



2007

ANNUAL REPORT

CITY OF HOLYOKE GAS & ELECTRIC DEPARTMENT

In Memoriam



Neil J. Moriarty Jr.

June 1, 1931-September 1, 2007

HG&E Commission Chairman Neil J. Moriarty, Jr. died on September 1, 2007 after a long illness. Neil served on the Holyoke Gas & Electric Commission for 19 years, and was the Commission Chairman for the last ten years. He guided HG&E through some of the most complex initiatives in the Department's history including: Electric Utility Deregulation, the Development of a Fiber Optic Network, and the purchase of the Holyoke Hydroelectric Dam and Canal System. HG&E owes a huge debt of gratitude to Neil for his tireless efforts and longtime support.

We hereby dedicate our 2007 Annual Report in his memory.

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gas | electric | steam | telecom

Commissioners:
Neil J. Moriarty, Jr.
Francis J. Hoey, III
Robert H. Griffin

Manager:
James M. Lavelle

To the Honorable Mayor, Members of the City Council, and our Valued Customers:

Submitted herewith is the One Hundred and Fifth Annual Report of the City of Holyoke Gas & Electric Department for the year ending December 31, 2007.

On a somber note, September 1st 2007 brought the passing of Neil J. Moriarty Jr, our Commission Chairperson. Having served on the HG&E Commission for the past 19 years, he guided the Department through some of the most complex initiatives in its history including: Electric Utility Deregulation, the Development of a Fiber Optic Network, and the purchase of the Holyoke Hydroelectric Dam and Canal System. HG&E owes a huge debt of gratitude to Neil for his tireless efforts and longtime support.

In keeping with values instilled upon it during Mr. Moriarty's tenure, HG&E continued to provide its customers with some of the lowest utility rates in the Commonwealth. HG&E electric customers received rates that are almost 50% less than those offered to residents of surrounding communities served by investor-owned utilities.

In addition to low rates, over 50% of the electric power consumed by our customers in 2007 came from clean renewable energy sources. This resulted in the City having a carbon footprint that was almost 1/3 that the New England average.

In 2007, our electric division completed work on a multi-million dollar capital improvement project at our Ingleside substation. This project added a third transformer at that site, now providing for up to 40 MVA of connected capacity at that facility.

Our Gas Division continued to make upgrades to its distribution system, replacing almost one mile of cast iron pipe with modern plastic gas mains. In addition, significant system expansion continued in Southampton with over 1.5 miles of new gas lines installed.

2007 brought the expansion of our fiber optic internet network into Chicopee. Working in cooperation with Chicopee Electric Light, customers in that City now have access to the same reliable high speed services that Holyoke businesses have enjoyed for over a decade.

We thank the City officials and Department employees for their continued faithful service to HG&E, and we will continue to work diligently to provide our customers with service at the lowest possible rates and backed by a dedication to service that is second to none.

Respectfully,

Neil J. Moriarty, Commission Chairman
Francis J. Hoey, Commission Treasurer
Robert H. Griffin, Commission Secretary
James M. Lavelle, Manager

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gas

New Services

In 2007, the Department installed services to 96 new customers. 46 of those customers were in Holyoke with the remaining 50 located in Southampton. The Department also replaced 87 existing services in Holyoke by burying new plastic pipe or inserting it through older existing steel pipes. 49 unneeded gas service lines in Holyoke were disconnected from the Distribution System.

New and Replacement Mains

Replacement of cast iron gas mains in Holyoke continued this year. In conjunction with extensive road construction in the Commercial Street area, the Department replaced a total of 1,200 feet of cast iron pipes with new plastic pipe. Upper Brookline Avenue, Clinton Avenue, and Liberty Street were also completely reconstructed, and over 2,500 feet of new plastic pipe was installed. Numerous smaller projects were also completed, resulting in abandonment of 4,500 feet of cast iron and wrought iron pipe in total. These facilities were replaced with plastic pipe that was generally four or six inches in diameter.

A new plastic gas main was also installed on Bemis Road, although approximately 1 mile of cast iron pipe remains in that area. New regulator vaults were also installed on Vadnais Street. This equipment is expected to help alleviate pressure fluctuations in the Highlands area. These additions to the Distribution System could also aid in delivery of gas to the Smith's Ferry area if facilities are extended as anticipated.

The Gas Division continued its expansion in Southampton through completion of gas installations in Red Brook Estates.

This work included addition of 4,500 feet of 6" plastic pipe on Katelyn Way, Brittney Lane, and Kevin Drive. Elsewhere in Southampton, new subdivisions on Pine Wood Drive, Maddeline Way, and Whispering Meadow Road were connected to the gas system through installation of 2,800 feet in new plastic mains.

In total, 3.25 miles of plastic gas main was installed in Holyoke and Southampton in 2007, while 0.85 miles of cast iron mains were abandoned in Holyoke.

The Holyoke/Southampton natural gas distribution system now consists of over 166 miles of mains and 7,350 active gas services.

In total, 10% of the Department's gas mains and service pipes are located in the Town of Southampton, although only 5% of the Gas Division sales by volume come from this area.

Leak Surveys

The Department helps ensure the safety and reliability of the gas distribution system through an extensive series of compulsory and voluntary comprehensive leak surveys.

Each year the Department conducts public building, mobile and walking flame ionization patrols, special monthly winter patrols, and vegetation observation surveys. The full-length walking survey covered 3,500 service lines in 2007, representing nearly one-half of the services in the system. Combined the surveys accounted for the detection of 139 underground leaks of varying extents. All leaks were investigated and prioritized. 91 were repaired in 2007, and the remainder were monitored throughout the winter and/or scheduled for repair in 2008.

Other Preventative Maintenance - Corrosion Mitigation

The Gas Division continued its aggressive program to mitigate corrosion on its coated steel piping systems. In 2007, professional inspections were made of all 63 of the cathodically protected gas main subsystems, and the 28 coated steel services longer than 100 feet.

At year's end 80% of the systems exceeded the federal requirements for corrosion control, with the rest expected to become satisfactory in 2008. In addition, 64 isolated steel gas services (less than 100 feet in length) were inspected and maintained. Additional remedial actions are scheduled for 2008, accompanied by with more inspections.

Gas Supply and Flow Control

The Gas Division continues to operate its new Liquefied Natural Gas storage and vaporizing system, providing the extra gas needed during the coldest winter days. The system can also act as an emergency supply for the entire city if needed.

The Department also provided peaking service to Bay State Gas as part of a LNG supply and vapor displacement contract. This arrangement has enabled the Department to better utilize its LNG assets, and has provided benefits for both companies. This service is expected to be continued in 2008.

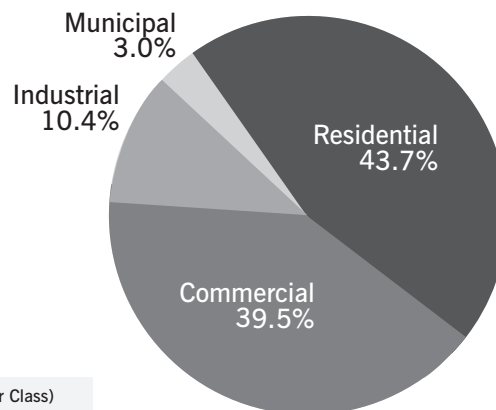
Gas Works

The Department operated its two tar removal systems during the year. The Tailrace system, which intercepts dense non-aqueous phase liquid (DNAPL) coal tar before it can migrate beneath the river, collected 2,317 gallons of tar. The tar is collected and then sent off site for disposal. The second system is on the site itself, and pumps DNAPL in a similar fashion as the Tailrace area recovery system. The on-site DNAPL system uses steam generated from the Cabot Street Station to warm the DNAPL in order to aid in its pumping to the recovery wells. This system only collected 16 gallons of tar in 2007. The tar is less mobile than anticipated even with steam injection and may not need to be recovered. Further analysis of this system will take place in 2008.

River Sediment Remediation - Northeast Utilities

Holyoke Water Power (HWP) continued to work with the MA DEP in performing a Method 3 Risk Characterization for all remaining tar deposits in Site Portion 1 (SP-1) and Site Portion 2 (SP-2) of the river. SP-1 starts at the dam and extends to just south of Riverside Station and SP-2 starts at Riverside Station and extends to the 391 Connecticut River Bridge. HWP performed some preliminary work on the Method 3 risk Characterization at the site in order to provide field data to support its position.

2007 Gas Division Revenues (by Customer Class)



steam

Cabot Street Repowering

Previous repowering studies were further developed during 2007 to determine if additional steam and electric generation equipment could be installed at the plant.

A study conducted in 2006 had identified that a 15 MW gas turbine could be economically installed at the plant. In 2007, this option was further defined and it was determined that the anticipated capacity payments would not be sufficient to support the project. Consequently, the project was put on hold to await the results of the First ISO Forward Capacity Auction in February of 2008.

The department also evaluated installation of a 60 MW gas turbine peaking unit as part of these investigations.

Operations

- The electric station had a maximum electric generation load of 305,000 lbs/hr during 2007. The maximum non generation hourly load was 140,000 lbs/hr.
- The electric station produced 450,678,000 lbs of steam in 2007. The steam is used for electric generation and is supplied to 37 customers for heating and production uses.
- The Distribution portion of Steam Schedule I was raised by 10% in July which will generate approximately \$38,000 of revenue per year.
- Superior Carriers relocated a wax transfer station to Holyoke and will be using steam on a year round basis. It is estimated that this customer will contribute an estimated \$26,000 per year in steam distribution revenue.

Distribution System Study

A plan to reduce the number of steam distribution mains and concentrate on the core customers was developed. This plan will reduce the number of mains by 37% and remove 13 customers from the system.

This plan would improve the steam division net revenue by \$70,000 and avoid a 100% distribution rate increase. It will also avoid over \$1.2 million in capital expenses over the next 5 years. Evaluation of this plan will continue throughout 2008.

Boiler Demolition

The demolition of boiler #6 was began in September of 2007 and will be completed in 2008. This boiler was retired at the end of 2006 with the completed installation of boilers #7 & #8.

Boiler #6 was a 4 story boiler that was erected in the 1950's. The demolition includes asbestos abatement, hazardous material remediation and traditional demolition. The demolition of boiler #6 will allow for future equipment to be added at the station.

electric

Hydro Production

The Hydro Division continues to focus on its mission to provide the Department with the lowest cost electrical energy available in an environmental responsible manner.

In 2007, the Division generated 187,168 MWhrs (net of station service loads) from its hydroelectric plants. This renewable energy resource amounted to 50.6% of all electricity consumed within the City.

Hydroelectric production was lower than expected due to the unscheduled outage of Hadley Falls Unit 1 (16,000 kW) from January 15 to May 17, 2007. This outage was due to the failure of a turbine wicket gate stem. Repairs were made "in place" to return the unit to service. Inspections of the repairs are expected to occur in the summer of 2008.

Generation Unit Improvements

Several key projects which improved generation capacity and reliability were completed or substantially near completion by year end. These include:

Riverside 8 - Complete "water-to-wire" rebuilt of unit. It is anticipated that this work will increase generating capacity by 300 kW or 1000 MWhr annually. Expected return to service date is spring 2008.

Boatlock 3 - Completed installation of new turbine runner. In service date of 11/27/07.

Valley (City #5) - completed unit overhaul which included a complete generator stator rewind. Overhaul increase capacity from 340 kW to 720 kW. In service date of 11/5/07.

Other Key Accomplishments

The Department conducted a number of programs in 2007 in concurrence with its 40-year operation licence for the Hadley Falls Hydroelectric Project.

These initiatives included: a River Impoundment Study, Downstream Fish Passage Studies related to Hadley Falls Station, continued evaluation of shoreline erosion, and implementation of recreation and land management objectives as stated in the FERC project license.

2007 Fish Passage Counts

The fishlift at HG&E's Robert E. Barrett Fishway helps migrating fish over the Holyoke Hydroelectric Dam. It was the first and most successful fish lift on the Atlantic coast. It consists of two elevators or "lifts" which carry migrating fish up and over the dam.

In 2007, the following quantities of monitored fish species were observed utilizing the lift system.

Atlantic Salmon	102
American Shad	158,807
Blueback Herring	75
Sea Lamprey	42,435
Striped Bass	142
Shortnose Sturgeon	4

electric

Electric Distribution

System improvements in 2007 for increased reliability of electric service to the City of Holyoke included replacing eight three phase live front transformers with new single phase dead front transformers in the Knollwood Circle area. A half mile section of main line underground along Northampton Street including six laterals originating from this cable were replaced and five new vacuum switches were installed providing sectionalizing points to isolate outages. This work also included other reliability upgrades such as replacing all porcelain hardware with polymer and installing new crossarms, connectors, poles, and fault indicators.

A portion of the 4.8 kV O1 circuit was converted to 13.8 kV in 2007. This area included Brown Avenue, View Street, Glen Street, Larkin Avenue, and small sections of Willow Street, Laurel Street, and South Street. Over a half mile of 336 Al overhead wire replaced existing wire along Brown Avenue and View Street providing a new tie point to the 52W1 circuit at View and Northampton Streets. Also included within the project was the replacement of 17 poles, all deteriorated crossarms, any porcelain hardware with new polymer hardware, and secondary mains as required. This extension of the 17L2 circuit not only provides enhanced reliability for the immediate area but also provides a new circuit tie to enhance reliability for an even broader area of the City.

As a result of a third transformer recently installed at Ingleside Substation, two new 500 MCM getaway cables were installed from this new transformer. The two new circuits, 52W9 and 52W11, became the new designation for the 52W4 and 52W5 circuits respectively.

The first of three phases of the Riverview Estates Condominium project on Northampton Highway was completed. Electric services to 14 units were provided resulting in a new connected load of 100 kVA. Approximately 1,000' of new underground primary cable and five contract lights were installed as part of this phase of the project.

A new electrical feed to the Gill D hydro generation wheel building was installed. This new feed replaces the old feed originating from inside the Gill A building to the Gill D building operating from the same switchgear. A new pole, transformer, and primary wire were installed to complete this job and isolate this wheel from the Gill D switchgear.

A State project involving improvements to Commercial Street and Nick Cosmos Way was completed in 2007. A portion of Commercial Street near the intersection of Cabot Street was reconfigured to improve traffic flow and connect directly to Nick Cosmos Way. As a result, eleven wood poles were removed and the overhead wire relocated underground improving not only any safety issues along Commercial Street but also enhancing reliability. Ten new concrete street poles were also installed replacing four wood poles and six steel poles that were removed as part of the project.

Fourteen services on Lincoln Street, Beacon Avenue, Cleveland Street, Allyn Street, Meadow Street, S. Bridge Street, N. Canal Street, Hitchcock Street, Northampton Street, Harvard Street, Longwood Avenue, and Morgan Street were relocated from heavily overgrown areas with difficult accessibility to the street. This will provide these customers with not only a more reliable electric service but also protection from potential safety hazards and safety code violations which will, in turn, reduce some of the tree trimming and outage costs of the Department.

Electric Distribution - continued

Utility Pole Technologies (UPT) was hired to inspect and treat all wood poles as well as provide GPS points for all poles in our service territory. UPT inspected 2,034 Department owned wood distribution and transmission poles and 118 wood distribution and transmission poles at Cobble Mountain hydro generation facility. Of the Department-owned poles, some jointly owned with Verizon, a total of 5 poles were identified as Danger requiring replacement within 3 business days while another 74 poles were found to be Reject requiring replacement within 1 year. This is the first of three phases for the inspection and treatment of wood poles.

There were three residential/commercial buildings that required new electric services. Mount Marie Assisted Living Complex on Lower Westfield Road, Sullivan Steel on Appleton Street, and Steibel apartments on Nonotuck Street resulted in a net additional connected load of 1,075 kVA. There were also 7 new homes that required new electric services resulting in a connected load of 75 kVA. The new homes were constructed on available lots along Southampton Road, Western View Road, Longfellow Road, Stratford Road, Dale Street, and Fairfield Avenue.

(continued on next page)

Electric Distribution System Reliability Statistics

	HG&E 2007	HG&E 2006	TYPICAL MUNICIPAL UTILITY	PRIVATE UTILITIES
ASAI	99.993%	99.992%	99.989%	99.982%
CAIDI	113.85min	103.84min	60min	90min
SAIDI	44.33min	71.67min	60min	102.32min
SAIFI	0.34outages	0.68outages	1outage	1.02outages
MAIFI	2.77events	3.25events	2-4events	3.13events

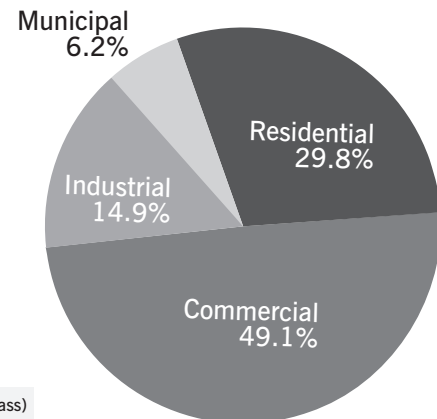
Average System Availability Index (ASAI) - represents how much of the time a customer actually has service available to them.

Customer Average Interruption Duration Index (CAIDI) represents the average time expected to take to restore service after a sustained interruption.

System Average Interruption Duration Index (SAIDI) defines the average interruption duration per customer served.

System Average Interruption Frequency Index (SAIFI) defines the average number of times that a customer's service is interrupted during a given year.

Momentary Average Interruption Frequency Index (MAIFI) defines the average number of momentary outages a customer may experience in a year.



2007 Electric Division Revenues (by Customer Class)

electric

Electric Distribution - Continued

In summary for 2007, HG&E set 46 poles and removed 26. A net 297 kVA connected load was installed on the distribution system. Some 17,422 circuit feet of underground cable was installed while 5,157 was removed. Similarly, 34,646 circuit feet of overhead wire was installed while 18,220 was removed. Approximately 2.2 miles of conduit was installed including 11,592 feet of PVC and 60 feet of steel. A net total of 53 contract lights were installed on the distribution system.

Electric Operations

Two major substation capital improvement projects were completed during the year at the Department's Ingleside and Holyoke Substations. Commissioning of the third 115 kV power transformer at Ingleside occurred in April providing firm capacity for peak station loading which now exceeds 40 MVA. The project spanned three years at a total cost of \$2.0 million including an additional 115 kV high side breaker and four (4) new 13.8 kV low side feeder positions.

At Holyoke Substation the 1950's vintage 115 kV 25,000 Amp oil interrupting 1T circuit breaker was replaced with an SF6 gas insulated unit with a 40,000 Amp interrupting rating. The new breaker was commissioned on October 14th and resolves the maintenance, age and inadequate interrupting duty issues with the previous unit. Total project cost was \$125,000 and constituted 100% PTF.

Substation circuit reconfiguration during the year included the re-termination of the 52W4 and 52W5 feeders at Ingleside to breaker positions on the newly added 13.8 kV A3 Bus. This accomplished a load balance between the three transformers while equipping the relocated feeders with enhanced metering and protective relaying functionality.

Based on a 2004 report which outlined operational deficiencies, reliability issues, and deteriorating condition of equipment, work commenced on a project to replace Prospect Substation with a new substation and two (2) 115 kV transmission lines in Holyoke. In 2007, the Department retained an engineering firm, legal representation, and a surveying contractor for the preliminary design of the station and preparation of required filings. The station has a tentative in service date of 2010.

At Prospect Substation, two major projects were started and are substantially complete. During the week of 11/26 to 11/30, thirteen (13) 1950's vintage 15kV air magnetic circuit breakers were replaced with new vacuum interrupting breakers. The original breakers had bad Doble insulation power factor test results and were a liability to worker safety and system reliability. As a separate project, SCADA control and indication points were installed and tested on the Prospect RTU for four (4) HG&E feeders and two (2) transformer low side breakers. Control and indication points were also commissioned for the auto reclosing function associated with each of these breakers as applicable. This allows for the remote operation of the station and enhances the operator's ability to respond to system disturbances.

As part of the Department's preventative maintenance (PM) plan, major maintenance and testing was performed on various substation equipment throughout the year. In summary, four (4) 115 kV transformers, one (1) 4.8 kV generator, three (3) air magnetic circuit breakers, and eight (8) vacuum circuit breakers were tested and maintained as required. In addition, all protective relays affecting the Department's transmission system, including underfrequency load shedding relaying (UFLS), were tested in accordance with NPCC and NERC requirements. In total, 141 relays were tested at three (3) bulk

Electric Operations - Continued

power substations: Holyoke 17L, Ingleside 52W, and Prospect 24B. All relays serviced were calibrated to values that fall within the manufacturers published limits.

Support for Electric Distribution during the year included the preparation of fifty five (55) switching orders with forty one (41) clearances issued for planned and emergency high voltage work. Maintenance/repair operations were also performed as required on various distribution equipment including monthly inspections of line recloser and capacitor switching controls as well as acceptance testing of ninety nine (99) transformers. Support was again provided for the City owned Flood Control Pumping Stations as well as the Department's Steam Division in the form of electrical marking and isolating work associated with boiler demolition at the Cabot Street Generating Station.

Metering

The metering group continued to make progress in its gas and electric AMR migration as 81% of the entire City can now be read remotely. On the electric side, the group installed 3,588 AMR meters in the field this year. There are now a total of 15,077 AMR electric meters installed, which represents approximately 84% of all electric meters. Most installations are predominantly single phase residential and smaller three phase commercial customers. On the gas side, the metering group installed a total of 275 AMR-enabled gas meter indexes. Along with assistance from the gas service department, the total number of AMR gas meters installed is 9,130, which represents approximately 78% of all gas meters.

A total of three additional ION 8600 series revenue meters were programmed, configured, and installed at our largest industrial customer's plant, Sonoco Products, to provide real-time data

of their plant's electrical services for their corporate headquarters in S. Carolina. Access to real-time data was made available via web browser utilizing our fiber optic network. These meters also provided the Department informational data to explain outages, voltage fluctuations, or any other similar electrical issues that may have occurred on the circuit and/or substation and eliminated antiquated telephone modem connections to each of their electric meters.

A total of 36 tie-line and generation meters were tested to meet ISO-NE's OP-18 metering requirements which include 6 meters at Prospect Sub utilized by Chicopee Electric Light Department. These meters are tested by Electric operations personnel on a biannual basis through the use of the Department's own portable test unit.

Throughout the year, the metering group continued to support the Credit Department on a full time basis, performing delinquent customer ons and offs, tagging notifications, meter reads, and collections. In total, 3,085 credit related duties were performed, a small increase from last year.

In summary, there were a net total of 123 electric meters removed and 3,455 replaced having an average age of 35.74 years. A total of 1,860 and 2,566 gas and electric meters respectively were tested and calibrated, 6 meters repaired, 2 power factor checks performed, and 92 no or low consumption reports investigated for metering problems and/or theft of service. A net total of 7 current transformers were installed. On the gas side, 1,860 meters were removed and tested, 1,863 meters were installed, another 1,728 meters were sealed, and 941 meters were condemned.

electric

Wholesale Power

A total of 187,169 MWh of net generation was produced from the Department-owned hydro resources which continued to help drive down the overall cost of power. During 2007, a credit of \$429,301 was applied to residential accounts due to these hydro facilities. Our hydro preference power credits to our residential customers, including both Department-owned hydro and NYPA, was increased for the 2nd consecutive year in August resulting in around a 1.5% overall rate drop.

Cabot 6 & 8 had 578 MWh of output during 2007, primarily due to performing capability audits. The steam turbines were dispatched by the pool 4 times.

During 2007, the Department procured 31,852 MWh of energy to meet its summer shortfall at a cost of \$2.05M. Roughly 80% of this energy was during on-peak hours where the Department is most exposed due to the volatility of the energy markets and the lack of hydro output. Throughout the entire year, the Department purchases under contract around 3,000 MWh in total from Sonoco Products and Open Square energy from canal hydro units at a price of around \$50/MWh.

The capacity market under the Transition Period which started on December 1, 2006 set capacity revenues for generation at \$3.05/kW-month for the entire 2007 calendar year. Since there is more generation than load in New England, the cost for load is greater at roughly \$3.89/kW-month. The Department's net capacity position was that it paid \$132,427 during 2007. 80% of this net cost was primarily due to the termination of the Masspower contract effective September 1, 2007, where final outcome of two litigations are still uncertain pending appeal.

The Department executed several contracts for the sale of renewable certificates through the

Nepool-GIS market system. These transactions brought in \$11,225 of revenues through selling CT Class 2 and ME respective renewable portfolio standard market requirements. Several 2007 calendar year certificates were banked to allow for sale during 2008.

Reliability Must Run (RMR) Agreements have been setup by ISO-NE to pay generators determined to be necessary for system reliability sufficient costs that don't recover their costs through the standard energy, capacity, and ancillary markets. Presently, there are four such RMR Agreements within this region Berkshire, Pittsfield, W. Spfld 3, and W. Spfld GT1/GT2. Based on settlement agreements that were negotiated on HG&E's behalf by MMWEC, FERC ordered revised annual requirements for all of these resources. HG&E received refunds during April through August 2007 in the amount of around \$850,000 for amounts previously paid between May 2005 and March 2007. 2006 RMR costs were \$1.489M, while a credit of \$63k resulted during 2007. RMR costs for 2008 are now on the order of around \$500k.

Significant transmission improvements made by the Department during the 2005 and 2006 calendar years, resulted in a 36% increase to the Department's annual revenue requirements through the ISO-NE for regional network service from \$825k to \$1,122k. This benefit of transmission ownership completed mitigated, at least for 2007, the Department's exposure to the increasing costs of transmission construction throughout New England of which HG&E's portion went from \$1.41M to \$1.66M.

The Department continued to explore other power supply options to meet its future needs, including repowering Cabot Station, purchasing interest in existing plants for sale or new peaking plants with lower debt service costs, and through additional or expanded renewable or alternative resources.

A table of the Department's power resources follows on the opposite page.

Supply

2007 POWER SUPPLY RESOURCES

PROJECT NAME	FUEL TYPE	PROJECT START DATE	CONTRACT CAPACITY (kW)		CONTRACT END DATE
			WINTER	SUMMER	
BASE UNITS					
NYPA FIRM	HYDRO	1985	2,662	2,662	9/1/25
MASSPOWER	GAS	1993	9,157	7,781	8/31/07***
MILLSTONE 3 - MIX 1	NUCLEAR	1986	1,327	1,327	11/25/45 *
MILLSTONE 3 - PROJ 3	NUCLEAR	1986	2,313	2,313	11/25/45 *
SEABROOK - MIX 1	NUCLEAR	1990	137	137	3/31/30 *
SEABROOK - PROJ 4	NUCLEAR	1990	3,080	3,080	3/31/30 *
SEABROOK - PROJ 5	NUCLEAR	1990	380	380	3/31/30 *
INTERMEDIATE UNITS					
HYDRO QUEBEC 1	N/A	1986	1,204	1,784	LOU **
HYDRO QUEBEC 2	N/A	1989	1,962	2,906	LOU **
W.F. WYMAN 4	#2 OIL	1978	4,267	4,229	LOU *
PEAKING UNITS					
HOLYOKE #6 & #8	#2 OIL, #6 OIL, GAS	1951	19,306	19,306	OWNED *
HOLYOKE #9	#2 OIL, #6 OIL, GAS	1941	3,500	3,500	OWNED *
NYPA PEAK	HYDRO	1985	578	578	9/1/25
STONYBROOK GT 2A	#2 OIL	1982	2,409	1,842	LOU *
STONYBROOK GT 2B	#2 OIL	1982	2,409	1,842	LOU *
HYDRO UNITS					
HADLEY FALLS 1&2	HYDRO	1949	33,400	33,400	OWNED *
RIVERSIDE 8	HYDRO	1931	4,500	4,500	OWNED *
RIVERSIDE 4-7	HYDRO	1921	3,435	3,435	OWNED *
BOATLOCK	HYDRO	1924	3,094	3,094	OWNED *
HOLYOKE HYDRO / CABOT 1-4	HYDRO	1923	3,147	3,147	OWNED *
CHEMICAL	HYDRO	1935	1,600	1,600	OWNED *
BEEBE HOLBROOK	HYDRO	1948	586	586	OWNED *
SKINNER	HYDRO	1924	280	280	OWNED *
VALLEY HYDRO	HYDRO	2004	790	790	OWNED *
ALBION A	HYDRO	2004	281	281	OWNED *
ALBION D	HYDRO	2004	395	395	OWNED *
CROCKER AB	HYDRO	2004	370	370	OWNED *
CROCKER C	HYDRO	2004	230	230	OWNED *
GILL A	HYDRO	2004	450	450	OWNED *
GILL D	HYDRO	2004	330	330	OWNED *
MT. TOM	HYDRO	2004	473	473	OWNED *
NONOTUCK	HYDRO	2004	472	472	OWNED *
OPEN SQUARE	HYDRO	2004	600	600	YR TO YR
SONOCO PRODUCTS	HYDRO	2005	300	300	YR TO YR

(All capacity contracts follow the ISO New England calendar system)
 * - Investments continue for the life of the unit (LOU)
 ** - After 8/31/01, there is no firm energy contract, only capacity entitlement which continues for life of unit
 *** - Contract terminated as of this date

UNITS WERE ACQUIRED
EFFECTIVE 12/1/2004

telecom

Telecom Division

In 2007, twenty-six new customer sites were added to the HGE.net fiber optic and wireless networks. In addition, 14 existing customers upgraded to a higher level of service. A summary of the Division's major accomplishments follows:

Network Upgrades

In 2007, a plan was completed to upgrade the customer network to a Metro Ethernet (MetroE) / MPLS network design. The Telecom Division is in the process of evaluating and testing equipment from several vendors to determine which offers the most cost-effective upgrade path.

A new Cisco 7606 Aggregation router was installed and tested. This device allows for the addition of increased internet bandwidth to the HGE.net network. In addition, CALEA Lawful Intercept (wire tapping) devices were installed at both HGE.net internet gateways in compliance with new federal regulations.

Chicopee Fiber Services

Installation of fiber optic switching equipment facilitated the offering of fiber optic services in Chicopee. These services are provided in cooperation with Chicopee Electric Light (CEL) utilizing their existing fiber optic ring. A sales and marketing effort was completed to inform Chicopee businesses of these services. Three customer sites were connected as a result of these efforts.

Consulting Services

The Telecom Division has responsibility for ongoing maintenance, installation and applications operation of the City's network. In 2007, the Division installed a new Email system, a new Network Management Server, and an automatic backup system. A complete reconstruction of the City Hall data center was also conducted.

Municipal Camera System

The Department has worked in conjunction with the Holyoke Police Department to create a municipal camera system throughout the downtown area. The Telecom Division, working with the Electric Division, is responsible for designing and engineering all facets of the system deployment including custom fabrication of hardware. The cameras are centrally monitored from the Police Department's 911 Dispatch Center.

In 2007, five new surveillance camera locations were added to this system.

Enterprise Network

In addition to provisioning and maintaining retail internet customers, the Telecom Division is also responsible for the design, operation and maintenance of the Department's internal network and Information Systems needs. A summary of those accomplishments follows:

- Installation of IP-based security alarms at several hydroelectric production locations, and continued development of networked recording system for video surveillance cameras.
- Migrated the Department's data storage needs to a distributed Network Attached Storage (NAS) solution, adding redundancy and improved disaster recovery capabilities.
- Offered continued support to the Electric Division's industrial customer meter network and the Division's SCADA system.



The Department provides telecommunications services under the trade name HGE.net

goodwill

Community Goodwill

Community involvement is a central belief of the public power philosophy, and the Department is proud of the role it takes in making Holyoke a better place to call home.

In 2007, HG&E offered support to several major community events including the Hispanic Family Festival, the St. Patrick's Day Parade, and the Holyoke Fireworks, which is underwritten by the department. In total, over \$73,000 in sponsorships, and over \$16,000 in labor was provided for nonprofit causes.

Neil J. Moriarty, Jr. Scholarship for Cadet Engineers

The Cadet Engineer program was dedicated in memory of our late Commission Chairperson, Neil J. Moriarty, Jr. He often noted that the admission of new students into the program was one of most rewarding actions that the Commission made each year.

The program offered aid to 3 Holyoke students in 2007 who are pursuing a Bachelor of Science in Engineering. The Commission voted to admit Timothy Coogan, Logan Greaney, and Sarah LaRose were admitted as new participants in this program in 2007.

Summary of Community Support

Nonprofit Sponsorships	\$73,611
Nonprofit Labor	16,239
Cadet Engineer Program	41,250
Payment in Lieu of Taxes	\$808,320
Municipal Payment Discounts	304,333
Discounted Street Lighting	587,556*
Economic Dev. Discounts	\$91,231
New Homeowner Discounts	112,865
Energy Conservation Programs	68,000
Energy Conservation Assistance Programs	\$571,150**
Total Community Support	\$2,674,555

Economic Development

In 2007, the Department provided \$91,231 in additional discounts to businesses that have relocated or expanded within the City under the Economic Development Discount Program. This program provides an additional 10% off their gas and electric bills for a 3 year period.

The Department also offers a similar program for residential customers, under which first-time Holyoke homebuyers can receive 10 percent off their first three years of gas and electricity bills. In 2007, the Department provided \$112,865 in additional discounts under this program.

HG&E also promotes economic growth through our Commercial and Residential Energy Conservation Programs. These plans offer interest-free financial assistance to our customers, thus helping them make their homes or businesses more energy efficient. In 2007, the Department paid out over \$571,150 in zero-interest assistance to Holyoke home and business owners.

Municipal Benefits

The Department contributed \$808,320 to the City of Holyoke's General Fund during 2007 as an in-lieu of tax payment. Payment discounts of \$304,333 were provided on the City's utility accounts.

Beyond these direct financial benefits, HG&E continues to provide other valuable services to the City including: offering low-cost street lighting, low-cost maintenance on city-owned gas and electric equipment, and low municipal rates to City departments on their gas and electric accounts.

* Based on market average of 22.5¢/kWh vs. 9.21¢/kWh billed

** Programs that encourage conservation and economic development

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Lester Halpern & Company P.C.
Certified Public Accountants

Lester L. Halpern CPA • Robert B. McKay CPA • Thomas A. Terry CPA • Betty Jane Bourdon CPA • Mary-Anne S. Stearns CPA

INDEPENDENT AUDITOR'S REPORT

May 20, 2008

TO THE COMMISSIONERS
CITY OF HOLYOKE, MASSACHUSETTS
GAS AND ELECTRIC DEPARTMENT
Holyoke, Massachusetts 01040

We have audited the accompanying financial statements of the City of Holyoke, Massachusetts - Gas and Electric Department as of and for the years ended December 31, 2007 and 2006, as listed in the table of contents. These financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Gas and Electric Department and are not intended to present fairly the financial position of the City of Holyoke, Massachusetts and the results of its operations and cash flows of its proprietary fund types and nonexpendable trust funds in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Holyoke, Massachusetts - Gas and Electric Department as of December 31, 2007 and 2006, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Very truly yours,

Lester Halpern & Company P.C.

Certified Public Accountants

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Balance Sheets — December 31, 2007 and 2006

ASSETS		2007	2006
Plant, Property and Equipment:			
	Plant, property and equipment in service	\$146,336,353	\$143,675,274
	Construction in progress	<u>4,376,870</u>	<u>4,125,559</u>
		150,713,223	147,800,833
	Less accumulated depreciation	<u>65,539,005</u>	<u>65,202,909</u>
	<u>Total Plant, Property and Equipment</u>	<u>85,174,218</u>	<u>82,597,924</u>
Restricted Assets:			
	Funds required under bond indenture - held by trustee	3,363,576	3,192,932
	Funds required under bond indenture - other	10,207,828	10,511,418
	Customers' deposits	<u>494,039</u>	<u>466,363</u>
	<u>Total Restricted Assets</u>	<u>14,065,443</u>	<u>14,170,713</u>
Other Fund Reserves:			
	Purchased Power Funds	2,737,082	2,957,940
	Rate Stabilization Funds	<u>39,118,219</u>	<u>37,103,029</u>
	<u>Total Other Funded Reserves</u>	<u>41,855,301</u>	<u>40,060,969</u>
Current Assets:			
	Cash	15,000	15,000
	Operating Cash Invested	4,616,875	4,202,128
	Accounts receivable net of reserve for uncollectible accounts of \$400,000, 2007 and 2006	8,059,091	6,949,179
	Accounts receivable - City of Holyoke	469,688	653,471
	Materials and supplies	2,155,713	2,150,996
	Fuel for electric generation and gas in storage	2,347,699	3,254,939
	Prepaid expense	502,097	752,132
	Other receivables	1,441,415	1,579,101
	Deferred fuel costs		740,629
	Accrued interest receivable	<u>231,088</u>	<u>209,051</u>
	<u>Total Current Assets</u>	<u>19,838,666</u>	<u>20,506,626</u>
Other Assets:			
	Other investments	248,429	252,190
	Preliminary investigation charges		30,287
	Intangible assets	6,945,647	7,740,436
	Other receivables - after one year	<u>1,223,004</u>	<u>1,884,849</u>
	<u>Total Other Assets</u>	<u>8,417,080</u>	<u>9,907,762</u>
TOTAL ASSETS		<u>\$169,350,708</u>	<u>\$167,243,994</u>
LIABILITIES AND RETAINED EARNINGS			
Long-Term Liabilities:			
	Bonds payable - long-term	\$38,780,000	\$39,660,000
	Notes payable - long-term	3,567,939	4,098,342
	Leases payable - long-term	116,065	83,144
	Accrued compensated absences	2,047,133	1,960,862
	Accrued environmental costs	760,482	194,497
	Deferred rate stabilization costs	<u>30,990,290</u>	<u>32,240,290</u>
	<u>Total Long-Term Liabilities</u>	<u>76,261,909</u>	<u>78,237,135</u>
Current Liabilities:			
	Due to other funds	8,362,851	3,207,182
	Accounts payable	7,628,082	10,769,248
	Current portion bonds, notes and leases payable	1,463,353	1,417,925
	Customers' deposits	475,957	459,366
	Accrued liabilities	1,316,367	1,191,410
	Accrued interest	172,318	178,670
	Current portion - accrued compensated absences	261,809	332,600
	Current portion - accrued environmental costs	259,000	225,000
	Current portion - deferred rate stabilization costs	2,250,000	1,000,000
	Deferred credits - current	<u>237,672</u>	<u>202,289</u>
	<u>Total Current Liabilities</u>	<u>22,427,409</u>	<u>18,983,690</u>
Total Liabilities:		<u>98,689,318</u>	<u>97,220,825</u>
Retained Earnings:		<u>70,661,390</u>	<u>70,023,169</u>
TOTAL LIABILITIES AND RETAINED EARNINGS		<u>\$169,350,708</u>	<u>\$167,243,994</u>

See accompanying notes.

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Statement of Revenues, Expenses and Changes in Retained Earnings
December 31, 2007 and 2006

See accompanying notes.

	2007			2006		
	Gas	Electric / Steam Telecommunications	Total	Gas	Electric / Steam Telecommunications	Total
<u>Operating Revenues</u>	<u>\$27,895,210</u>	<u>\$47,906,761</u>	<u>\$75,801,971</u>	<u>\$29,349,086</u>	<u>\$45,691,885</u>	<u>\$75,040,971</u>
<u>Operating Expenses:</u>						
Cost of power, gas water and steam sold	21,886,660	30,016,532	51,903,192	23,508,605	24,530,983	48,039,588
Transmission	1,837,829	1,837,829	1,837,829	3,105,507	3,105,507	3,105,507
Distribution	4,130,971	6,713,617	6,713,617	2,563,165	3,390,778	5,953,943
Customer accounts	413,315	648,994	1,062,309	402,441	609,113	1,011,554
General and administrative	2,368,266	5,742,282	8,110,548	2,132,179	5,540,981	7,673,160
Depreciation - plant and equipment	821,937	3,418,201	4,240,138	797,357	3,191,707	3,989,064
<u>Total Operating Expenses</u>	<u>28,072,824</u>	<u>45,794,809</u>	<u>73,867,633</u>	<u>29,403,747</u>	<u>40,369,069</u>	<u>69,772,816</u>
<u>Operating Income (Loss)</u>	<u>\$ -177,614</u>	<u>\$ 2,111,952</u>	<u>1,934,338</u>	<u>\$ -54,661</u>	<u>\$ 5,322,816</u>	<u>5,268,155</u>
<u>Other Revenues (Expenses):</u>						
Investment income			2,519,772			2,351,314
Net gain (loss) on investments			198,079			-329,953
Bond interest expense			-2,033,352			-1,953,200
Other interest expense			-217,530			-136,431
Miscellaneous income - net			614,964			654,620
Amortization			-124,676			-124,676
Impairment loss - Harris water rights			-670,115			-671,437
Net loss - plant retirements			-117,466			-181,250
Boiler demolition expense			-622,735			
Net gain - merchandise jobbing			49,417			62,254
Taxes - others			-84,155			-84,155
<u>Total Other Revenues (Expenses)</u>			<u>-487,797</u>			<u>-412,914</u>
<u>Income Before Operating Transfers</u>			<u>1,446,541</u>			<u>4,855,241</u>
Payment in lieu of taxes - City of Holyoke			-808,320			-808,320
<u>Net Income</u>			<u>638,221</u>			<u>4,046,921</u>
Retained Earnings - Beginning of Year			70,023,169			65,976,248
<u>Retained Earnings - End of Year</u>			<u>\$70,661,390</u>			<u>\$70,023,169</u>

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Statement of Cash Flows — December 31, 2007 and 2006

	2007	2006
<u>Cash Flows from Operating Activities:</u>		
Cash received from customers	\$ 76,158,822	\$ 70,774,311
Cash paid to suppliers	-60,276,737	-46,745,292
Cash paid to employees	-10,437,954	-9,797,830
In lieu of taxes paid	-808,320	-808,320
Interest paid	-17,373	-16,433
<u>Net Cash Provided by Operating Activities</u>	<u>4,618,438</u>	<u>13,406,436</u>
<u>Cash Flows from Investing Activities:</u>		
Proceeds from sale of investments	13,668,847	14,933,150
Purchase of investments	-16,978,924	-14,925,473
Net transfer from restricted assets and other fund reserves	578,641	2,708,022
Investment income	2,497,735	2,209,895
Decrease (increase) in invested cash	829,464	-2,016,706
Net advance to (payment from) customers	105,656	-276,824
<u>Net Cash Provided by Investing Activities</u>	<u>701,419</u>	<u>2,605,064</u>
<u>Net Cash Provided by (Used in) Noncapital Financing Activities</u>		
Increase (decrease) in due to other funds	<u>5,155,669</u>	<u>-1,898,224</u>
<u>Cash Flows from Capital and Related Financing Activities:</u>		
Investment in plant, property and equipment	-6,854,084	-10,454,091
Payments on bonds, notes and leases payable	-1,411,868	-1,336,204
Interest paid on bonds, notes and leases payable	-2,239,861	-2,292,694
Decrease (increase) in preliminary investigation charges	30,287	-30,287
<u>Net Cash Used in Capital and Related Financing Activities</u>	<u>-10,475,526</u>	<u>-14,113,276</u>
<u>Increase (decrease) in Cash</u>		
Cash - beginning of year	15,000	15,000
<u>Cash - End of Year</u>	<u>\$15,000</u>	<u>\$15,000</u>
<u>Supplemental Cash Flow Information:</u>		
Total interest paid	<u>\$ 2,257,294</u>	<u>\$ 2,309,127</u>
<u>Supplemental Noncash Financing Activity:</u>		
Equipment acquired under capital lease	<u>\$ 79,813</u>	<u>\$ 95,360</u>

See accompanying notes.

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Schedule of Reconciliation of Operating Income to Net Cash
Provided by Operating Activities — December 31, 2007 and 2006

	2007	2006
Operating Income	<u>\$ 1,934,338</u>	<u>\$ 5,268,155</u>
 <u>Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities</u>		
Depreciation	4,240,138	3,989,064
Other interest expense	-17,373	-16,433
Other non-operating income	664,381	716,874
Boiler Demolition Expense	-622,735	
Payment in lieu of taxes and other property taxes	-892,475	-892,475
Changes in operating assets and liabilities		
(Increase) decrease - accounts receivable	-926,129	1,453,335
- materials and supplies	-4,717	-259,709
- fuel for electric generation and gas in storage	907,240	-387,207
- prepaid expense	250,035	-270,808
- deferred fuel costs	740,629	24,831
- other receivables	693,875	-1,181,544
Increase (decrease) - accounts payable	-3,141,165	3,662,136
- customer deposits	16,591	-4,987
- accrued liabilities	124,957	86,353
- accrued compensated absences	15,480	252,522
- deferred rate stabilization costs		1,383,021
- accrued environmental costs	599,985	-609,711
- deferred credits	<u>35,383</u>	<u>193,019</u>
 <u>Total Adjustments</u>	 <u>2,684,100</u>	 <u>8,138,281</u>
 <u>Net Cash Provided by Operating Activities</u>	 <u>\$ 4,618,438</u>	 <u>\$ 13,406,436</u>

See accompanying notes.

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1.0 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Nature of Business - The financial statements present information on the activities of the Gas and Electric Department (the Department), an Enterprise Fund of the City of Holyoke, Massachusetts (the City). The Department provides gas, electric, water, telecommunications and steam services to its customers, substantially all of whom are local residents and commercial and industrial businesses. Approximately 53% of the Department's revenues are derived from its electric division. The Department is subject to regulation by the Federal Energy Regulatory Commission (FERC), the Massachusetts Department of Public Utilities (DPU), and the Massachusetts Department of Telecommunication & Cable (DTC).

Accounting Method - The financial statements are prepared on the accrual basis. The Department applies all Governmental Accounting Standards Board (GASB) pronouncements as well as the Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

Expense Allocation - Expenses associated with a particular division are charged to that division. For the years ended December 31, 2007 and 2006, shared expenses including administrative and supporting costs are allocated to each division as follows:

Gas	35.0%
Electric, Steam and Telecommunications	65.0%

Use of Estimates - The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Plant, Property and Equipment - Additions to and replacements of plant, property and equipment are recorded at cost. The cost of plant, property and equipment retired, less accumulated depreciation and salvage, is charged against revenue in the year retired. The cost of repairs and minor renewals is charged to maintenance expense.

Depreciation - Depreciation of \$4,240,138 in 2007 and \$3,989,064 in 2006 is computed using the straight-line method. The composite rate for 2007 and 2006 is 3% of depreciable property in service. The composite rate is in accordance with Massachusetts Department of Public Utilities and Energy regulations.

Materials, Supplies and Fuel - Materials, supplies and fuel are valued at average cost.

Revenue Recognition - Operating revenues are recognized on the basis of cycle billings rendered monthly, net of discounts. Revenues are not accrued for services delivered beyond such cycle billing dates.

Discounts reported for the years ended December 31, 2007 and 2006 are as follows:

	2007	2006
Gas	\$ 2,207,321	\$ 2,534,191
Electric	3,504,055	3,565,773
Steam	<u>34,453</u>	<u>25,019</u>
Total	<u>\$ 5,745,829</u>	<u>\$ 6,124,983</u>

Income Taxes - Income of the Department is excluded from taxation by Section 115 of the United States Internal Revenue Code.

1.0 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (CONTINUED)

Investments - Investments totaling \$80,429 and \$84,190 in 2007 and 2006, respectively, represent the Department's equity in New England Hydro-Transmission Corporation and New England Hydro-Transmission Electric Company. These investments represent .2653 percent of the issued common stock of these untraded companies.

In addition, the Department has invested \$168,000 with the Public Utility Mutual Insurance Company (PUMIC). PUMIC was formed to provide general insurance to members of the Public Utility Risk Management Association (PURMA).

These investments are carried at original cost on the balance sheets. It was not practicable to estimate the fair value of these investments.

Investments in debt and equity securities are recorded at fair market value (See Note 5).

Interest Capitalized - The Department follows the policy of capitalizing interest as a component of the cost of plant, property and equipment in service constructed for its own use. During the years ended December 31, 2007 and 2006, the Department capitalized interest of \$-0- and \$218,851, respectively.

Intangible Assets - Intangible assets are recorded at cost. Intangible assets subject to amortization include debt issue costs, customer contracts, the franchise area fee associated with the December, 2001 hydroelectric project purchase, and the FERC licenses associated with the hydroelectric generating facilities purchased in November, 2004. Debt issue costs are being amortized on a straight-line basis over the term of the issue. Customer contracts, franchise and FERC licenses are being amortized on a straight-line basis over the remaining lives of the respective licenses. Intangible assets not subject to amortization include water rights acquired with the hydroelectric generating facilities purchased in November, 2004. These costs are evaluated annually for impairment.

Cash - For purposes of the statement of cash flows, cash includes cash on hand and cash in the Department's checking account.

Deferred Fuel Costs - The balance in deferred fuel costs represents actual costs in excess of billings, which can be recovered under purchase gas adjustment clauses. Included in deferred fuel costs at December 31, 2006 are the amounts the Department expected to bill and collect in 2007 for underbilled purchased gas costs previously incurred.

Environmental Matters - Expenditures that result from the remediation of an existing condition caused by past operations and that do not contribute to current or future revenues are expensed. Liabilities are recognized for remedial activities when the cleanup is probable and the cost can be reasonably estimated. Estimated liabilities are not discounted to present value.

Accounts Receivable - Accounts receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a charge to earnings and a credit to the valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

Advertising - The Department expenses the cost of advertising as incurred. Advertising expense was \$73,645 and \$86,046 for the years ended December 31, 2007 and 2006, respectively.

2.0 PLANT, PROPERTY AND EQUIPMENT IN SERVICE:

Plant, property and equipment in service consists of the following:

2007

	<u>Electric/ Telecommunications</u>	<u>Steam</u>	<u>Gas</u>	<u>Total</u>
Land	\$ 1,776,677	\$ 240,418	\$ 320,271	\$ 2,337,366
Plant Investment	94,628,281	16,421,928	\$ 25,436,941	136,487,150
Office Furniture and Equip.	1,810,330	24,580	923,988	2,758,898
Transportation Equip.	2,886,834	68,020	1,002,781	3,957,635
Other	608,199	18,510	168,595	795,304
Total	<u>\$ 101,710,321</u>	<u>\$ 16,773,456</u>	<u>\$ 27,852,576</u>	<u>\$ 146,336,353</u>

2006

	<u>Electric/ Telecommunications</u>	<u>Steam</u>	<u>Natural Gas</u>	<u>Total</u>
Land	\$ 1,776,677	\$ 240,418	\$ 320,271	\$ 2,337,366
Plant Investment	90,015,480	18,994,923	\$ 24,988,562	133,998,965
Office Furniture and Equip.	1,756,770	24,580	910,475	2,691,825
Transportation Equip.	2,805,246	68,020	958,378	3,831,644
Other	549,669	7,310	258,495	815,474
Total	<u>\$ 96,903,842</u>	<u>\$ 19,335,251</u>	<u>\$ 27,436,181</u>	<u>\$ 143,675,274</u>

3.0 CASH AND RESTRICTED ASSETS:

The Department participates in a cash and investment pool maintained by the City. In addition, the Department holds certain cash separately from the pool.

Custody and use of restricted assets are subject to requirements and restrictions imposed under contractual agreements, bond indentures, and the General Laws of the Commonwealth of Massachusetts, and are not available for normal operating purposes. Purchased power funds are on deposit with Massachusetts Municipal Wholesale Electric Company (MMWEC) to pay for energy and related services as required under existing agreements. Rate stabilization funds are amounts set aside to be used to stabilize current and future power costs.

4.0 DUE TO / FROM OTHER FUNDS:

"Due to/from other funds" represents the amount by which the Department's equity in pooled cash differs from the expenditures paid and receipts collected by the City.

5.0 INVESTMENTS IN DEBT AND EQUITY SECURITIES

The Department invests various funds in debt and equity securities which are held in the Department's name by UBS Financial Services Inc. All investments must be made in securities or deposits as authorized by Massachusetts General Laws, Chapters 54 and 55.

Investments are stated at fair value, which is the amount at which an investment could be exchanged in a current transaction between willing parties. Fair values are based on quoted market prices.

Net unrealized gain on investments at December 31, 2007 and 2006 is \$200,549 and \$32,354, respectively

Interest Rate Risk - Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Department does not have a formal investment policy that limits investment maturities.

At December 31, 2007, the Department's investments were as follows:

	Fair Value	Maturity in Years			
		Less Than 1	1-5	6-10	Over 10
Debt Securities:					
U.S. Agency Bonds	\$ 17,771,079	\$ 149,813	\$ 4,454,786	\$ 10,627,974	\$ 2,538,506
Municipal Securities	1,600,000				1,600,000
Corporate Bonds and Notes	1,960,764		424,404	1,536,360	
Asset Backed and Preferred Securities	1,015,783				1,015,783
	<u>22,347,626</u>	<u>\$ 149,813</u>	<u>\$ 4,879,190</u>	<u>\$ 12,164,334</u>	<u>\$ 5,154,289</u>
Other Investments:					
Equity Mutual Funds	5,216,789				
Fixed Income Mutual Funds	1,504,287				
Cash, Certificates of Deposit and Money Market Funds	750,475				
Preferred Securities	200,300				
	<u>\$ 30,019,477</u>				

At December 31, 2006, the Department's investments were as follows:

	Fair Value	Maturity in Years			
		Less Than 1	1-5	6-10	Over 10
Debt Securities:					
U.S. Agency Bonds	\$ 17,990,536	\$ 6,970,970	\$ 4,252,008	\$ 4,294,866	\$ 2,472,692
Municipal Securities	795,000				795,000
Corporate Bonds and Notes	1,484,802		518,360	538,102	428,340
Asset Backed Securities	474,682				474,682
	<u>20,745,020</u>	<u>\$ 6,970,970</u>	<u>\$ 4,770,368</u>	<u>\$ 4,832,968</u>	<u>\$ 4,170,714</u>
Other Investments:					
Equity Mutual Funds	2,807,678				
Fixed Income Mutual Funds	1,428,070				
Cash, Certificates of Deposit and Money Market Funds	3,349,052				
	<u>\$ 28,329,820</u>				

5.0 INVESTMENTS IN DEBT AND EQUITY SECURITIES (CONTINUED)

Credit Risk - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Department does not have a separate formal policy regarding credit risk.

As of December 31, 2007 and 2006, the Department's investments were rated as follows:

	2007		2006	
	Standard & Poor's	Moody's Investment Service	Standard & Poor's	Moody's Investment Service
U.S. Agency Bonds	AAA	Aaa	AAA	Aaa
Municipal Securities	AAA to A	Aaa to A3	AAA to A	Aa1 to A2
Corporate Bonds and Notes	A+ to B-	A1 to Caa1	A to BBB	A2 to Baa3
Preferred Securities	A to A-	A1 to A2	N/A	N/A
Fixed Income Mutual Funds	AA to B	N/A	N/A	N/A

Custodial Credit Risk

Deposits - Custodial credit risk is the risk that the Department's deposits may not be returned to the Department. As of December 31, 2007 and 2006, \$750,475 and \$3,349,052, respectively were uninsured and uncollateralized and subject to custodial credit risk.

Investments - For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Department will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. The Department's investment policy addresses credit risk by defining allowable investments.

Concentration of Credit Risk - Concentration of credit risk is the risk of loss attributed to the magnitude of the Department's investment in a single issuer.

At December 31, 2007 and 2006, the Department's investment portfolio was concentrated as follows:

Issuer	Investment Type	Percentage of Portfolio	
		2007	2006
Federal National Mortgage Assn.	U.S. Agency Security	14.09%	16.25%
Federal Home Loan Bank	U.S. Agency Security	18.82%	33.45%
Federal Home Loan Mortgage	U.S. Agency Security	16.99%	13.81%
Federal Farm Credit Bank	U.S. Agency Security	7.93%	

The investments are included on the Balance Sheet as follows:

	2007	2006
Funds required under bond indenture - other	\$ 3,000,000	\$ 3,000,000
Customers' deposits	476,952	450,437
Rate stabilization funds	21,925,650	20,677,255
Operating cash invested	4,616,875	4,202,128
	<u>\$ 30,019,477</u>	<u>\$ 28,329,820</u>

In addition, rate stabilization funds of \$17,192,569 at December 31, 2007 and \$16,425,774 at December 31, 2006 are on deposit with and are invested through the Massachusetts Municipal Wholesale Electric Company (MMWEC). These funds are reported on the Balance Sheet at market value.

6.0 RETIREMENT PLANS

Contributory Plan - Substantially all full-time employees participate in the Holyoke Contributory Retirement System, a cost sharing multiple employer public employee retirement system. The system is partially funded by employee contributions.

The plan provides pension benefits, deferred allowances and death and disability benefits. A member may retire after reaching age 55 with 10 years of creditable service, or with no age requirement after 20 years of service. Members become vested after ten full years of creditable service.

Retirement allowance is based on the following factors: age, length of creditable service, level of salary, and group classification. Age at retirement and group classification determine a benefit rate. This rate, multiplied by the length of creditable service, is multiplied by the average of the three highest (consecutive) years' compensation. Percentages are specified in Chapter 32 of the Massachusetts General Laws. Participants may elect to receive their retirement in one of three optional forms of payment.

Member employers are required by state statutes to make contributions to the plan. Contributions are determined by the Commonwealth of Massachusetts Division of Public Employee Retirement Administration (PERA). The Department's contributions charged to expense for the years ended December 31, 2007, 2006 and 2005, are \$2,329,371, \$2,036,052 and \$1,799,395, respectively. The total contribution figure represents approximately 21%, 20% and 24% of covered payroll for the years ended December 31, 2007, 2006 and 2005, respectively. Total payroll for the same periods was approximately \$10,979,128, \$10,417,981, and \$7,637,500, respectively. The Department's contributions for the years ended December 31, 2007, 2006 and 2005 was 19.8%, 18.8% and 18.6%, respectively, of the total contributions for all employers covered by the plan.

Covered employees are required by state statute to contribute a fixed percentage of their earnings into the plan. The percentage varies from 5 to 9 percent depending upon date of hire. All employees hired after January 1, 1979 contribute an additional 2% on all gross regular earnings over \$30,000 per year. Employee contributions for the years ended December 31, 2007, 2006 and 2005 are \$844,501, \$807,504 and \$753,529, respectively.

The plan issues a publicly available financial report that includes financial statements and required supplementary information. This report may be obtained by writing or calling the plan as follows:

Attn: Daniel Owens, Executive Director
Holyoke Retirement Board
City Hall Annex - Room 207
Holyoke, Massachusetts 01040
(413) 534-2179

Noncontributory Plan - Employees hired prior to January 1, 1938, participate in the noncontributory pension plan. The Department is required by state statutes to pay benefits as the obligation arises. Benefits are established by state statutes. The Department's contributions for the years ended December 31, 2007, 2006 and 2005 are \$20,397, \$19,675 and \$19,675, respectively.

7.0 POST-RETIREMENT HEALTH CARE AND LIFE INSURANCE BENEFITS

The Department provides health care and life insurance benefits to retirees, their dependents, or their survivors. These benefits are provided through the City's group plans. The cost of these benefits are included in the total cost of benefits for both active and retired employees. The total cost of providing these benefits to retirees was \$532,975 in 2007 and \$518,232 in 2006. There were 108 retirees covered by the plan in 2007 and 111 retirees covered by the plan in 2006.

8.0 CONCENTRATIONS OF CREDIT RISKS:

At December 31, 2007 and 2006, the Department had amounts on deposit with a bank which exceeded FDIC insurance limits by \$720,835 and \$1,448,560, respectively.

In the ordinary course of business, the Department extends unsecured credit to its regular customers. Amounts outstanding at December 31, 2007 and 2006 were \$8,928,779 and \$8,002,650, respectively.

Sources of Labor Supply - Sixty-four percent of the Department's labor force is covered under a collective bargaining agreement between the City of Holyoke Gas and Electric Department and the Holyoke Municipal Gas, Light & Power Guild, Inc. The agreement was extended through March 31, 2011.

The Department had one customer that accounted for 72% and 87% of steam sales in 2007 and 2006, respectively. There were no steam sales receivables outstanding from this customer at December 31, 2007 or 2006.

9.0 ELECTRIC POWER PURCHASES:

Electric Power Purchases were as follows:

	2007	2006
Masspower	\$ 2,812,326	\$ 4,113,619
MMWEC - NYPA	154,271	139,585
MMWEC - Wyman No. 4	468,814	186,756
MMWEC - Nuclear Mix No. 1	2,487,105	2,272,230
MMWEC - Nuclear Project No .3	2,542,520	2,522,614
MMWEC - Nuclear Project No. 4		-40,111
MMWEC - Nuclear Project No. 5		-12,176
MMWEC - Stony Brook / Peaking	155,516	150,890
MMWEC - Special Project 2006A	112,700	75,667
NEPEX - Net of Sales	7,189,673	-681,371
Short-term Power Supply - net of Hydro Sales	2,340,818	2,181,482
	<u>\$ 18,263,743</u>	<u>\$ 10,909,185</u>
Rate stabilization reserve used during current year	<u>-1,000,000</u>	
	<u>\$ 17,263,743</u>	<u>\$ 10,909,185</u>

10.0 DEFERRED RATE STABILIZATION COSTS

During 2003, the Department began to set aside funds which will be used for rate stabilization in the development of future rates and allow the Department to remain competitive when (if) deregulation goes into effect. In addition, the Department set aside funds received from the buyout of a power contract from Select Energy during 2005. These funds will be used to stabilize future power costs.

Amounts set aside are as follows:

	2007	2006
Balance - beginning of year	\$ 33,240,290	\$ 31,857,269
Current year's expense set aside	1,000,000	1,383,021
Amounts used during current year	<u>-1,000,000</u>	
Balance - end of year	<u>\$ 33,240,290</u>	<u>\$ 33,240,290</u>

11.0 BONDS PAYABLE:

	Balance Outstanding		Interest Expense	
	2007	2006	2007	2006
Bond payable - 2001 Series A				
Date of issue: December 13, 2001				
Interest rates:				
2002-2008 4.00%				
2009-2010 5.00%				
2011-2018 5.375%				
2019-2031 5.00%				
	\$ 39,660,000	\$ 40,505,000	\$ 2,033,352	\$ 2,077,200
Less - amount due within one year	<u>880,000</u>	<u>815,000</u>		
Bonds Payable - Due After One Year	\$ 38,780,000	\$ 39,660,000		

Principal maturing and interest payments are anticipated to be as follows:

	Principal	Interest	Total
2008	\$ 880,000	\$ 2,007,866	\$ 2,887,866
2009	915,000	1,971,788	2,886,788
2010	960,000	1,925,850	2,885,850
2011	1,010,000	1,877,326	2,887,326
2012	1,060,000	1,822,815	2,882,815
2013-2017	6,235,000	8,189,686	14,424,686
2018-2022	8,065,000	6,354,648	14,419,648
2023-2027	10,295,000	4,111,355	14,406,355
2028-2031	<u>10,240,000</u>	<u>1,268,583</u>	<u>11,508,583</u>
	<u>\$ 39,660,000</u>	<u>\$ 29,529,917</u>	<u>\$ 69,189,917</u>

The Department is required to satisfy certain bond covenant requirements in connection with the bonds payable. The following funds are required as part of the Bond agreements:

	2007	2006
Debt Service Fund:		
The debt service fund represents amounts held by a trustee to provide for debt service payments.	\$ 142,681	\$ 106,888
Debt Service Reserve Fund:		
The debt service reserve fund represents amounts held by a trustee in order to provide a reserve for the payment of the principal or redemption price and interest on the Bonds.	3,220,895	3,086,044
Operating Expense Fund:		
The operating expense fund is held by the City of Holyoke and represents an amount sufficient to pay only the operating expenses of the Department for the next succeeding month.	7,207,828	7,511,418
Operation and Maintenance Reserve Fund:		
The operation and maintenance reserve fund is invested with other funds as described in Note 5.	3,000,000	3,000,000

12.0 NOTES PAYABLE

	2007	2006
Note payable to bank, secured by revenues of the Department (subject to existing pledge of revenues under the Revenue Bonds 2001 Series A), monthly payments of \$19,508 including interest at 4.15% for a five year period commencing November, 2003 (monthly payments and interest rate to be adjusted thereafter to \$20,590 and 5.25%, respectively through March, 2013 and \$20,868 and 5.75%, respectively through maturity date), matures October, 2018	\$ 2,033,270	\$ 2,178,490
Note payable to bank, secured by revenues of the Department (subject to existing pledge of revenues under the Revenue Bonds 2001 Series A), monthly payments of \$39,123 including interest at 4.39%, matures November, 2012	<u>2,065,073</u>	<u>2,433,692</u>
	4,098,343	4,612,182
<u>Less</u> -Amount due within one year	<u>530,404</u>	<u>513,840</u>
Notes Payable - Due After One Year	<u>\$ 3,567,939</u>	<u>\$ 4,098,342</u>

Principal maturing and interest payments are anticipated to be as follows:

	Principal	Interest	Total
2008	\$ 530,404	\$ 181,798	\$ 712,202
2009	553,049	163,469	716,518
2010	579,543	136,975	716,518
2011	607,315	109,203	716,518
2012	591,562	80,363	671,925
2013-2017	1,033,280	217,501	1,250,781
2017-2018	<u>203,190</u>	<u>5,459</u>	<u>208,649</u>
	<u>\$ 4,098,343</u>	<u>\$ 894,768</u>	<u>\$ 4,993,111</u>

13.0- CAPITAL LEASES PAYABLE

	2007	2006
Capital lease payable to Deere Credit, Inc. in monthly installments of \$2,180 including interest at 3.90%, secured by equipment, matures April, 2008	\$ 8,650	\$ 33,936
Capital lease payable to Richo Corp. in monthly installments of \$355 including interest at 10%, secured by equipment, matures February, 2009	4,651	7,948
Capital lease payable to Richo Corp. in monthly installments of \$223 including interest at 13%, secured by equipment, matures February, 2009	2,867	4,984
Capital lease payable to IBM Credit LLC in monthly installments of \$2,166 including interest at 4.3%, secured by equipment, matures December, 2010	73,033	95,361
Capital lease payable to Municipal Services Group, Inc. in monthly installments of \$18,140 including interest at 4.42%, secured by equipment, matures December, 2012	<u>79,813</u>	<u>142,229</u>
	169,014	59,085
<u>Less</u> - amount due within one year	<u>52,949</u>	<u>59,085</u>
Lease Payable - Due After One Year	<u>\$ 116,065</u>	<u>\$ 83,144</u>

13.0- CAPITAL LEASES PAYABLE (CONTINUED)

The following is a schedule of future minimum lease payments under capital leases together with the present value of the net minimum lease payments as of December 31, 2007:

2008	\$ 59,786
2009	45,288
2010	44,132
2011	18,140
2012	<u>18,140</u>
	185,486
Less - amount representing interest	16,472
Present value of future minimum lease payments	<u>\$ 169,014</u>

Leased assets recorded under plant, property and equipment include:

Backhoes	\$ 119,050
Copiers	26,305
IBM Server	95,361
Dump truck	<u>79,813</u>
	320,529
	<u>133,847</u>
Less - accumulated depreciation	<u>\$ 186,682</u>

14.0 OPERATING LEASE PAYABLE

In March, 2006, the Department entered into a four year lease on a copier. Monthly payments are \$329. The lease expires February, 2010 and has a fair market value purchase option.

In March, 2006, the Department entered into a three year lease on a copier. Monthly payments are \$65. The lease expires May, 2009 and has a fair market value purchase option.

In September, 2003, the Department entered into a three year lease on a computer. Monthly payments were \$1,986. The lease expired September, 2006 and had a fair market value purchase option.

Lease expense for the years ended December 31, 2007 and 2006 was \$4,728 and \$21,814, respectively.

15.0 ACQUIRED INTANGIBLE ASSETS

Amortized Intangibles:

	Life in Years	2007		2006	
		Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Debt issue costs	30	\$ 1,297,211	\$ 261,604	\$ 1,297,211	\$ 218,364
Customer contracts and franchise fees	30	2,000,000	403,334	2,000,000	336,667
License fees	16	<u>240,000</u>	<u>45,538</u>	<u>240,000</u>	<u>30,769</u>
		<u>\$ 3,537,211</u>	<u>\$ 710,476</u>	<u>\$ 3,537,211</u>	<u>\$ 585,800</u>

Unamortized Intangibles:

	2007 Fair Value	2006 Fair Value
Water rights	<u>\$ 4,118,912</u>	<u>\$ 4,789,025</u>

15.0 ACQUIRED INTANGIBLE ASSETS (CONTINUED)

Aggregate amortization expense was \$124,676 for the years ended December 31, 2007 and 2006. Estimated aggregate amortization expense is \$124,676 for each of the next five years.

In accordance with SFAS No. 142 "Goodwill and Other Intangible Assets" water rights were tested for impairment by comparing their fair value to their carrying value. The fair value was established based upon a combination of the discounted cash flows, projected output, and projected market value of output. Using this procedure, the carrying value of the water rights exceeded its fair value creating an impairment loss of \$670,115 and \$671,437 for the years ended December 31, 2007 and 2006, respectively, which is shown separately on the Statement of Revenues, Expenses and Changes in Retained Earnings.

16.0 RELATED PARTY TRANSACTIONS:

The Department provides gas, electric and steam sales and service, as well as, telecommunication services to the City of Holyoke. Total sales were \$3,632,696 and \$3,727,778 for the years ending December 31, 2007 and 2006, respectively. Amounts due from the City totaled \$469,688 and \$653,471 at December 31, 2007 and 2006, respectively.

The Department has also recorded contributions in lieu of taxes to the City of Holyoke of \$808,320 for the years ended December 31, 2007 and 2006.

17.0 COMMITMENTS AND CONTINGENCIES:

Purchased Power Contracts:

Masspower - During 1989, a contract was signed with Masspower, through MMWEC, for approximately 9.157 MW during the winter and 7.781 MW during the summer per year starting in 1993 until July 31, 2013. Annual charges will be approximately \$5 million depending on level of dispatch of the facility. During 2006, MMWEC filed a civil action against Masspower. The court ruled in favor of Masspower and MMWEC has appealed this decision. In addition, in July, 2007, MMWEC terminated the contract for material breach. Masspower filed a civil action against MMWEC and in January, 2008 the court ruled in favor of MMWEC. Masspower has appealed this decision. It is unknown at this time how the outcome of this litigation will affect future contract terms (including pricing).

Short-term power - On a continuing basis, the Department also enters into several short-term power supply contracts for either the purchase or sale of capacity, energy, or ancillary services with various suppliers.

MMWEC Special Project 2006A - In August, 2006, the Department executed a Participation Acknowledgement Certificate and Project Development Agreement (PDA) with MMWEC for all pre-development costs associated with its share of a new generating facility to meet a projected future need of baseload energy and capacity. The Department agreed to 17,000 kW of winter-rated capacity and associated energy from this new facility. Under the PDA, the Department's cost range is between \$308,000 and \$476,000 depending on the participation rate and ultimate size of the plant. It is not expected that this plant would be operational until about June, 2011.

Telecommunications Contracts - The Department has entered into long-term contracts for dedicated point-to-point data lines and Internet Access services from several companies. These contracts have five to ten year terms. In addition the Department has entered into one-year contracts with two companies for frame relay lines, dialup help desk support and dedicated line monitoring services.

In 2006, the Department entered into an agreement with the City of Chicopee Electric Light Department (CEL) to offer and provide telecommunication services to Chicopee residents and businesses. The Department will pay CEL \$250 per month for each connection, as well as, all costs to connect to customer facilities. This agreement is for an initial term of six years.

17.0 COMMITMENTS AND CONTINGENCIES: (CONTINUED)

Telecommunications Contracts (continued) - In 2002, the Department entered into a lease with Fiber Technologies Networks, LLC (Fibertech) for use of the Department's fiber optic lines. The lease provides for an annual payment per route mile for 20 years with an option to renew for an additional five years.

MMWEC - General - The Department is a Participant in certain Projects of the Massachusetts Municipal Wholesale Electric Company (MMWEC), a public corporation and a political subdivision of the Commonwealth of Massachusetts. Currently, the Department is a member of MMWEC on a month to month basis. Any decision regarding membership status will have no effect on the Department's commitments and contingencies on MMWEC projects in existence prior to the Department's membership termination.

MMWEC was created as a means to develop bulk power supply for its Members and Project Participants. MMWEC is authorized to construct, own or purchase ownership interests in and to issue revenue bonds to finance electric facilities (Projects). MMWEC has acquired ownership interests in electric facilities operated by other utilities and also operates its own electric facilities. MMWEC sells all of the capability of each of its Projects to its Members and other utilities (Project Participants) under Power Sales Agreements (PSAs). Among other things, the PSAs require each Project Participant to pay its pro rata share of MMWEC's costs related to the Project, which costs include debt service on bonds issued by MMWEC to finance the Project, plus 10% of MMWEC's debt service to be paid into a Reserve and Contingency Fund. In addition, should any Project Participant fail to make any payment, other Project Participants may be required to increase (step-up) their payments and correspondingly their Participants' share of Project Capability to an additional amount not to exceed 25% of their original Participants' share of the Project Capability. Project Participants have covenanted to fix, revise and collect rates at least sufficient to meet their obligations under the PSAs.

The Department has entered into Power Sales Agreements (PSAs) and Power Purchase Agreements (PPAs) with MMWEC. Under both the PSAs and PPAs, the Department is required to make certain payments to MMWEC payable solely from the Department's revenues. Under the PSAs, each participant is unconditionally obligated to make payments due to MMWEC whether or not the Project(s) is completed or operating and notwithstanding the suspension or interruption of the output of the Project(s).

MMWEC operates the Stony Brook Intermediate Project and Stony Brook Peaking Project fossil-fueled power plants, (the latter which the Department has a 4.818 MW share). In addition, MMWEC has a 3.7% interest in the W.F. Wyman Unit No. 4 plant owned and operated by FPL Energy Wyman IV, a subsidiary of FPL Energy, Inc. and a 4.8% ownership interest in the Millstone Unit 3 nuclear unit operated by Dominion Nuclear Connecticut, Inc. (DNCI) a subsidiary of Dominion Resources, Inc. In addition to Millstone Unit 3, DNCI also is the owner of Millstone Unit 2. DNCI requested and received an exemption from the Nuclear Regulatory Commission (NRC) enabling them to submit an application earlier than 20 years before the expiration of the operating license for Unit 3 so that DNCI could submit its application for license renewal for Unit 2 and Unit 3 at the same time. In November, 2006, the NRC renewed the operating licenses for Unit 2 and Unit 3 for an additional twenty years. The license for Unit 2 was extended to July 31, 2035 and the license for Unit 3 was extended to November 25, 2045.

A substantial portion of MMWEC's plant investment and financing program is an 11.6% ownership interest in the Seabrook Station nuclear generating unit operated by FPL Energy Seabrook, LLC, an indirect subsidiary of FPL Group, Inc. In December, 2006, the NRC issued an amendment to the operating license that extends the expiration date from October, 2026 to March, 2030 to recapture the period from 1986 to 1990 during which time Seabrook Station had an operating license but did not operate. FPL Energy Seabrook, LLC intends to request an extension of the Seabrook Station operating license beyond March, 2030. Pursuant to the PSAs, the MMWEC Seabrook and Millstone Project Participants are liable for their proportionate share of the costs associated with decommissioning the plants, which is being funded through monthly Project billings. The Project Participants are also liable for their proportionate share of the uninsured costs of a nuclear incident that might be imposed under the Price-Anderson Act. In July, 2006, as part of the Energy Policy Act of 2006, Congress extended the Price-Anderson Act through the end of 2025.

17.0 COMMITMENTS AND CONTINGENCIES: (CONTINUED)

MMWEC - General (continued) - MMWEC represents certain municipal light plants, including the Department, with respect to the Hydro Quebec-Phase II project (Project). The Department is an equity participant in the Project. The agreements which comprise the Project include requirements that the participant make equity contributions, provide credit support and furnish certain guarantees. In addition, the Project contains a step-up mechanism which requires participants to assume obligations of other participants who are in default, subject to certain limitations. The Department's potential liability cannot be reasonably estimated at this time.

As of December 31, 2007, total capital expenditures by MMWEC amounted to \$1,538,931,000 of which \$44,018,000 represents the amount associated with the Department's Project Capability. MMWEC's debt outstanding for the Projects includes Power Supply System Revenue Bonds totaling \$641,630,000 of which \$21,432,000 is associated with the Department's share of Project Capability. As of December 31, 2007, MMWEC's total future debt service requirement on outstanding Bonds issued for the Projects is \$763,040,000, of which \$25,099,000 is anticipated to be billed to the Department in the future.

The estimated aggregate amount of the Department's required payments under the PSAs and PPAs, exclusive of the Reserve and Contingency Fund billings, to MMWEC at December 31, 2007 and estimated for future years is shown below:

For the years ended December 31, 2008	3,367,000
2009	3,149,000
2010	2,940,000
2011	2,885,000
2012	2,889,000
2013-2017	9,706,000
2018-2019	162,000
	<u>\$25,099,000</u>

In addition, the Department is required to pay its share of the operation and maintenance (O&M) costs of the Projects in which they participate. The Department's total O&M costs including debt service under the PSAs were \$5,929,000 and \$5,499,000 for the years ended December 31, 2007 and 2006, respectively.

Deregulation - In 1997, legislation was passed mandating retail wheeling of electricity for private electric utilities. If the Department opts to open its borders, it will no longer have a franchise area and all utilities may have the ability to enter into contracts to provide electricity generation to any customer. The potential impact on the Department's revenue from retail competition cannot be reasonably estimated at this time.

Hydroelectric Facility - As part of the Department's purchase of hydroelectric generating assets and a distribution franchise in 2001, FERC required certain modifications to the hydroelectric facility. The cost of these modifications over ten years is likely to exceed ten million dollars.

Self Insurance - For general liability purposes, the Department is self-insured up to \$50,000, has self-insurance trust coverage in the amount of \$400,000 and general liability insurance for \$50,000 to \$10,000,000 per occurrence. The Department is also self insured for workers compensation up to \$250,000 per occurrence. A policy is in effect for excess workers compensation.

Environmental Protection and Other Issues - The United States Environmental Protection Agency (EPA) has determined that a release of hazardous substances under the Comprehensive Response, Compensation and Liability Act (CERCLA) has occurred at the Rose Chemical Site in Holden, Missouri (Site) and that there is a substantial threat of further release of hazardous substances at the Site. Polychlorinated biphenyls (PCB) shipped by the Department to the Site for disposal may not have been disposed of properly, which creates the potential for liability under CERCLA. The manner in which PCB and PCB items are stored or otherwise located at the Site and the abandonment of the Site by Martha C. Rose Chemicals, Inc. creates the potential for further liability. The Department entered into two separate Buyout Agreements in 1988 and 1989 which terminated the Department's liability, except under limited circumstances.

17.0 COMMITMENTS AND CONTINGENCIES: (CONTINUED)

MMWEC - General (continued) - MMWEC represents certain municipal light plants, including the Department, with respect to the Hydro Quebec-Phase II project (Project). The Department is an equity participant in the Project. The agreements which comprise the Project include requirements that the participant make equity contributions, provide credit support and furnish certain guarantees. In addition, the Project contains a step-up mechanism which requires participants to assume obligations of other participants who are in default, subject to certain limitations. The Department's potential liability cannot be reasonably estimated at this time.

As of December 31, 2007, total capital expenditures by MMWEC amounted to \$1,538,931,000 of which \$44,018,000 represents the amount associated with the Department's Project Capability. MMWEC's debt outstanding for the Projects includes Power Supply System Revenue Bonds totaling \$641,630,000 of which \$21,432,000 is associated with the Department's share of Project Capability. As of December 31, 2007, MMWEC's total future debt service requirement on outstanding Bonds issued for the Projects is \$763,040,000, of which \$25,099,000 is anticipated to be billed to the Department in the future.

The estimated aggregate amount of the Department's required payments under the PSAs and PPAs, exclusive of the Reserve and Contingency Fund billings, to MMWEC at December 31, 2007 and estimated for future years is shown below:

18.0 PRIOR PERIOD RECLASSIFICATION

Prior year's financial statements have been reclassified to conform with the current year's presentation. The reclassification has no effect on the previously reported net income for the year ended December 31, 2006.

Lester Halpern & Company P.C.
Certified Public Accountants

Lester L. Halpern CPA • Robert B. McKay CPA • Thomas A. Terry CPA • Betty Jane Bourdon CPA • Mary-Anne S. Stearns CPA

**INDEPENDENT AUDITOR'S REPORT
ON SUPPLEMENTAL INFORMATION**

May 20, 2008

TO THE COMMISSIONERS
CITY OF HOLYOKE, MASSACHUSETTS
GAS AND ELECTRIC DEPARTMENT
Holyoke, Massachusetts 01040

Our report on our audit of the basic financial statements of City of Holyoke, Massachusetts Gas and Electric Department for 2007 and 2006 appears on page 1. That audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The information on pages 23 through 24 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, such information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Very truly yours,

Lester Halpern & Company P.C.
Certified Public Accountants

GAS DIVISION	2007	2006
Operating Revenues:		
Residential	\$ 10,356,264	\$ 11,120,355
Commercial	9,357,127	10,122,423
Industrial	2,470,344	2,645,180
Municipal	717,679	828,963
Department sales	4,188,296	4,632,165
Sales for resale	805,500	
<u>Total Operating Revenues</u>	<u>\$ 27,895,210</u>	<u>\$ 29,349,086</u>
Cost of Gas Sold:		
Purchases - natural gas	\$ 19,643,090	\$ 21,851,042
Liquid natural gas processed	1,160,093	406,719
Environmental response	862,872	1,150,500
Supplies and expenses	220,605	100,344
<u>Total Cost of Gas Sold</u>	<u>\$ 21,886,660</u>	<u>\$ 23,508,605</u>
Distribution:		
Salaries and wages		
- system control and load dispatch	\$ 369,814	\$ 407,514
- supervision and engineering	345,791	394,347
- customer installation	481,095	430,267
- operation	300,180	209,470
- maintenance	458,538	555,745
Supplies and expenses	627,228	565,822
<u>Total Distribution</u>	<u>\$ 2,582,646</u>	<u>\$ 2,563,165</u>
Customer Accounts:		
Salaries and wages		
- meter reading	\$ 79,700	\$ 86,595
- accounting and collection	129,793	114,458
Supplies and expenses	11,777	15,200
Uncollectible accounts	192,045	186,188
<u>Total Customer Accounts</u>	<u>\$ 413,315</u>	<u>\$ 402,441</u>
General and Administrative:		
Salaries	\$ 599,310	\$ 621,870
Pensions and benefits	1,274,983	1,118,583
Insurance	136,547	120,392
General supplies and expenses	357,426	271,334
<u>Total General and Administrative</u>	<u>\$ 2,368,266</u>	<u>\$ 2,132,179</u>

ELECTRIC, STEAM AND TELECOMMUNICATIONS DIVISIONS

	2007	2006
Operating Revenues:		
Electric Sales-		
Residential	\$ 11,881,876	\$ 11,503,870
Commercial	19,606,126	18,766,620
Industrial	5,937,978	5,684,924
Municipal	2,465,589	2,403,618
Water	5,827	8,096
Cobble Mountain operation - net	421,183	276,557
Steam sales	5,990,112	5,629,487
Telecommunication sales	<u>1,598,070</u>	<u>1,418,713</u>
Total Operating Revenues	<u>\$ 47,906,761</u>	<u>\$ 45,691,885</u>
Cost of Electricity/Steam/Water Sold:		
Purchases - electricity	\$ 17,263,743	\$ 10,909,185
Replacement power	1,000,000	1,383,021
Fuel for electric generation	149,561	602,195
Salaries and wages - production	1,486,850	1,418,650
- maintenance	1,114,832	1,141,202
Supplies and expenses	2,569,201	2,333,215
Cost of water sold	504,439	481,569
Cost of steam sold	<u>5,927,906</u>	<u>6,261,946</u>
Total Cost of Electricity Sold	<u>\$ 30,016,532</u>	<u>\$ 24,530,983</u>
Electric Transmission:		
Salaries and wages	\$ 523,999	\$ 241,735
Supplies and expenses	83,879	110,942
Transmission by others	<u>1,229,951</u>	<u>2,752,830</u>
Total Electric Transmission	<u>\$ 1,837,829</u>	<u>\$ 3,105,507</u>
Distribution:		
Electric-		
Salaries and wages - lines, equipment and street lights	\$ 1,521,646	\$ 1,482,598
- customer installations	218,069	241,236
Supplies and expenses	1,216,074	545,367
Steam Distribution	98,967	233,567
Telecommunications distribution	<u>1,076,215</u>	<u>888,010</u>
Total Distribution	<u>\$ 4,130,971</u>	<u>\$ 3,390,778</u>
Customer Accounts:		
Electric-		
Salaries and wages - meter reading	\$ 145,687	\$ 132,557
- accounting and collection	241,044	212,565
Supplies and expenses	22,806	39,010
Uncollectible accounts	239,065	223,646
Telecommunications customer accounts	<u>392</u>	<u>1,335</u>
Total Customer Accounts	<u>\$ 648,994</u>	<u>\$ 609,113</u>
General and Administrative:		
Electric-		
Salaries	\$ 964,362	\$ 951,746
Pensions and benefits	2,102,060	2,038,678
Insurance	480,342	497,253
General supplies and expenses	1,428,065	1,456,045
Steam general and administrative	397,960	349,970
Telecommunications general and administrative	<u>369,493</u>	<u>247,289</u>
Total General and Administrative	<u>\$ 5,742,282</u>	<u>\$ 5,540,981</u>

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