HUDSON RIVER-BLACK RIVER REGULATING DISTRICT
(A DISCRETELY PRESENTED COMPONENT UNIT OF THE STATE OF NEW YORK)

Financial Statements
June 30, 2008 and 2007
Together with
Independent Auditors' Report

Bonadio & Co., LLP
Certified Public Accountants

HUDSON RIVER-BLACK RIVER REGULATING DISTRICT
(A DISCRETELY PRESENTED COMPONENT UNIT OF THE STATE OF NEW YORK)

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Bonadio & Co., LLP
Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

October 14, 2008

To the Board of Directors of
Hudson River-Black River Regulating District:

We have audited the accompanying financial statements of the business-type activities of Hudson River-Black River Regulating District (the Regulating District), a New York Public Benefit Corporation, which is a component unit of the State of New York, as of and for the year ended June 30, 2008 as listed in the table of contents. These financial statements are the responsibility of the management of the Regulating District. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Regulating District as of June 30, 2007, were audited by other auditors whose report dated August 16, 2007, expressed an unqualified opinion on those statements.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Regulating District as of June 30, 2008 and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States.

The Management's Discussion and Analysis on pages 2 through 6 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the basic financial statements. The accompanying supplemental combining information included in Schedules I and II is presented for purposes of additional analysis and is not a required part of the basic financial statements. These schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

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This Management Discussion and Analysis (MD&A) of Hudson River-Black River Regulating District (the Regulating District) provides an introduction to the major activities and operations of the Regulating District and an introduction and overview to the Regulating District's financial performance and statements for the fiscal years ended June 30, 2008 and 2007.

Following this MD&A are the basic financial statements of the Regulating District together with the notes thereto, which are essential to a full understanding of the data contained in the financial statements. The information contained in the MD&A should be considered in conjunction with the information contained in the Financial Statements and the Notes to Financial Statements.

REGULATING DISTRICT ACTIVITIES

The Regulating District was created in 1959 when the New York State Legislature passed legislation (Article 15 Title 21 of the Environmental Conservation Law) combining the Hudson River Regulating District, founded in 1922, and the Black River Regulating District, founded in 1919. Both were created to regulate the flow of the waters of New York State's two great neighboring watersheds.

The legislation charged the Regulating District with regulating the flow of the two rivers as required by the public welfare including health and safety. Specifically, the Regulating District's responsibilities involve reducing floods caused by excess run-off, and augmenting river flow at times of drought or other periods when normal river flows are low. Organized as a public benefit corporation, the Regulating District was given a broad spectrum of legal powers to accomplish this mission, including the authority to build and operate reservoirs, issue bonds, and apportion costs on its beneficiaries to finance construction, maintenance, and operation of its reservoirs.

The Regulating District's operations are conducted under two regional operating units - one for the Black River area and another for the Hudson River area - each with segregated budgets. The management of both regions is vested in a seven-member Board appointed by the governor. The mission of the Regulating District is to regulate the flows of the Hudson River and Black River for the purposes of flood protection and flow augmentation**.** The Regulating District Board formulates policies to accomplish its mission at Great Sacandaga Lake, providing flood protection and low flow augmentation through reservoir releases in accordance with the Upper Hudson/Sacandaga Offer of Settlement; at Indian Lake, Stillwater Reservoir, Old Forge and Sixth Lake, providing storage during periods of high flow and augmenting flows during periods of low flow; operating a data-gathering system for precipitation, stream flow, snow depth and flood conditions; providing the public with information pertinent to its mission; operating and maintaining facilities; maintaining a sound financial status for Regulating District operations; managing the lands of the State of New York under the Regulating District's jurisdiction; and promulgating rules and regulations necessary to fulfilling its mission.

The Regulating District receives its primary funding from statutory beneficiaries, comprised of hydroelectric power generators, industrial operations and municipalities that directly benefit from augmented river flow and flood protection. These beneficiaries are annually assessed their proportional share of Regulating District operating expenses. A secondary revenue source comes from hydropower agreements that provide annual revenue in exchange for the ability to utilize headwater on Regulating District-administered state land for hydroelectric generating purposes. A third source of revenue, in the Hudson River area only, is the Sacandaga Lake Access Permit System, which generates revenue equal to the cost to operate the Great Sacandaga Lake Permit System.

FACILITIES

Hudson River Area Facilities: The Regulating District administers the lands of the State of New York that constitute the Great Sacandaga Lake (Sacandaga Reservoir) as well as its shoreline, and issues annual revocable permits to eligible property owners for access to the lake across State land. The lake, impounded behind the Conklingville Dam, is the heart of Regulating District operations in the 8,300 square mile Hudson-Sacandaga area. The Regulating District also owns and operates Indian Lake Reservoir and Dam.

Black River Area Facilities: In the Black River drainage area of 1,916 square miles, the Regulating District operates reservoirs and dams at Stillwater, Old Forge, and Sixth Lake.

Administrative Offices: The Regulating District's main office occupies leased space in Albany. A Regulating District-owned building in Mayfield houses the branch office for the Hudson-Sacandaga area. A branch office for the Black River area occupies rented space in Watertown.

OPERATIONS SUMMARY

The Regulating District's scope of operations and concomitant costs (in 000s) tend to be relatively stable from year to year:

	Black River Area			Hudson River Area		
	2008	2007	2006	2008	2007	2006
Operating revenues	$ 965	$ 969	$ 880	$ 5,846	$ 5,798	$ 5,452
Operating expenses	(1,135)	(930)	(677)	(6,728)	(5,456)	(5,369)
Operating income (loss)	(170)	39	203	(882)	342	83
Net non-operating revenue (expense)	186	179	(87)	128	153	(459)
Net income (loss)	$ 16	$ 218	$ 116	$ (754)	$ 495	$ (376)

The consolidated Regulating District revenues are derived from three primary sources. The financing of the two areas is accomplished independently because operating costs of each are recovered from two different sets of statutory beneficiaries, hydropower (or water usage) agreements and, in the Hudson River area only, the Great Sacandaga Lake Permit System. Statutory beneficiaries in both watersheds are assessed proportional shares of all other budgeted operating and overhead costs, after deducting the estimated revenue from the hydropower agreements, permit system revenue, and estimated interest income. The Regulating District is currently in the process of determining the cost of the Permit System pursuant to the costing methodology recommended to the Board by an outside consultant. Revenue from statutory beneficiaries, hydropower agreements, and permit holders is reliably adequate to balance the Regulating District's annual budget.

Operating expenses fall into four major categories: property taxes, personnel expenses, engineering and maintenance, and administrative overhead. While other expenses remain fairly stable, engineering and maintenance costs vary from year to year depending on a number of factors that affect our reservoirs, dams, and shoreline. These factors include, but are not necessarily limited to, weather, environmental protection and remediation, regulatory requirements, and recreational use of facilities. Since it is the dams that make possible the Regulating District's regulating of reservoir levels and river flows, and which restrain water to prevent flooding, maintenance of these dams is the Regulating District's primary activity.

OPERATIONS SUMMARY (Continued)

There were several material year over year operating expense variances worth noting. For fiscal year 2006 versus 2007, salaries increased approximately $306k or 22%. The reason for this increase was largely due to the filling of open positions such as Licensed Land Surveyor, General Counsel, and Plant Operator. Also, professional fees decreased approximately $41k or 9% due to the reduced activities of the Regulating District's Permit System Rulemaking Project initiated in 2006. Finally, erosion control decreased approximately $45k or 125% due to an increase in rip rap purchases during fiscal year 2006/2007 in anticipation of the need to place additional stone in response to significant erosion created by the Flood Emergency of June 2006. Also, there was $13.5k in non-rip rap expenditures during that same period.

For fiscal year 2007 versus 2008, materials and supplies increased approximately $64k or 38%. Several small projects, including the roof replacement of the Black River Field Office at the Stillwater Dam facility and installation of security cameras at the Conklingville Dam, contributed largely to this increase. Additionally, contractual services increased approximately $126k or 14% due to several Federal Energy Regulatory Commission (FERC) mandated projects requiring engineering services work. The largest of those contributed to 90% of the increase and included the Conklingville Dam Gate Intake Repair project, Dam Breach Analysis, and Dam Vent/Siphon, and Trash Rack Feasibility study and Ice Sluice Analysis.

The Regulating District maintains board restricted reserve funds to minimize the effect that budget fluctuations would have on the statutory beneficiaries that provide its primary funding. These reserve funds absorb operating surpluses in lower expense years, and provide a means of funding operating deficits in high expense years – an effective means of assessment stabilization. Current reserves represent 30% of the total Regulating District unrestricted net assets designated by the Board.

Contributing somewhat to annual imbalances between revenues and expenses has been the Regulating District’s legislative mandate to adopt three-year budgets. While multi-year budgets, with revenues assessed equally for three years, serve to stabilize assessments during the budget cycle, they also tend toward surplus early in the multi-year cycle, and deficit in the final year.

BALANCE SHEET SUMMARY (000s)

	2008	2007	2006
Buildings	$ 937	$ 937	$ 937
Building improvements, furniture and equipment	752	673	650
Vehicles	819	761	657
Construction in progress	629	635	-
Dam structures	14,118	14,118	14,118
Cost of capital assets	17,255	17,124	16,362
Less: Accumulated depreciation	(12,955)	(12,701)	(12,459)
Net book value of capital assets	4,300	4,423	3,903
Current assets	6,691	6,219	6,162
Total assets	10,991	10,642	10,065
Less: Liabilities	(2,076)	(989)	(1,125)
Net assets	$ 8,915	$ 9,653	$ 8,940

BALANCE SHEET SUMMARY (Continued)

This analysis reflects the Regulating District's stable financial position. Asset growth generally occurs in governmental units when 1) cash assets are accumulated, and/or 2) debt is used to finance acquisition or construction of fixed (durable) assets such as equipment, furniture, land, buildings, major improvements that extend the life of a fixed asset, or leasehold improvements.

Asset shrinkage occurs when 1) accumulated cash assets are used for expenses that exceed revenues, and/or 2) assets acquired during the year cost less than "depreciation."

The Regulating District's reserve funds for repairs and assessment stabilization. The Regulating District is managing its financial position by currently appropriating accumulated surpluses to minimize assessment increases to statutory beneficiaries. The effect on the balance sheet is to reduce cash assets.

During the past year, the cost of assets acquired totaled less than depreciation expense, decreasing the book value of assets. Growth of fixed assets in a governmental unit is not necessarily an indicator of financial condition, nor is negative fixed asset growth necessarily an indicator of financial deterioration.

For the Regulating District, the stability in its balance sheet reflects the current adequacy of its fixed assets, and the conservative management of its cash assets to minimize increases in assessments and fees.

DEBT

The Regulating District's anticipated Capital Plan expenditures and current operations budget is sufficient. Accordingly, the Board does not contemplate incurring debt for the current budget cycle.

FINANCIAL CONDITION

The financial position of the Regulating District remains stable and healthy. Likewise, operating results remain predictable and within an acceptable range of budget variance.

During the current fiscal year ended June 30, 2008, the Regulating District implemented Governmental Accounting Standards Board Statement No. 45 (GASB No. 45). This implementation changed the accounting for other post employment health benefits from a "pay as you go" method of recognition to an accrual-basis measurement and recognition. In 2008, an additional cost of $1.7 million for post retirement health insurance was recognized, less approximately $337 thousand paid to current retirees, resulting in a net liability for future benefits of $1.4 million. The post employment health benefits and corresponding expense represent the main increase in operating expenses in 2008.

Despite the stability of its operations, the Regulating District is functioning in a dynamic fiscal environment. The statutory beneficiaries have remained largely unchanged since the creation of the Regulating District. However, since 2000 and every year thereafter to date, a statutory beneficiary has commenced proceedings against the Regulating District challenging the Regulating District's apportionment of cost. The statutory beneficiary argues that there are other entities benefitting from the Regulating District that are not apportioned a share of its costs. The suit seeks changes in future assessments as well as refund of allegedly over-charged assessments for pervious years. As described in Note 8 in the notes to the financial statements, this litigation may impact future operating statements, but the affect cannot be reasonably estimated at this time.

REQUESTS FOR INFORMATION

The accompanying financial statements are designed to provide detailed information on the Regulating District's operations to all those with an interest in the Regulating District's financial affairs. Questions concerning any of the information provided in this report, or any request for additional information, should be addressed to the Chief Fiscal Officer, Hudson River-Black River Regulating District, 350 Northern Boulevard, Albany, New York 12204.

HUDSON RIVER-BLACK RIVER REGULATING DISTRICT
(A DISCRETELY PRESENTED COMPONENT UNIT OF THE STATE OF NEW YORK)

STATEMENT OF NET ASSETS
JUNE 30, 2008 AND 2007

	2008	2007
ASSETS		
CURRENT ASSETS:		
Cash	$ 2,580,479	$ 2,182,619
Investments	3,632,547	3,424,868
Accounts receivable	5,125	127,765
Prepaid expenses	472,487	484,045
Total current assets	6,690,638	6,219,297
CAPITAL ASSETS, net	4,300,207	4,423,084
Total assets	10,990,845	10,642,381
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable	39,766	34,643
Compensated absences	358,940	417,139
Current portion of settlement payable	227,334	227,333
Current portion of other post employment benefits	371,279	-
Current portion of due to New York State Retirement System	33,336	38,048
Total current liabilities	1,030,655	717,163
SETTLEMENT PAYABLE, net of current portion	-	227,334
OTHER POST EMPLOYMENT BENEFITS, net of current portion	1,000,469	-
DUE TO NEW YORK STATE RETIREMENT SYSTEM, net of current portion	45,109	45,109
Total liabilities	2,076,233	989,606
NET ASSETS		
INVESTED IN CAPITAL ASSETS	4,300,207	4,423,084
UNRESTRICTED NET ASSETS	4,614,405	5,229,691
Total net assets	$ 8,914,612	$ 9,652,775

The accompanying notes are an integral part of these statements.

HUDSON RIVER-BLACK RIVER REGULATING DISTRICT
(A DISCRETELY PRESENTED COMPONENT UNIT OF THE STATE OF NEW YORK)

STATEMENT OF REVENUE, EXPENSES AND CHANGE IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2008 AND 2007

	2008	2007
OPERATING REVENUE:		
Assessments	$ 5,355,871	$ 5,361,186
Water power service	1,011,678	982,212
Permit fees	414,194	423,681
Other	29,207	3,014
Total operating revenue	6,810,950	6,770,093
OPERATING EXPENSES:		
Personnel services and employee benefits	3,929,343	2,608,754
Repairs and maintenance	55,356	81,620
Material and supplies	231,603	167,264
Real estate taxes	2,377,231	2,391,985
Contractual services	1,015,372	889,060
Depreciation	254,629	247,732
Total operating expenses	7,863,534	6,386,415
Total operating income (loss)	(1,052,584)	383,678
NON-OPERATING REVENUE:		
Interest and dividend income	314,421	328,861
Total non-operating revenue	314,421	328,861
CHANGE IN NET ASSETS	(738,163)	712,539
NET ASSETS - beginning of year	9,652,775	8,940,236
NET ASSETS - end of year	$ 8,914,612	$ 9,652,775

The accompanying notes are an integral part of these statements.

HUDSON RIVER-BLACK RIVER REGULATING DISTRICT
(A DISCRETELY PRESENTED COMPONENT UNIT OF THE STATE OF NEW YORK)

STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2008 AND 2007

	2008	2007
CASH FLOW FROM OPERATING ACTIVITIES:		
Revenues -		
Cash received from assessments	$ 5,478,511	$ 5,236,774
Cash received from water power service	1,011,678	982,212
Cash received from permit fees	414,194	423,681
Other cash receipts	29,207	3,014
Expenses -		
Payments to vendors and suppliers for goods and services	(3,890,215)	(3,780,511)
Payments to employees	(2,620,505)	(2,465,510)
Net cash flow from operating activities	422,870	399,660
CASH FLOW FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Purchases of capital assets	(131,752)	(767,922)
Net cash flow from capital and related financing activities	(131,752)	(767,922)
CASH FLOW FROM INVESTING ACTIVITIES		
Proceeds from sales of investments	-	390,677
Purchases of investments	(207,679)	(174,784)
Interest and dividends received	314,421	328,858
Net cash flow from investing activities	106,742	544,751
CHANGE IN CASH	397,860	176,489
CASH - beginning of year	2,182,619	2,006,130
CASH - end of year	$ 2,580,479	$ 2,182,619
CASH FLOW FROM OPERATING ACTIVITIES:		
Operating income	$ (1,052,584)	$ 383,678
Adjustments to reconcile operating income to net cash flow from operating activities:		
Depreciation	254,629	247,732
Changes in:		
Accounts receivable	122,640	(124,412)
Prepaid expenses	11,558	27,426
Accounts payable	5,123	(50,675)
Settlement payable	(227,333)	(227,333)
Compensated absences	(58,199)	150,229
Other post employment benefits obligation	1,371,748	-
Due to New Yok State Retirement System	(4,712)	(6,985)
Net cash flow from operating activities	$ 422,870	$ 399,660

The accompanying notes are an integral part of these statements.

1. ORGANIZATION AND REPORTING ENTITY

Hudson River-Black River Regulating District (the Regulating District) was created in 1959 under Article 15, Title 21 of the Environmental Conservation Law, which combined two organizations, the Black River Regulating District (formed in 1919) and the Hudson River Regulating District (formed in 1922). The Regulating District is a New York State public benefit corporation that is mandated to regulate stream flows as required by public welfare, including health and safety. The regulation of stream flows into the two watershed areas is the mission of the consolidated organization. The day-to-day operation of the two areas is conducted independently, because they are not physically related or connected in any way. Accordingly, the financing of the two areas is accomplished independently, because operating costs of each are recovered from two different sets of statutory beneficiaries, hydropower (or water power) agreements and, in the Hudson River area, the Great Sacandaga Lake Permit System. Each watershed area has its own operating personnel; however, a common professional staff serves both. Overall direction is supplied by a board appointed by the Governor of New York State.

The Regulating District is a component unit of the State of New York and, as such, is included in the State's general purpose financial statements. The Regulating District's financial statements include all operations for which the Regulating District has financial accountability.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The accompanying basic financial statements of the Regulating District have been prepared in conformity with accounting principles generally accepted in the United States for governments as prescribed by the Governmental Accounting Standards Board (GASB), which is the primary standard setting body for establishing governmental accounting and financial reporting principles. The Regulating District is engaged only in business-type activities as defined in GASB Statement No. 34. In compliance with GASB Statement No. 20, the Regulating District applies all applicable GASB pronouncements as well as Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions, issued on or before November 30, 1989 unless these pronouncements conflict with or contradict GASB pronouncements.

The operations of the Regulating District are reported as a proprietary fund and, as such, are accounted for on a flow of economic resources measurement focus and the accrual basis of accounting. Within this measurement focus, all assets and liabilities associated with operations are included on the balance sheet with revenues recorded when earned and expenses recorded at the time liabilities are incurred, regardless of when the cash is received or paid.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Basis of Presentation

GASB requires the classification of net assets into three components, as defined below:

- **Invested in capital assets, net of related debt** - consists of capital assets including restricted capital assets, net of accumulated depreciation, reduced by the outstanding balances of any bonds, notes or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. As of June 30, 2008 and 2007, the Regulating District did not have any debt.

- **Restricted net assets** - consists of net assets with constraints placed on their use either by (1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments; or (2) law through constitutional provisions or enabling legislation.

- **Unrestricted net assets** - all other net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt”.

Cash

The Regulating District’s monies must be deposited in FDIC insured commercial banks or trust companies located within the state. For the years ended June 30, 2008 and 2007, the Regulating District had funds held by New York State in Short Term Investment Pools (STIP). The Regulating District is not responsible for collateralizing the STIP funds. The Regulating District's cash in FDIC insured commercial banks, at times, may exceed federally insured limits. The Regulating District has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk with respect to cash.

Investments

The Regulating District’s investment policies comply with the New York State Comptroller’s guidelines for such policies. In addition, the Regulating District has its own written investment policy. Those policies permit investments in, among other things, obligations of the U.S. Treasury and its agencies and instrumentalities, certificates of deposit and obligations of the State of New York. Investments are recorded at amortized cost, which approximates market value and investment income is recorded in the statement of revenues, expenses and changes in net assets. Investments are in mutual funds with short term maturities and are reported as current assets in the statement of net assets.

Capital Assets

Capital assets are recorded at cost. Capital assets are defined as assets with initial, individual costs exceeding a capitalization threshold of $5,000 and useful life of two years or more. Depreciation is provided using the straight-line method over the following estimated useful lives:

Dam structures	100 years
Buildings and improvements	15 - 40 years
Equipment	5 - 7 years
Vehicles	5 years

Accrued Employee Benefits

It is the Regulating District’s policy to record employee benefits, including accumulated vacation and sick leave, as a liability. Regulating District employees are granted vacation in varying amounts. Upon retirement from the Regulating District, union employees are reimbursed for fifty percent of all accumulated sick days, up to a stated maximum, as specified in the collective bargaining agreement.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Budgets

By legislation, the Regulating District operates on a three-year cycle. Separate budgets are developed for the Hudson River area and Black River area since the cost of their respective operations is borne by a group of designated beneficiaries in each watershed. General administration costs, including Board expenses, are allocated on a proportionate basis to the two areas. The cost of operating the Permit System at the Great Sacandaga Lake is estimated for a three-year period. This involves allocating personnel salaries and benefits, as well as portion of facility and equipment costs to permit system operations.

Assessments

Resolutions are passed by the Regulating District's Board for both the Hudson River area and Black River area annual assessments at the June Board meeting. On July 1st of each year, assessments are billed, and on November 1st, a transmittal letter is sent to each town, city, or village informing it of each statutory beneficiary in their respective community who did not pay their assessment. Also on November 1st, a letter is sent to each county where a statutory beneficiary is located requesting it to charge unpaid assessments on the County's property tax levy for the subsequent year.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

3. CASH

Cash consisted of the following at June 30, 2008:

	Carrying Value	Bank Balance
Deposit accounts	$ 475,623	$ 630,216
	$ 475,623	$ 630,216

The Regulating District's cash deposits at June 30, 2008 were secured by the Federal Depository Insurance Corporation and uncollateralized, as follows:

FDIC	$ 221,233
Uncollateralized	408,983
	$ 630,216

Deposits held by New York State in Short Term Investment Pools (STIP) were $2,104,856 and $1,946,931 at June 30, 2008 and 2007, respectively.

4. INVESTMENTS

New York State statutes and guidelines, and the Regulating District's own investment policies, limit the investment of funds to obligations of the U.S. Government and its agencies, certificates of deposit and obligations of the State of New York. At June 30, 2008, investments include $3,632,547 of government mutual funds with short-term maturities, under a managed investments arrangement with Sentinel Funds. The Regulating District's investments are carried at amortized cost, which approximates market value. At June 30, 2007, investments included $3,424,868 under a similar investment management arrangement.

The Regulating District's investments are categorized in accordance with criteria established by GASB to give an indication of the level of risk assumed by the entity at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the Regulating District or its agent in the Regulating District's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counter parties trust department or agent in the Regulating District's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counter parties, or by their trust departments or agents but not in the Regulating District's name. All of the Regulating District's investments are classified in Category 1.

5. CAPITAL ASSETS

Capital assets consisted of the following at June 30:

	6/30/07	Additions	Deductions	6/30/08
Hudson River Area:				
Construction in progress	$ 635,155	$ -	$ (6,467)	$ 628,688
Total non-depreciable assets	$ 635,155	$ -	$ (6,467)	$ 628,688
Dam structures	$ 12,104,830	$ -	$ -	$ 12,104,830
Building	936,787	-	-	936,787
Building improvements	43,300	-	-	43,300
Office equipment	125,953	17,669	-	143,622
Other equipment	31,208	49,430	-	80,638
Vehicles	664,289	27,378	-	691,667
Total at cost	13,906,367	94,477	-	14,000,844
Less: Accumulated depreciation				
Dam structures	(9,685,062)	(120,085)	-	(9,805,147)
Building	(395,584)	(25,927)	-	(421,511)
Building improvements	(12,315)	(2,657)	-	(14,972)
Office equipment	(96,007)	(4,652)	-	(100,659)
Other equipment	(21,881)	(3,589)	-	(25,470)
Vehicles	(526,492)	(52,076)	-	(578,568)
Less: Accumulated depreciation	(10,737,341)	(208,986)	-	(10,946,327)
Total Hudson River Area depreciable assets, net	3,169,026	(114,509)	-	3,054,517
Black River Area:				
Dam structures	2,013,195	-	-	2,013,195
Building improvements	406,442	-	-	406,442
Equipment	58,884	13,256	-	72,140
Vehicles	96,906	30,486	-	127,392
Office equipment	6,736	-	-	6,736
Total at cost	2,582,163	43,742	-	2,625,905
Less: Accumulated depreciation				
Dam structures	(1,760,202)	(20,000)	-	(1,780,202)
Building improvements	(75,614)	(10,746)	-	(86,360)
Equipment	(54,099)	(2,214)	-	(56,313)
Vehicles	(73,345)	(12,683)	-	(86,028)
Less: Accumulated depreciation	(1,963,260)	(45,643)	-	(2,008,903)
Total Black River Area depreciable assets, net	618,903	(1,901)	-	617,002
Total depreciable assets, net	$ 3,787,929	$ (116,410)	$ -	$ 3,671,519
Total capital assets, net	$ 4,423,084	$ (116,410)	$ (6,467)	$ 4,300,207

5. CAPITAL ASSETS (Continued)

	6/30/06	Additions	Deductions	6/30/07
Hudson River Area:				
Construction in progress	$ -	$ 635,155	$ -	$ 635,155
Total non-depreciable assets	$ -	$ 635,155	$ -	$ 635,155
Dam structures	$ 12,104,830	$ -	$ -	$ 12,104,830
Building	936,787	-	-	936,787
Building improvements	43,300	-	-	43,300
Office equipment	109,927	16,026	-	125,953
Other equipment	31,208	-	-	31,208
Vehicles	560,349	103,940	-	664,289
Total at cost	13,786,401	119,966	-	13,906,367
Less: Accumulated depreciation				
Dam structures	(9,562,793)	(122,269)	-	(9,685,062)
Building	(372,164)	(23,420)	-	(395,584)
Building improvements	(11,232)	(1,083)	-	(12,315)
Office equipment	(86,356)	(9,651)	-	(96,007)
Other equipment	(19,547)	(2,334)	-	(21,881)
Vehicles	(483,258)	(43,234)	-	(526,492)
Total accumulated depreciation	(10,535,350)	(201,991)	-	(10,737,341)
Total Hudson River Area depreciable assets, net	3,251,051	(82,025)	-	3,169,026
Black River Area:				
Dam structures	2,013,195	-	-	2,013,195
Building improvements	406,442	-	-	406,442
Equipment	52,819	6,065	-	58,884
Vehicles	96,906	-	-	96,906
Office equipment	6,318	6,736	(6,318)	6,736
Total at cost	2,575,680	12,801	(6,318)	2,582,163
Less: Accumulated depreciation				
Dam structures	(1,741,452)	(18,750)		(1,760,202)
Building improvements	(63,283)	(12,331)	-	(75,614)
Equipment	(57,710)	(2,707)	6,318	(54,099)
Vehicles	(61,392)	(11,953)	-	(73,345)
Less: Accumulated depreciation	(1,923,837)	(45,741)	6,318	(1,963,260)
Total Black River Area depreciable assets, net	651,843	(32,940)	-	618,903
Total depreciable assets, net	$ 3,902,894	$ (114,965)	$ -	$ 3,787,929
Total capital assets, net	$ 3,902,894	$ 520,190	$ -	$ 4,423,084

Depreciation expense charged to operations for the year ended June 30 is as follows:

	2008	2007
Hudson River Area	$ 208,986	$ 201,991
Black River Area	45,643	45,741
Total capital assets	$ 254,629	$ 247,732

6. RETIREMENT SYSTEM

Plan Description

The Regulating District participates in the New York State and Local Employees' Retirement System (the System). This is a cost-sharing, multiple-employer retirement system. The System provides retirement benefits, as well as death and disability benefits. Obligations of employers and employees to contribute and benefits to employees are governed by the New York State Retirement and Social Security law (NYSRSSL). As set forth in NYSRSSL, the Comptroller of the State of New York (Comptroller) serves as sole trustee and administrative head of the System. The Comptroller shall adopt and may amend rules and regulations for the administration and transaction of the business of the System and for the custody and control of their funds. The System issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the New York State and Local Employees' Retirement Systems, 110 State Street, Albany, New York 12244.

Funding Policy

The System is non-contributory except for employees who joined the New York State and Local Employees' Retirement System after July 27, 1976, who contribute 3% of their salary for the first ten years of employment and nothing thereafter. Under the authority of NYSRSSL, the Comptroller shall certify annually the rates expressed as proportions of payroll of members, which shall be used in computing the contributions required to be made by employers to the Pension Accumulation Fund.

The Regulating District is required to contribute at an actuarially determined rate. The required contributions for the current year and two preceding years were:

2008	$	132,268
2007	$	138,925
2006	$	167,426

The Regulating District's contributions made to the System were equal to 100% of the contributions required for 2008 and 2007.

On May 14, 2003, Chapter 49 of the Laws of 2003 of the State of New York was enacted which made the following changes in the Systems:

- Requires minimum contributions by employers of 4.5% of payroll every year, including years in which the investment performance would make a lower contribution possible.
- Changes the cycle of annual billing such that the contribution for a given fiscal year will be based on the value of the pension fund on the prior to April 1st.

On July 30, 2004, Chapter 260 of the Laws of 2004 of the state of New York was enacted that allows local employers to bond or amortize a portion of their retirement bill for up to 10 years in accordance with the following schedule:

- For State fiscal year (SFY) 2004-05, the amounts in excess of seven percent of employees' covered salaries, with the first payment of those pension costs not due until the fiscal year succeeding that fiscal year in which the bonding/amortization was instituted.
- For SFY 2005-06, the amount in excess of 9.5% of employees' covered salaries.
- For SFY 2006-07, the amount in excess of 10.5% of employees' covered salaries.

The law required participating employers to make payments on a current basis, while bonding or amortizing existing unpaid amounts relating to the System's fiscal years ending March 31, 2005 through 2007.

6. RETIREMENT SYSTEM (Continued)

Funding Policy (Continued)

Chapter 260 of the Laws of New York State changed the annual payment due date for employers who participate in the New York State and Local Employees' Retirement System. The December 15 payment due date changed to February 1; however, employees were allowed to prepay their payment by December 15. The covered salary period (April 15 - March 31) will not change for the calculation.

7. NET ASSETS

The following is a description of unrestricted net assets designated by the Board:

- **Assessment Stabilization**
  $676,667 ($676,667 at June 30, 2007) has been designated for the purpose of stabilizing future assessments.

- **Capital Projects**
  $1,170,000 ($1,170,000 at June 30, 2007) has been designated for future capital projects.

- **Other**
  $413,282 ($413,282 at June 30, 2007) has been designated for legal, engineering and tax purposes.

8. CONTINGENCIES

Prior to 2006, the Regulating District was involved in litigation with two statutory beneficiaries. During 2006, a settlement was agreed to with one of the statutory beneficiaries requiring credits totaling $682,000 to be applied to the beneficiaries' future assessments in equal annual installments of $227,333 for the fiscal years ended June 30, 2007, 2008, and 2009. Additionally, the settlement requires that the Regulating District will apply $380,000 of the existing board designated existing Hudson River Stabilization fund to reduce future budgets in equal annual installments of $126,667 for the fiscal years ended June 30, 2007, 2008, and 2009. A liability and settlement expense of $682,000 was reflected in the June 30, 2006 financial statements. As of June 30, 2007, the Regulating District continues to be in litigation with one major statutory beneficiary for assessment abatement that could materially affect the financial position of the Regulating District. The case has been in litigation since 2001, and the litigant has filed challenges to its assessment for the last seven fiscal years. The litigation is now in the discovery phase and therefore the outcome is uncertain. No amounts have been accrued related to this contingency.

In 2006, the Regulating District was involved in litigation with a person who slipped on property under the Regulating District's jurisdiction. Since the case is in the discovery phase, it is not practical to estimate the ultimate liability of the Regulating District, and no amounts have been accrued related to this contingency.

The Regulating District has been named as defendant in a number of litigation actions relating to challenges to its assessments to various beneficiaries. Due to the nature of these actions, no estimate of ultimate liability, if any, to the Regulating District can be made. Consequently, no reserves have been recorded in the accompanying financial statements for the settlement of these matters. Management believes settlement of these matters could have a material adverse effect on the Regulating District's financial position, however, at this stage of litigation, it is not possible to estimate the amounts.

9. HYDROPOWER (WATER USAGE) AGREEMENTS

In the Hudson River area, the Regulating District has a Hydropower Agreement with a hydroelectric company effective July 1, 2003 and expiring June 30, 2021, requiring an initial annual payment of $850,000, increasing by 3.0% each year.

In the Black River area, the Regulating District has a Hydropower Agreement with a hydroelectric company effective January 1, 1986 and expiring in December 31, 2016, requiring an initial annual payment of $30,000 increasing by 3.0% each year.

Estimated annual required payments to the Regulating District under the terms of these agreements are as follows for the years ending June 30:

2008	$ 1,042,029
2009	1,073,290
2010	1,105,488
2011	1,138,653
2012	1,172,813
Thereafter	10,360,947
	$ 15,893,220

10. CONCENTRATION

Approximately 65% of assessment revenues and 66% of total operating revenues were provided by two statutory beneficiaries in 2008 and 2007.

11. POST-EMPLOYMENT HEALTH CARE BENEFITS

Plan Description

The Regulating District provides certain health care benefits for retired employees. The Regulating District administers the Retirement Benefits Plan (the "Retirement Plan") as a single-employer defined benefit Other Post-employment Benefit Plan (OPEB).

In general, the Regulating District provides health care benefits for those retired personnel who are eligible for a pension through the New York State Employees' Retirement System (ERS). The Retirement Plan can be amended by action of the District subject to applicable collective bargaining and employment agreements. The number of retired employees currently receiving benefits at June 30, 2008 and 2007 was 39 and 33 respectively. The Retirement Plan does not issue a stand-alone financial report since there are no assets legally segregated for the sole purpose of paying benefits under the plan.

Funding Policy

The obligations of the Retirement Plan are established by action of the Regulating District pursuant to applicable collective bargaining and employment agreements. The required premium contribution rates of retirees range from 0%-25%, depending on when the employee was hired and if the employee is governed by a CSEA or a management exempt plan. The Regulating District will pay 100% of the premiums for the retiree and spouse for a management exempt employee, 100% of the premium for a Union employee, and 75% of the premium for a Union employees' spouse. The Regulating District pays the costs of administering the Retirement Plan. The Regulating District currently contributes enough money to the Retirement Plan to satisfy current obligations on a pay-as-you-go basis to cover annual premiums. The amounts paid during 2008 and 2007 were approximately $338,000 and $287,000 respectively.

11. POST-EMPLOYMENT HEALTH CARE BENEFITS (Continued)

Annual OPEB Cost and Net OPEB Obligation

The Regulating Districts' annual OPEB cost is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with generally accepted accounting principles. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year plus the amortization of the unfunded actuarial accrued liability over a period not to exceed 30 years. The following table shows the components of the Regulating Districts' annual OPEB cost for the year, the amount actually contributed to the Retirement Plan, and the changes in the Regulating Districts' net OPEB obligation:

Annual required contribution	$ 1,709,274
Interest on net OPEB obligation	-
Adjustment to ARC	-
Annual OPEB cost	1,709,274
Contributions made	(337,526)
Increase in net OPEB obligation	1,371,748
Net OPEB obligation - beginning of year	-
Net OPEB obligation - end of year	$ 1,371,748
Percentage of Annual OPEB Cost Contributed	19.75%

Funded Status and Funding Progress

The projection of future benefits for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the Retirement Plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The Retirement Plan is currently not funded.

The schedule of funding progress presents information on the actuarial value of plan assets relative to the actuarial accrued liabilities for benefits. In the future, the schedule will provide multi-year trend information about the value of plan assets relative to the AAL.

Schedule of Funding Progress for the Regulating District's Plan

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b) - (a)	Funded Ratio (a)/(b)	Covered Payroll (c)	UAAL as a% of Covered Payroll (b-a)/(c)
7/1/2007	$ -	$ 17,665,905	$ 17,665,905	0.0%	$ 1,580,121	1,118%

11. POST-EMPLOYMENT HEALTH CARE BENEFITS (Continued)

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan as understood by the employer and plan members and include the types of benefits provided at the time of the valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the July 1, 2007 valuation, the following methods and assumptions were used:

Actuarial cost method	Projected unit credit
Discount rate*	2.0%
Medical care cost trend rate	9.0% or 10.0% initially, based on age of retirees. The rate is reduced by decrements to an ultimate rate of 5.0% after eight years.
Unfunded actuarial accrued liability:	
Amortization period	30 years
Amortization method	Level Dollar
Amortization basis	Open

* As the plan is unfunded, the assumed discount rate considers that the Regulating District's investment assets are low risk in nature, such as money market or Sentinel fund

12. COMMITMENTS

During fiscal 2008, the Regulating District entered into two operating lease agreements for office space that require monthly payments of $1,190 through November 2012, and monthly payments of $3,500 through March 2013.

The future minimum lease payments for fiscal years ending June 30 under the terms of these lease agreements are as follows:

2009	$ 56,376
2010	56,376
2011	56,376
2012	49,188
2013	10,500
	$ 228,816

Total rent expense recognized by the Regulating District under the terms of all of its office lease agreements was approximately $54,200 and $52,500 during the years ended June 30, 2008 and 2007, respectively.

HUDSON RIVER-BLACK RIVER REGULATING DISTRICT
(A DISCRETELY PRESENTED COMPONENT UNIT OF THE STATE OF NEW YORK)

COMBINING STATEMENT OF NET ASSETS
JUNE 30, 2008

	Hudson River	Black River	Total Regulating District
ASSETS			
CURRENT ASSETS:			
Cash	$ 1,448,986	$ 1,131,493	$ 2,580,479
Investments	1,167,554	2,464,993	3,632,547
Accounts receivable	-	5,125	5,125
Due (from) to District	6,095	(6,095)	-
Prepaid expenses	460,817	11,670	472,487
Total current assets	3,083,452	3,607,186	6,690,638
CAPITAL ASSETS, net	3,683,205	617,002	4,300,207
Total assets	6,766,657	4,224,188	10,990,845
LIABILITIES			
CURRENT LIABILITIES:			
Accounts payable	39,766	-	39,766
Compensated absences	301,669	57,271	358,940
Current portion of settlement payable	174,000	53,334	227,334
Current portion of other postemployment benefits	315,587	55,692	371,279
Current portion due to New York State Retirement System	33,336	-	33,336
Total current liabilities	864,358	166,297	1,030,655
OTHER POST EMPLOYMENT BENEFITS, net of current portion	850,399	150,070	1,000,469
DUE TO NEW YORK STATE RETIREMENT SYSTEM, net of current portion	45,109	-	45,109
Total liabilities	1,759,866	316,367	2,076,233
NET ASSETS			
INVESTED IN CAPITAL ASSETS	3,683,205	617,002	4,300,207
UNRESTRICTED NET ASSETS	1,323,586	3,290,819	4,614,405
Total net assets	$ 5,006,791	$ 3,907,821	$ 8,914,612

The accompanying notes are an integral part of these schedules.

HUDSON RIVER-BLACK RIVER REGULATING DISTRICT
(A DISCRETELY PRESENTED COMPONENT UNIT OF THE STATE OF NEW YORK)

COMBINING STATEMENT OF REVENUE, EXPENSES AND CHANGE IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2008

	Hudson River	Black River	Total Regulating District
OPERATING REVENUE:			
Assessments	$ 4,445,595	$ 910,276	$ 5,355,871
Water power service	956,682	54,996	1,011,678
Permit fees	414,194	-	414,194
Other	29,127	80	29,207
Total operating revenue	5,845,598	965,352	6,810,950
OPERATING EXPENSES:			
Personnel services and employee benefits	3,268,256	661,087	3,929,343
Repairs and maintenance	47,930	7,426	55,356
Material and supplies	187,221	44,382	231,603
Real estate taxes	2,337,999	39,232	2,377,231
Contractual services	884,137	131,235	1,015,372
Allocated general board expenses	(206,753)	206,753	-
Depreciation	208,986	45,643	254,629
Total operating expenses	6,727,776	1,135,758	7,863,534
Total operating loss	(882,178)	(170,406)	(1,052,584)
NON-OPERATING REVENUE:			
Interest and dividend income	128,121	186,300	314,421
Total non-operating revenue	128,121	186,300	314,421
CHANGE IN NET ASSETS	(754,057)	15,894	(738,163)
NET ASSETS - beginning of year	5,760,848	3,891,927	9,652,775
NET ASSETS - end of year	$ 5,006,791	$ 3,907,821	$ 8,914,612

The accompanying notes are an integral part of these schedules.

Bonadio & Co., LLP
Certified Public Accountants

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

October 14, 2008

To the Board of Directors of
Hudson River-Black River Regulating District:

We have audited the financial statements of Hudson River-Black River Regulating District (the Regulating District), as of and for the year ended June 30, 2008, and have issued our report thereon dated October 14, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting
In planning and performing our audit, we considered the Regulating District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Regulating District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Regulating District's internal control over financial reporting.

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

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

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

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*
(Continued)

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

We noted certain other matters that we reported to management of the Regulating District in a separate letter dated October 2008.

This report is intended solely for the information and use of management, the audit committee, Board of Directors, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.

Bonadio & Co., LLP