, the obligation to

make such purchase being subject to certain terms and conditions set forth in the purchase contract, the approval of certain legal matters by counsel and certain other conditions. Such Series A/B Bonds may be offered and sold by the Underwriters to certain dealers (including dealers depositing such Series A/B Bonds in unit investment trusts or mutual funds, some of which may be managed by the Underwriters) and certain dealer banks and banks acting as agents at prices lower (or yields higher) than the public offering prices (or yields) set forth on the inside cover page of this Official Statement. Subsequent to such initial public offering, the Underwriters may change the public offering prices (or yields) as they may deem necessary in connection with the offering of such Series A/B Bonds.

RATINGS

The Series A/B Bonds have been rated “AAA” by Fitch Ratings (“Fitch”), One State Street Plaza, New York, New York, “Aaa” by Moody’s Investors Service, Inc. (“Moody’s”), 99 Church Street, New York, New York and “AAA” by Standard & Poor’s Ratings Services (“Standard & Poor’s”), a division of The McGraw-Hill Companies, Inc., 55 Water Street, New York, New York, based on the bond insurance on the Series A/B Bonds provided by Financial Security. See “Bond Insurance” and Appendix F.

The ratings express only the views of the rating agencies. The explanation of the significance of the ratings may be obtained from Fitch, Moody’s and Standard & Poor’s, respectively. There is no assurance that any rating will continue for any period of time or that it will not be revised or withdrawn. Any revision or withdrawal of ratings on the Series A/B Bonds may have an effect on the market price thereof.

VERIFICATION OF MATHEMATICAL COMPUTATIONS

The arithmetical accuracy of certain computations included in the schedules provided by Bear, Stearns & Co. Inc. on behalf of the Authority relating to (a) computation of anticipated receipts of principal and interest on the Escrow Securities and the anticipated payments of principal and interest to redeem the Refunded Bonds, and (b) computation of the yields on the Series B Bonds and the Escrow Securities was examined by The Arbitrage Group, Inc. Such computations were based solely upon assumptions and information supplied by Underwriters on behalf of the Issuer. The Arbitrage Group, Inc. has restricted its procedures to examining the arithmetical accuracy of certain computations and has not made any study or evaluation of the assumptions and information upon which the computations are based and, accordingly, has not expressed an opinion on the data used, the reasonableness of the assumptions, or the achievability of future events.

CONTINUING DISCLOSURE

General. The Authority has undertaken for the benefit of the owners of the Series A/B Bonds to provide certain continuing disclosure pursuant to the provision of Rule 15c2-12(b)(5) under the Securities Exchange Act of 1934 (as amended, the “Rule”). Specifically, the Authority and State Street Bank and Trust Company, predecessor in interest to U.S. Bank National Association, as Dissemination Agent (the “Dissemination Agent”) have executed and delivered a Continuing Disclosure Agreement dated November 21, 1995 (the “Continuing Disclosure Agreement”) for the benefit of the owners of all bonds (including the Series A/B Bonds) issued by or on behalf of the Authority which are designated by resolution of the Authority as subject to and having the benefits of the Continuing Disclosure Agreement. As of the date hereof, the Authority is in full compliance with the terms of the Continuing Disclosure Agreement.

Annual Filings. Pursuant to the Continuing Disclosure Agreement, not later than January 1 of each year, commencing January 1, 1998, the Authority will, or will cause the Dissemination Agent to, provide an Annual Filing (as described below) to each nationally recognized municipal securities information repository (the “National Repositories”) and any public or private repository or entity designated by the Commonwealth as a state information repository for the purpose of the Rule (a “State Depository” and, collectively with the National Repositories, the “Repositories”). The Annual Filing may be submitted as a single document or as separate documents comprising a package, and may cross-reference other information as provided in the Continuing Disclosure Agreement. If the Dissemination Agent determines that the Authority has failed to comply with the undertaking regarding the Annual Filing, the Dissemination Agent will

send a notice to that effect in a timely manner to the Municipal Securities Rulemaking Board (the “MSRB”) and the State Depository, if any.

The Authority’s Annual Filing will contain or incorporate by reference the following:

(a) quantitative information for, or as of the end of, the preceding fiscal year of the type presented in the Authority’s most recent official statement, including (i) a summary table of revenues, expenses and fund deposits, (ii) the amount of outstanding indebtedness of the Authority, and the debt limit as of the end of the fiscal year, (iii) a summary table with respect to the coverage covenants in the Authority’s General Resolution and (iv) a summary table showing the Authority’s capital investments by major category during the preceding fiscal year;

(b) quantitative information for the current fiscal year of the type presented in the Authority’s most recent official statement, including (i) a table of the Authority’s current water and wastewater charges by Local Body, (ii) the current expense budget’s rate revenue requirement and the percentage increases for water and wastewater over the prior fiscal year and (iii) executive summaries of the Authority’s most recently adopted current expense budget and capital improvement program; and

(c) the most recently available audited financial statements of the Authority, prepared in accordance with accounting principles generally accepted in the United States of America. (If audited financial statements for the preceding fiscal year are not available when the Annual Filing is submitted, the Annual Filing will include unaudited financial statements for the preceding fiscal year.)

Any or all of the items listed above may be incorporated by reference from other documents, including official statements of debt issues of the Authority or related public entities, which have been submitted to each of the Repositories or the Securities and Exchange Commission. If the document incorporated by reference is a final official statement, it must be available from the MSRB.

Reporting of Material Events. Pursuant to the Continuing Disclosure Agreement, whenever the Authority obtains knowledge of the occurrence of any of the following events with respect to the Series A/B Bonds (each a “Listed Event”), if material under applicable federal securities laws, the Authority will promptly notify the Dissemination Agent. The Dissemination Agent shall file a notice of such occurrence promptly with the MSRB and the State Depository, if any.

1. Principal and interest payment delinquencies.
2. Non-payment related defaults.
3. Unscheduled draws on debt service reserves reflecting financial difficulties.
4. Unscheduled draws on credit enhancements reflecting financial difficulties.
5. Substitution of credit or liquidity providers, or their failure to perform.
6. Receipt by the Authority of an adverse tax opinion or the occurrence of an event affecting the tax-exempt status of the Series A/B Bonds.
7. Modifications to rights of any owners of the Series A/B Bonds.
8. Bond calls.
9. Defeasance of the Series A/B Bonds or any portion thereof.
10. Release, substitution or sale of property securing repayment of any Series A/B Bonds.

11. Rating changes.

Termination of Reporting Obligation. The Authority's and Dissemination Agent's obligations under the Continuing Disclosure Agreement will terminate upon the defeasance, prior redemption or payment in full of all of the bonds (including the Series A/B Bonds) designated as subject to the agreement.

Amendment; Waiver. Notwithstanding any other provision of the Continuing Disclosure Agreement, the Authority and the Dissemination Agent may amend the Continuing Disclosure Agreement, and any provision of the Continuing Disclosure Agreement may be waived, if such amendment or waiver is permitted by the Rule, as evidenced by an opinion of counsel expert in federal securities laws, acceptable to both the Authority and the Dissemination Agent, to the effect that such amendment or waiver would not, in and of itself, cause the Authority's undertakings to violate the Rule if such amendment or waiver had been effective on the date hereof but taking into account any subsequent change in or official interpretation of the Rule.

If the amendment provides for a change in the accounting principles to be followed in preparing financial statements, the Annual Filing for the year in which the change is made shall present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles. The comparison shall include a qualitative discussion of the differences in the accounting principles and the impact of the change in the accounting principles on the presentation of the financial information in order to provide information to investors to enable them to evaluate the ability of the Authority to meet its obligations. To the extent reasonably feasible, the comparison shall also be quantitative. A notice of the change in the accounting principles shall be sent to each Repository.

Default. In the event of a failure of the Authority or the Dissemination Agent to comply with any provision of the Continuing Disclosure Agreement, the Dissemination Agent may (and, at the request of any of the Underwriters or the owners of at least 25% aggregate principal amount outstanding of the Series A/B Bonds, shall), or any owner of the Series A/B Bonds may, seek a court order for specific performance by the Authority or Dissemination Agent, as the case may be, of its obligations under the Continuing Disclosure Agreement. A default under the Continuing Disclosure Agreement shall not be deemed an Event of Default under the General Resolution, and the sole remedy under the Continuing Disclosure Agreement in the event of any failure of the Authority or the Dissemination Agent to comply with the Continuing Disclosure Agreement shall be an action to compel performance of the defaulting party's obligations thereunder and not for money damages in any amount.

BONDS AS LEGAL INVESTMENTS

Under Section 14 of the Act, bonds and notes of the Authority are made securities in which all public officers and agencies of the Commonwealth and its political subdivisions, all insurance companies, trust companies in their commercial departments, savings banks, cooperative banks, banking associations, investment companies, executors, administrators, trustees and other fiduciaries may properly invest funds, including capital in their control or belonging to them.

BONDS AS SECURITY FOR DEPOSIT

Under Section 14 of the Act, bonds and notes of the Authority are made securities which may properly be deposited with and received by any state or municipal officer of any agency or political subdivision of the Commonwealth for any purpose for which the deposit of bonds or other obligations of the Commonwealth is now or may hereafter be authorized by law.

MISCELLANEOUS

The summaries or descriptions herein of provisions of the Act, the Series A/B Bonds, the General Resolution and the Continuing Disclosure Agreement, and all references to other materials not purporting to be quoted in full, are

only brief outlines of some of the provisions thereof and do not purport to summarize or describe all of the provisions thereof. So far as any statements are made in this Official Statement involving matters of opinion, whether or not expressly so stated, they are intended merely as such and not as representations of fact. Copies of the documents mentioned in this paragraph are on file at the offices of the Authority and the Trustee.

The execution and delivery of this Official Statement have been duly authorized by the Massachusetts Water Resources Authority.

MASSACHUSETTS WATER RESOURCES AUTHORITY

By: /s/ Frederick A. Laskey
Frederick A. Laskey
Executive Director

By: /s/ Patricia A. Filippone
Patricia A. Filippone
Chief Financial Officer

January 17, 2007