

MIDDLESEX WATER CO  
Form 10-Q  
August 02, 2012

UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
**WASHINGTON, DC 20549**

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

**For the quarterly period ended June 30, 2012**

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-422

MIDDLESEX WATER COMPANY

(Exact name of registrant as specified in its charter)

New Jersey **22-1114430**

(State of incorporation) (IRS employer identification no.)

Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

1500 Ronson Road, Iselin, NJ 08830

(Address of principal executive offices, including zip code)

**(732) 634-1500**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or such shorter period that the registrant was required to submit and post files).

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes  No

The number of shares outstanding of each of the registrant's classes of common stock, as of July 31, 2012: Common Stock, No Par Value: 15,733,286 shares outstanding.

INDEX

<u>PART I. FINANCIAL INFORMATION</u>	PAGE
<u>Item 1. Financial Statements (Unaudited):</u>	
<u>Condensed Consolidated Statements of Income</u>	1
<u>Condensed Consolidated Balance Sheets</u>	2
<u>Condensed Consolidated Statements of Cash Flows</u>	3
<u>Condensed Consolidated Statements of Capital Stock and Long-Term Debt</u>	4
<u>Notes to Unaudited Condensed Consolidated Financial Statements</u>	5
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	13
<u>Item 3. Quantitative and Qualitative Disclosures of Market Risk</u>	21
<u>Item 4. Controls and Procedures</u>	22
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	23
<u>Item 1A. Risk Factors</u>	23
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	23
<u>Item 3. Defaults upon Senior Securities</u>	23
<u>Item 4. Mine Safety Disclosures</u>	23
<u>Item 5. Other Information</u>	23
<u>Item 6. Exhibits</u>	23
<u>SIGNATURES</u>	24

Index

MIDDLESEX WATER COMPANY  
 CONDENSED CONSOLIDATED  
 STATEMENTS OF INCOME  
 (Unaudited)  
 (In thousands except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Operating Revenues	\$ 27,401	\$ 26,102	\$ 50,947	\$ 50,098
Operating Expenses:				
Operations and Maintenance	14,765	14,062	29,140	28,093
Depreciation	2,582	2,417	5,130	4,829
Other Taxes	2,844	2,885	5,590	5,670
Total Operating Expenses	20,191	19,364	39,860	38,592
Operating Income	7,210	6,738	11,087	11,506
Other Income (Expense):				
Allowance for Funds Used During Construction	137	197	273	391
Other Income	125	202	317	359
Other Expense	(11 )	(111 )	(151 )	(160 )
Total Other Income, net	251	288	439	590
Interest Charges	1,779	1,714	3,133	2,928
Income before Income Taxes	5,682	5,312	8,393	9,168
Income Taxes	1,957	1,687	2,861	2,913
Net Income	3,725	3,625	5,532	6,255
Preferred Stock Dividend Requirements	51	51	103	103
Earnings Applicable to Common Stock	\$ 3,674	\$ 3,574	\$ 5,429	\$ 6,152
Earnings per share of Common Stock:				
Basic	\$ 0.23	\$ 0.23	\$ 0.35	\$ 0.40

Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

Diluted	\$ 0.23	\$ 0.23	\$ 0.35	\$ 0.40
Average Number of Common Shares Outstanding :				
Basic	15,716	15,598	15,704	15,587
Diluted	15,979	15,861	15,967	15,850
Cash Dividends Paid per Common Share	\$ 0.1850	\$ 0.1825	\$ 0.3700	\$ 0.3650

See Notes to Condensed Consolidated Financial Statements.

Index

MIDDLESEX WATER COMPANY  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (Unaudited)  
 (In thousands)

		June 30, 2012	December 31, 2011
<b>ASSETS</b>			
<b>UTILITY PLANT:</b>	Water Production	\$129,118	\$127,827
	Transmission and Distribution	332,715	326,629
	General	54,035	47,519
	Construction Work in Progress	9,940	12,575
	<b>TOTAL</b>	<b>525,808</b>	<b>514,550</b>
	Less Accumulated Depreciation	95,832	92,351
	<b>UTILITY PLANT - NET</b>	<b>429,976</b>	<b>422,199</b>
<b>CURRENT ASSETS:</b>	Cash and Cash Equivalents	2,727	3,106
	Accounts Receivable, net	10,232	11,280
	Unbilled Revenues	6,193	4,842
	Materials and Supplies (at average cost)	2,041	2,023
	Prepayments	2,242	1,622
	<b>TOTAL CURRENT ASSETS</b>	<b>23,435</b>	<b>22,873</b>
<b>DEFERRED CHARGES AND OTHER ASSETS:</b>	Unamortized Debt Expense	2,550	2,611
	Preliminary Survey and Investigation Charges	5,157	5,179
	Regulatory Assets	66,338	67,302
	Operations and Developer Contracts Receivable	2,147	5,300
	Restricted Cash	5,838	3,260
	Non-utility Assets - Net	9,106	8,182
	Other	594	630
	<b>TOTAL DEFERRED CHARGES AND OTHER ASSETS</b>	<b>91,730</b>	<b>92,464</b>
	<b>TOTAL ASSETS</b>	<b>\$545,141</b>	<b>\$537,536</b>
<b>CAPITALIZATION AND LIABILITIES</b>			
<b>CAPITALIZATION:</b>	Common Stock, No Par Value	\$142,592	\$141,432
	Retained Earnings	35,168	35,549
	<b>TOTAL COMMON EQUITY</b>	<b>177,760</b>	<b>176,981</b>
	Preferred Stock	3,353	3,353
	Long-term Debt	135,079	132,167
	<b>TOTAL CAPITALIZATION</b>	<b>316,192</b>	<b>312,501</b>

Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

CURRENT	Current Portion of Long-term Debt	4,996	4,569
LIABILITIES:	Notes Payable	25,250	24,250
	Accounts Payable	4,797	5,706
	Accrued Taxes	9,252	7,847
	Accrued Interest	1,622	1,628
	Unearned Revenues and Advanced Service Fees	743	734
	Other	1,875	1,953
	<b>TOTAL CURRENT LIABILITIES</b>	<b>48,535</b>	<b>46,687</b>
COMMITMENTS AND CONTINGENT LIABILITIES (Note 7)			
DEFERRED CREDITS	Customer Advances for Construction	21,707	21,944
AND OTHER LIABILITIES:	Accumulated Deferred Investment Tax Credits	1,107	1,146
	Accumulated Deferred Income Taxes	37,753	37,022
	Employee Benefit Plans	51,304	51,006
	Regulatory Liability - Cost of Utility Plant Removal	8,405	8,029
	Other	974	995
	<b>TOTAL DEFERRED CREDITS AND OTHER LIABILITIES</b>	<b>121,250</b>	<b>120,142</b>
CONTRIBUTIONS IN AID OF CONSTRUCTION		59,164	58,206
	<b>TOTAL CAPITALIZATION AND LIABILITIES</b>	<b>\$545,141</b>	<b>\$ 537,536</b>

See Notes to Condensed Consolidated Financial Statements.

Index

MIDDLESEX WATER COMPANY  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (Unaudited)  
 (In thousands)

	Six Months Ended June 30,	
	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net Income	\$ 5,532	\$ 6,255
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	5,489	5,174
Provision for Deferred Income Taxes and Investment Tax Credits	990	422
Equity Portion of Allowance for Funds Used During Construction (AFUDC)	(170 )	(260 )
Cash Surrender Value of Life Insurance	(90 )	(86 )
Stock Compensation Expense	372	234
Changes in Assets and Liabilities:		
Accounts Receivable	4,201	1,827
Unbilled Revenues	(1,351 )	(1,567 )
Materials & Supplies	(18 )	247
Prepayments	(620 )	(836 )
Accounts Payable	(909 )	(699 )
Accrued Taxes	1,405	485
Accrued Interest	(6 )	82
Employee Benefit Plans	1,846	891
Unearned Revenue & Advanced Service Fees	9	2
Other Assets and Liabilities	(867 )	(87 )
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>15,813</b>	<b>12,084</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Utility Plant Expenditures, Including AFUDC of \$103 in 2012, \$131 in 2011	(12,574 )	(11,039 )
Restricted Cash	(2,578 )	1,145
Investment in Joint Venture	(500 )	—
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>(15,652 )</b>	<b>(9,894 )</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Redemption of Long-term Debt	(1,590 )	(1,434 )
Proceeds from Issuance of Long-term Debt	4,929	2,315
Net Short-term Bank Borrowings	1,000	3,250
Deferred Debt Issuance Expense	(22 )	(19 )
Repurchase of Preferred Stock	—	(9 )
Proceeds from Issuance of Common Stock	788	775
Payment of Common Dividends	(5,809 )	(5,688 )



Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

Payment of Preferred Dividends	(103	)	(103	)
Construction Advances and Contributions-Net	267		553	
NET CASH USED IN FINANCING ACTIVITIES	(540	)	(360	)
NET CHANGES IN CASH AND CASH EQUIVALENTS	(379	)	1,830	
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	3,106		2,453	
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 2,727		\$ 4,283	
SUPPLEMENTAL DISCLOSURE OF NON-CASH ACTIVITY:				
Utility Plant received as Construction Advances and Contributions	\$ 453		\$ 6,288	
SUPPLEMENTAL DISCLOSURE OF CASH FLOWS INFORMATION:				
Cash Paid During the Year for:				
Interest	\$ 3,208		\$ 2,918	
Interest Capitalized	\$ 103		\$ 131	
Income Taxes	\$ 774		\$ 2,550	

See Notes to Condensed Consolidated Financial Statements.

Index

MIDDLESEX WATER COMPANY  
 CONDENSED CONSOLIDATED STATEMENTS OF CAPITAL STOCK  
 AND LONG-TERM DEBT

(Unaudited)  
 (In thousands)

		June 30, 2012	December 31, 2011
Common Stock, No Par Value			
Shares Authorized -	40,000		
Shares Outstanding -	2012 - 15,730	\$ 142,592	\$ 141,432
	2011 - 15,682		
Retained Earnings		35,168	35,549
TOTAL COMMON EQUITY		\$ 177,760	\$ 176,981
Cumulative Preferred Stock, No Par Value:			
Shares Authorized - 134			
Shares Outstanding - 32			
Convertible:			
Shares Outstanding, \$7.00 Series - 14		1,457	1,457
Shares Outstanding, \$8.00 Series - 7		816	816
Nonredeemable:			
Shares Outstanding, \$7.00 Series - 1		80	80
Shares Outstanding, \$4.75 Series - 10		1,000	1,000
TOTAL PREFERRED STOCK		\$ 3,353	\$ 3,353
Long-term Debt:			
8.05%, Amortizing Secured Note, due December 20, 2021		\$ 2,245	\$ 2,319
6.25%, Amortizing Secured Note, due May 19, 2028		6,685	6,895
6.44%, Amortizing Secured Note, due August 25, 2030		5,087	5,227
6.46%, Amortizing Secured Note, due September 19, 2031		5,367	5,507
4.22%, State Revolving Trust Note, due December 31, 2022		527	546
3.30% to 3.60%, State Revolving Trust Note, due May 1, 2025		3,519	3,623
3.49%, State Revolving Trust Note, due January 25, 2027		618	633
4.03%, State Revolving Trust Note, due December 1, 2026		805	825
4.00% to 5.00%, State Revolving Trust Bond, due August 1, 2021		434	434
0.00%, State Revolving Fund Bond, due August 1, 2021		352	359
3.64%, State Revolving Trust Note, due July 1, 2028		356	364
3.64%, State Revolving Trust Note, due January 1, 2028		119	122
3.45%, State Revolving Trust Note, due August 1, 2031		392	39
6.59%, Amortizing Secured Note, due April 20, 2029		5,871	6,046
7.05%, Amortizing Secured Note, due January 20, 2030		4,396	4,521
5.69%, Amortizing Secured Note, due January 20, 2030		9,017	9,273
3.75%, State Revolving Trust Note, due July 1, 2031		2,664	2,021
3.75%, State Revolving Trust Note, due November 30, 2030		1,415	1,404
First Mortgage Bonds:			

Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

5.20%, Series S, due October 1, 2022	12,000	12,000
5.25%, Series T, due October 1, 2023	6,500	6,500
5.25%, Series V, due February 1, 2029	10,000	10,000
5.35%, Series W, due February 1, 2038	23,000	23,000
0.00%, Series X, due September 1, 2018	368	375
4.25% to 4.63%, Series Y, due September 1, 2018	410	410
0.00%, Series Z, due September 1, 2019	876	894
5.25% to 5.75%, Series AA, due September 1, 2019	1,080	1,080
0.00%, Series BB, due September 1, 2021	1,183	1,206
4.00% to 5.00%, Series CC, due September 1, 2021	1,400	1,400
5.10%, Series DD, due January 1, 2032	6,000	6,000
0.00%, Series EE, due August 1, 2023	4,709	4,804
3.00% to 5.50%, Series FF, due August 1, 2024	6,160	6,160
0.00%, Series GG, due August 1, 2026	1,330	1,352
4.00% to 5.00%, Series HH, due August 1, 2026	1,640	1,640
0.00%, Series II, due August 1, 2024	1,127	1,150
3.40% to 5.00%, Series JJ, due August 1, 2027	1,560	1,560
0.00%, Series KK, due August 1, 2028	1,500	1,526
5.00% to 5.50%, Series LL, due August 1, 2028	1,635	1,635
0.00%, Series MM, due August 1, 2030	1,868	1,901
3.00% to 4.375%, Series NN, due August 1, 2030	1,985	1,985
0.00%, Series OO, due August 1, 2031	2,960	—
2.00% to 5.00%, Series PP, due August 1, 2031	915	—
<b>SUBTOTAL LONG-TERM DEBT</b>	<b>140,075</b>	<b>136,736</b>
Less: Current Portion of Long-term Debt	(4,996 )	(4,569 )
<b>TOTAL LONG-TERM DEBT</b>	<b>\$135,079</b>	<b>\$ 132,167</b>

See Notes to Condensed Consolidated Financial Statements.

Index

**MIDDLESEX WATER COMPANY**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

Note 1 – Basis of Presentation and Recent Developments

Middlesex Water Company (Middlesex or the Company) is the parent company and sole shareholder of Tidewater Utilities, Inc. (Tidewater), Tidewater Environmental Services, Inc. (TESI), Pinelands Water Company (Pinelands Water) and Pinelands Wastewater Company (Pinelands Wastewater) (collectively, Pinelands), Utility Service Affiliates, Inc. (USA), Utility Service Affiliates (Perth Amboy) Inc. (USA-PA), and Twin Lakes Utilities, Inc. (Twin Lakes). Southern Shores Water Company, LLC (Southern Shores) and White Marsh Environmental Systems, Inc. (White Marsh) are wholly-owned subsidiaries of Tidewater. The financial statements for Middlesex and its wholly-owned subsidiaries (the Company) are reported on a consolidated basis. All significant intercompany accounts and transactions have been eliminated.

The consolidated notes within the 2011 Annual Report on Form 10-K (the 2011 Form 10-K) are applicable to these financial statements and, in the opinion of the Company, the accompanying unaudited condensed consolidated financial statements contain all adjustments necessary (including normal recurring accruals) to present fairly the financial position as of June 30, 2012, the results of operations for the three and six month periods ended June 30, 2012 and 2011 and cash flows for the six month periods ended June 30, 2012 and 2011. Information included in the Condensed Consolidated Balance Sheet as of December 31, 2011, has been derived from the Company's audited financial statements for the year ended December 31, 2011 included in the 2011 Form 10-K.

*Contract Awarded to USA*

In March 2012, the Borough of Avalon, New Jersey (Avalon) awarded an operations and maintenance contract to USA for the Avalon water utility, sewer utility and storm water system. In addition to performing the day to day operations, USA will be responsible for all billing, collections, customer service, emergency responses and capital projects funded by Avalon. The contract is for a ten year term and USA assumed operation and maintenance of the Avalon water utility, sewer utility and storm water system on July 1, 2012.

*Recent Accounting Guidance*

**Fair Value Measurements and Disclosures** – In May 2011, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2011-04, which amends Accounting Standards Codification 820, Fair Value Measurements and Disclosures, to update guidance related to fair value measurements and disclosures as a step towards achieving convergence between generally accepted accounting principles and international financial reporting

standards. ASU 2011-04 clarifies intent about application of existing fair value measurements and disclosures, changes certain requirements for fair value measurements and requires expanded disclosures. ASU 2011-04 was effective for interim and annual periods beginning after December 15, 2011. The Company's adoption of ASU 2011-04 resulted in expanded fair value disclosures and did not have any impact on the Company's results of operations, cash flows or financial position.

**Note 2 – Rate Matters**

**Middlesex** - In July 2012, Middlesex's application with the New Jersey Board of Public Utilities (NJBPU) seeking permission to increase its base water rates was partially approved, granting an increase in annual operating revenues of \$8.1 million. The originally-filed base water rate increase request of \$11.3 million, which was filed in January 2012, was made to seek recovery of increased costs of operations, chemicals and fuel, electricity, taxes, labor and benefits, decreases in industrial and commercial customer demand patterns, as well as capital investment. The new base water rates are designed to recover these increased costs, as well as a return on invested capital in rate base of \$202.4 million based on a return on equity of 10.15%. The rate increase became effective on July 20, 2012.

Index

**Tidewater** – In June 2012, Tidewater’s application with the Delaware Public Service Commission (DEPSC) seeking permission to increase its base water rates was partially approved, granting an increase in annual operating revenues of \$3.9 million. The originally-filed base water rate increase request of \$6.9 million, which was filed in September 2011, was made to seek recovery of increased costs for operations, maintenance and taxes, as well as capital investment. Under PSC regulations, Tidewater had implemented interim rates in November 2011, which amounted to approximately \$2.5 million on an annual basis. The new final base rates will reflect the remaining \$1.4 million and became effective June 19, 2012.

**TESI** – In June 2012, TESI’s application with the DEPSC seeking permission to increase its base wastewater rates was partially approved, granting an increase in annual operating revenues of \$0.6 million, a portion of which is to be phased in through 2015. The originally-filed base wastewater rate increase request of \$0.8 million, which was filed in July 2011, was made to seek recovery of increased operation and maintenance costs, as well as capital investment. Under PSC regulations, TESI had implemented interim rates in September 2011, which amounted to approximately \$0.1 million on an annual basis. The new final base rates became effective June 5, 2012.

**Note 3 – Capitalization**

*Common Stock*

During the six months ended June 30, 2012, there were 42,472 common shares (approximately \$0.8 million) issued under the Company’s Amended and Restated Dividend Reinvestment and Common Stock Purchase Plan (DRP).

The Company maintains a stock plan for its non-management directors (Outside Director Stock Compensation Plan). In May 2012, the Company granted and issued 5,768 shares of common stock (approximately \$0.1 million) to the non-management directors under the plan.

*Long-term Debt*

In May 2012, Middlesex borrowed \$3.9 million through the New Jersey Environmental Infrastructure Trust under the New Jersey State Revolving Fund (SRF) loan program and issued first mortgage bonds designated as Series OO (\$3.0 million) and Series PP (\$0.9 million). The interest rate on the Series OO bond is zero and the interest rate on the Series PP bond ranges from 2.0% to 5.0% depending on the serial maturity date. The final maturity date for both bonds is August 1, 2031. Proceeds were recorded as Restricted Cash and may only be used for the Middlesex 2012 RENEW Program, which is Middlesex’s program to clean and cement unlined mains in the Middlesex system.

In March 2011, Tidewater closed on a \$2.8 million loan with the Delaware State Revolving Fund (SRF) program which allows, but does not obligate, Tidewater to draw against a General Obligation Note for a specific project. The

Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

interest rate on any draw will be set at 3.75% with a final maturity of July 1, 2031 on the amount actually borrowed. As of June 30, 2012, Tidewater has borrowed \$2.7 million against this loan.

In March 2011, Southern Shores closed on a \$1.6 million loan with the Delaware SRF program, which allows, but does not obligate, Southern Shores to draw against a General Obligation Note for a specific. The interest rate on any draw will be set at 3.75% with a final maturity of November 30, 2030 on the amount actually borrowed. As of June 30, 2012, Southern Shores has borrowed \$1.4 million against this loan.

Index*Fair Value of Financial Instruments*

The following methods and assumptions were used by the Company in estimating its fair value disclosure for financial instruments for which it is practicable to estimate that value. The carrying amounts reflected in the condensed consolidated balance sheets for cash and cash equivalents, trade receivables, accounts payable and notes payable approximate their respective fair values due to the short-term maturities of these instruments. The fair value of the Company's long-term debt relating to First Mortgage and SRF Bonds is based on quoted market prices for similar issues. Under the fair value hierarchy, the fair value of cash and cash equivalents is classified as a Level 1 measurement and the fair value of notes payable and the First Mortgage and SRF Bonds in the table below are classified as Level 2 measurements. The carrying amount and fair market value of the Company's bonds were as follows:

	(Thousands of Dollars)			
	June 30, 2012		December 31, 2011	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
First Mortgage Bonds	\$90,208	\$91,370	\$86,577	\$87,283
SRF Bonds	\$785	\$790	\$793	\$799

For other long-term debt for which there was no quoted market price, it was not practicable to estimate their fair value. The carrying amount of these instruments was \$49.1 million at June 30, 2012 and \$49.3 million at December 31, 2011. Customer advances for construction have a carrying amount of \$21.7 million and \$21.9 million, respectively, at June 30, 2012 and December 31, 2011. Their relative fair values cannot be accurately estimated since future refund payments depend on several variables, including new customer connections, customer consumption levels and future rate increases.

**Note 4 – Earnings Per Share**

Basic earnings per share (EPS) are computed on the basis of the weighted average number of shares outstanding during the period presented. Diluted EPS assumes the conversion of both the Convertible Preferred Stock \$7.00 Series and the Convertible Preferred Stock \$8.00 Series.

	(In Thousands Except per Share Amounts)			
	Three Months Ended June 30, 2012		2011	
	Income	Shares	Income	Shares
Basic:				
Net Income	\$3,725	15,716	\$3,625	15,598



Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

Preferred Dividend	(51 )		(51 )	
Earnings Applicable to Common Stock	\$3,674	15,716	\$3,574	15,598
Basic EPS	\$0.23		\$0.23	
Diluted:				
Earnings Applicable to Common Stock	\$3,674	15,716	\$3,574	15,598
\$7.00 Series Preferred Dividend	24	167	24	167
\$8.00 Series Preferred Dividend	14	96	14	96
Adjusted Earnings Applicable to Common Stock	\$3,712	15,979	\$3,612	15,861
Diluted EPS	\$0.23		\$0.23	

7

Index

	(In Thousands Except per Share Amounts)			
	Six Months Ended June 30,			
	2012		2011	
	Income	Shares	Income	Shares
Basic:				
Net Income	\$5,532	15,704	\$6,255	15,587
Preferred Dividend	(103 )		(103 )	
Earnings Applicable to Common Stock	\$5,429	15,704	\$6,152	15,587
Basic EPS	\$0.35		\$0.40	
Diluted:				
Earnings Applicable to Common Stock	\$5,429	15,704	\$6,152	15,587
\$7.00 Series Preferred Dividend	49	167	49	167
\$8.00 Series Preferred Dividend	28	96	28	96
Adjusted Earnings Applicable to Common Stock	\$5,506	15,967	\$6,229	15,850
Diluted EPS	\$0.35		\$0.40	

**Note 5 – Business Segment Data**

The Company has identified two reportable segments. One is the regulated business of collecting, treating and distributing water on a retail and wholesale basis to residential, commercial, industrial and fire protection customers in parts of New Jersey, Delaware and Pennsylvania. This segment also includes regulated wastewater systems in New Jersey and Delaware. The Company is subject to regulations as to its rates, services and other matters by New Jersey, Delaware and Pennsylvania with respect to utility services within these states. The other segment is primarily comprised of non-regulated contract services for the operation and maintenance of municipal and private water and wastewater systems in New Jersey and Delaware. Inter-segment transactions relating to operational costs are treated as pass-through expenses. Finance charges on inter-segment loan activities are based on interest rates that are below what would normally be charged by a third party lender.

Index

	(In Thousands)			
	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
Operations by Segments:	2012	2011	2012	2011
Revenues:				
Regulated	\$24,442	\$23,437	\$45,300	\$44,673
Non – Regulated	3,089	2,774	5,847	5,615
Inter-segment Elimination	(130 )	(109 )	(200 )	(190 )
Consolidated Revenues	\$27,401	\$26,102	\$50,947	\$50,098
Operating Income:				
Regulated	\$6,878	\$6,317	\$10,381	\$10,652
Non – Regulated	332	421	706	854
Consolidated Operating Income	\$7,210	\$6,738	\$11,087	\$11,506
Net Income:				
Regulated	\$3,557	\$3,372	\$5,144	\$5,745
Non – Regulated	168	253	388	510
Consolidated Net Income	\$3,725	\$3,625	\$5,532	\$6,255
Capital Expenditures:				
Regulated	\$6,296	\$6,024	\$12,335	\$10,856
Non – Regulated	140	127	239	183
Total Capital Expenditures	\$6,436	\$6,151	\$12,574	\$11,039

	As of	As of
	June 30,	December
	2012	31,
		2011
Assets:		
Regulated	\$544,458	\$539,947
Non – Regulated	10,862	10,325
Inter-segment Elimination	(10,179 )	(12,736 )
Consolidated Assets	\$545,141	\$537,536

**Note 6 – Short-term Borrowings**

As of June 30, 2012, the Company has established lines of credit aggregating \$60.0 million. At June 30, 2012, the outstanding borrowings under these credit lines were \$25.3 million at a weighted average interest rate of 1.36%.

The weighted average daily amounts of borrowings outstanding under the Company's credit lines and the weighted average interest rates on those amounts were as follows:

	(\$ In Thousands)			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Average Daily Amounts Outstanding	\$24,635	\$19,548	\$24,102	\$18,426
Weighted Average Interest Rates	1.38 %	1.59 %	1.35 %	1.59 %

Index

The maturity dates for the \$25.3 million outstanding as of June 30, 2012 are all in July 2012 and are extendable at the discretion of the Company.

Interest rates for short-term borrowings under the lines of credit are below the prime rate with no requirement for compensating balances.

**Note 7 – Commitments and Contingent Liabilities**

*Contract Operations* - USA-PA operates the City of Perth Amboy, NJ’s water and wastewater systems under a 20-year agreement, which expires in 2018. In connection with the agreement with Perth Amboy, USA-PA entered into a 20-year subcontract with a wastewater operating company for the operation and maintenance of the Perth Amboy wastewater collection system. The subcontract provides for the sharing of certain fixed and variable fees and operating expenses.

*Water Supply*

Middlesex has an agreement with the NJWSA for the purchase of untreated water through November 30, 2023, which provides for an average purchase of 27 million gallons a day (mgd). Pricing is set annually by the NJWSA through a public rate making process. The agreement has provisions for additional pricing in the event Middlesex overdrafts or exceeds certain monthly and annual thresholds.

Middlesex also has an agreement with a non-affiliated regulated water utility for the purchase of treated water. This agreement, which expires February 27, 2016, provides for the minimum purchase of 3 mgd of treated water with provisions for additional purchases.

Purchased water costs are shown below:

	(In Thousands)			
	Three Months		Six Months	
	Ended		Ended	
	June 30,		June 30,	
	2012	2011	2012	2011
Treated	\$775	\$652	\$1,494	\$1,292
Untreated	516	516	1,128	1,122

Total Costs \$1,291 \$1,168 \$2,622 \$2,414

*Construction*

The Company has budgeted approximately \$21.8 million on its construction program in 2012. The actual amount and timing of capital expenditures is dependent on project scheduling and refinement of engineering estimates for certain projects.

*Litigation*

The Company is a defendant in lawsuits in the normal course of business. We believe the resolution of pending claims and legal proceedings will not have a material adverse effect on the Company's consolidated financial statements.

*Change in Control Agreements*

The Company has Change in Control Agreements with certain of its officers that provide compensation and benefits in the event of termination of employment in connection with a change in control of the Company.

Index**Note 8 – Employee Benefit Plans***Pension Benefits*

The Company's Pension Plan covers substantially all employees hired prior to March 31, 2007. Employees hired after March 31, 2007 are not eligible to participate in this plan, but do participate in a defined contribution plan that provides an annual contribution into a self-directed retirement account at the discretion of the Company, based upon a percentage of the participants' compensation. In order to be eligible for contribution, the participating employee must be employed by the Company on December 31st of the year to which the award relates. For the three months ended June 30, 2012, the Company did not make any Pension Plan cash contributions. For the three months ended June 30, 2011, the Company made Pension Plan cash contributions of \$0.4 million. For the six months ended June 30, 2012 and 2011, the Company made Pension Plan cash contributions of \$0.8 million and \$0.7 million, respectively. The Company expects to make additional Pension Plan cash contributions of approximately \$3.3 million over the remainder of the current year. The Company also maintains an unfunded supplemental retirement benefit plan for certain active and retired Company officers and currently pays \$0.3 million in annual benefits to the retired participants.

*Other Benefits*

The Company's Other Benefits Plan covers substantially all of its retired employees. Employees hired after March 31, 2007 are not eligible to participate in this plan. Coverage includes healthcare and life insurance. For the three months ended June 30, 2012 and 2011, the Company did not make any Other Benefits Plan cash contributions. For the six months ended June 30, 2012 and 2011, the Company made Other Benefits Plan cash contributions of \$0.8 million and \$0.5 million, respectively. The Company expects to make additional Other Benefits Plan cash contributions of approximately \$4.0 million over the remainder of the current year.

The following tables set forth information relating to the Company's periodic costs for its employee retirement benefit plans:

	(In Thousands)			
	Pension Benefits		Other Benefits	
	Three Months Ended June 30,			
	2012	2011	2012	2011
Service Cost	\$549	\$393	\$446	\$327
Interest Cost	604	565	467	401
Expected Return on Assets	(614)	(570)	(315)	(257)
Amortization of Unrecognized Losses	388	142	442	220
Amortization of Unrecognized Prior Service Cost	3	3	—	—
Amortization of Transition Obligation	—	—	34	34

Net Periodic Benefit Cost

\$930 \$533 \$1,074 \$725

11



Index

	(In Thousands)			
	Pension Benefits		Other Benefits	
	Six Months Ended June 30,			
	2012	2011	2012	2011
Service Cost	\$1,099	\$787	\$892	\$653
Interest Cost	1,208	1,130	934	802
Expected Return on Assets	(1,229)	(1,141)	(629 )	(513 )
Amortization of Unrecognized Losses	775	283	883	439
Amortization of Unrecognized Prior Service Cost	5	5	—	—
Amortization of Transition Obligation	—	—	68	68
Net Periodic Benefit Cost	\$1,858	\$1,064	\$2,148	\$1,449

Index

**Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations**

The following discussion and analysis should be read in conjunction with the unaudited condensed consolidated financial statements of Middlesex Water Company (Middlesex or the Company) included elsewhere herein and with the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

**Forward-Looking Statements**

Certain statements contained in this periodic report and in the documents incorporated by reference constitute “forward-looking statements” within the meaning of Section 21E of the Securities Exchange Act of 1934 and Section 27A of the Securities Act of 1933. The Company intends that these statements be covered by the safe harbors created under those laws. These statements include, but are not limited to:

- statements as to expected financial condition, performance, prospects and earnings of the Company;
- statements regarding strategic plans for growth;
- statements regarding the amount and timing of rate increases and other regulatory matters, including the recovery of certain costs recorded as regulatory assets;
- statements as to the Company’s expected liquidity needs during the upcoming fiscal year and beyond and statements as to the sources and availability of funds to meet its liquidity needs;
- statements as to expected rates, consumption volumes, service fees, revenues, margins, expenses and operating results;
- statements as to the Company’s compliance with environmental laws and regulations and estimations of the materiality of any related costs;
- statements as to the safety and reliability of the Company’s equipment, facilities and operations;
- statements as to financial projections;
- statements as to the ability of the Company to pay dividends;
- statements as to the Company’s plans to renew municipal franchises and consents in the territories it serves;
- expectations as to the amount of cash contributions to fund the Company’s retirement benefit plans, including statements as to anticipated discount rates and rates of return on plan assets;
- statements as to trends; and
- statements regarding the availability and quality of our water supply.

These forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results to differ materially from future results expressed or implied by the forward-looking statements. Important factors that could cause actual results to differ materially from anticipated results and outcomes include, but are not limited to:

- the effects of general economic conditions;
- increases in competition in the markets served by the Company;
- the ability of the Company to control operating expenses and to achieve efficiencies in its operations;
- the availability of adequate supplies of water;
- actions taken by government regulators, including decisions on rate increase requests;
- new or additional water quality standards;
- weather variations and other natural phenomena;
- the existence of attractive growth opportunities and the risks involved in pursuing those opportunities;
- acts of war or terrorism;
- significant changes in the pace of housing development in Delaware;
- the availability and cost of capital resources;
- the ability to translate Preliminary Survey & Investigation (PS&I) charges into viable projects; and
- other factors discussed elsewhere in this quarterly report.



## Index

Many of these factors are beyond the Company's ability to control or predict. Given these uncertainties, readers are cautioned not to place undue reliance on any forward-looking statements, which only speak to the Company's understanding as of the date of this report. The Company does not undertake any obligation to release publicly any revisions to these forward-looking statements to reflect events or circumstances after the date of this report or to reflect the occurrence of unanticipated events, except as may be required under applicable securities laws.

For an additional discussion of factors that may affect the Company's business and results of operations, see Item 1A. - Risk Factors in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

## **Overview**

Middlesex has operated as a water utility in New Jersey since 1897, in Delaware through our wholly-owned subsidiary, Tidewater Utilities, Inc. (Tidewater), since 1992 and in Pennsylvania through our wholly-owned subsidiary, Twin Lakes Utilities, Inc. (Twin Lakes), since 2009. We are in the business of collecting, treating and distributing water for domestic, commercial, municipal, industrial and fire protection purposes. We also operate a New Jersey municipal water and wastewater system under contract and provide wastewater services in New Jersey and Delaware through our subsidiaries. We are regulated as to rates charged to customers for water and wastewater services, as to the quality of water service we provide and as to certain other matters in New Jersey, Delaware and Pennsylvania. Only our Utility Services Affiliates, Inc. (USA), Utility Services Affiliates (Perth Amboy), Inc. (USA-PA) and White Marsh Environmental Systems, Inc. (White Marsh) subsidiaries are not regulated utilities.

Our New Jersey water utility system (the Middlesex System) provides water services to approximately 60,000 retail customers, primarily in central New Jersey. The Middlesex System also provides water service under contract to several municipalities in central New Jersey. In partnership with our subsidiary, USA-PA, we operate the water supply system and wastewater system for the City of Perth Amboy, New Jersey. Our Bayview system provides water services in Downe Township, New Jersey. Our other New Jersey subsidiaries, Pinelands Water Company and Pinelands Wastewater Company (collectively, Pinelands), provide water and wastewater services to residents in Southampton Township, New Jersey.

USA offers residential customers in New Jersey and Delaware water service line and sewer lateral maintenance programs, which are serviced by HomeServe USA (HomeServe), a leading provider of home maintenance service programs. HomeServe has recently expanded its maintenance offerings under the program to include other household services. USA receives a service fee for the billing, cash collection and other administrative matters associated with HomeServe's service contracts. In February 2012, USA began to operate a wastewater treatment facility under contract at an industrial site in Southern New Jersey. On July 1, 2012, USA began operating the water and sewer utilities and storm water system of the Borough of Avalon, New Jersey.

## Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

Our Delaware subsidiaries, Tidewater and Southern Shores Water Company, LLC (Southern Shores), provide water services to approximately 36,000 retail customers in New Castle, Kent and Sussex Counties, Delaware. Tidewater's subsidiary, White Marsh, services an additional 4,700 customers in Kent and Sussex Counties through various operations and maintenance contracts.

Our Tidewater Environmental Services, Inc. (TESI) subsidiary provides wastewater services to approximately 2,200 residential retail customers. We expect the growth of our regulated wastewater operations in Delaware will eventually become a more significant component of our operations.

Our Pennsylvania subsidiary, Twin Lakes, provides water services to approximately 120 retail customers in the Township of Shohola, Pike County, Pennsylvania.

## Index

The majority of our revenue is generated from retail and contract water services to customers in our service areas. We record water service revenue as such service is rendered and include estimates for amounts unbilled at the end of the period for services provided after the last billing cycle. Fixed service charges are billed in advance by our subsidiary, Tidewater, and are recognized in revenue as the service is provided.

Our ability to increase operating income and net income is based significantly on four factors: weather, adequate and timely rate relief, effective cost management, and customer growth. These factors are evident in the discussions below which compare our results of operations with prior periods.

## **Recent Developments**

### *Rate Matters*

**Middlesex** - In July 2012, Middlesex's application with the New Jersey Board of Public Utilities (NJBP) seeking permission to increase its base water rates was partially approved, granting an increase in annual operating revenues of \$8.1 million. The originally-filed base water rate increase request of \$11.3 million, which was filed in January 2012, was made to seek recovery of increased costs of operations, chemicals and fuel, electricity, taxes, labor and benefits, decreases in industrial and commercial customer demand patterns, as well as capital investment. The new base water rates are designed to recover these increased costs, as well as a return on invested capital in rate base of \$202.4 million based on a return on equity of 10.15%. The rate increase became effective on July 20, 2012.

**Tidewater** – In June 2012, Tidewater's application with the Delaware Public Service Commission (DEPSC) seeking permission to increase its base water rates was partially approved, granting an increase in annual operating revenues of \$3.9 million. The originally-filed base water rate increase request of \$6.9 million, which was filed in September 2011, was made to seek recovery of increased costs for operations, maintenance and taxes, as well as capital investment. Under PSC regulations, Tidewater had implemented interim rates in November 2011, which amounted to approximately \$2.5 million on an annual basis. The new final base rates will reflect the remaining \$1.4 million and became effective June 19, 2012.

**TESI** – In June 2012, TESI's application with the DEPSC seeking permission to increase its base wastewater rates was partially approved, granting an increase in annual operating revenues of \$0.6 million, a portion of which is to be phased in through 2015. The originally-filed base wastewater rate increase request of \$0.8 million, which was filed in July 2011, was made to seek recovery of increased operation and maintenance costs, as well as capital investment. Under PSC regulations, TESI had implemented interim rates in September 2011, which amounted to approximately \$0.1 million on an annual basis. The new final base rates became effective June 5, 2012.

### *Contract Awarded to USA*

Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

In March 2012, the Borough of Avalon, New Jersey (Avalon) awarded an operations and maintenance contract to USA for the Avalon water utility, sewer utility and storm water system. In addition to performing the day to day operations, USA will be responsible for all billing, collections, customer service, emergency responses and capital projects funded by Avalon. The contract is for a ten year term and USA began operating the systems on July 1, 2012. The contract is expected to contribute less than \$0.01 to annual earnings per share.

Index

**Outlook**

Revenues for 2012 are expected to be favorably impacted from approved rate increases at Middlesex, Tidewater, TESI, Southern Shores and Twin Lakes. In addition, Pinelands Water and Pinelands Wastewater intend to file for base rate increases in the third quarter of 2012. Any decision on the expected rate filing would be rendered in 2013.

Ongoing economic conditions continue to negatively impact our customers' water consumption, particularly the level of water usage by our commercial and industrial customers in our Middlesex system. We are unable to determine when these customers' water demands may fully return to previous levels, or if a reduced level of demand will continue indefinitely. We were given appropriate recognition for this decrease in customer consumption in Middlesex's July 2012 rate increase.

Revenues and earnings are influenced by weather. Changes in usage patterns, as well as increases in capital expenditures and operating costs, are the primary factors in determining the need for rate increase requests. We continuously implement plans to streamline operations and reduce operating costs.

Changes in certain actuarial assumptions, including a lower discount rate and revised plan participant mortality factors, as well as a lower actual return in 2011 on assets held in our retirement plan funds resulted in a significant increase in our underfunded employee benefit plan obligation and will result in higher employee benefit plan expense and cash contributions in 2012. The rate increases recently approved for Tidewater and Middlesex reflected the resulting increased employee benefit plan expenses.

As a result of ongoing challenging economic conditions impacting the pace of new residential home construction, there may be an increase in the amount of PS&I costs that will not be currently recoverable in rates. If it is determined that recovery is unlikely, the PS&I costs deemed unrecoverable will be charged against income in the period of determination.

Our strategy is focused on four key areas:

- Serve as a trusted and continually-improving provider of safe, reliable and cost-effective water, wastewater and related services;

- Provide a comprehensive suite of water and wastewater solutions in the continually-developing Delaware market that results in profitable growth;



• Pursue profitable growth in our core states of New Jersey and Delaware, as well as additional states; and

• Invest in products, services and other viable opportunities that complement our core competencies.

Index**Operating Results by Segment**

The discussion of the Company's operating results is on a consolidated basis and includes significant factors by subsidiary. The Company has two operating segments, Regulated and Non-Regulated.

The segments in the tables included below consist of the following companies: Regulated-Middlesex, Tidewater, Pinelands, Southern Shores, TESI and Twin Lakes; Non-Regulated- USA, USA-PA, and White Marsh.

**Results of Operations – Three Months Ended June 30, 2012**

	(In Thousands)					
	<u>Three Months Ended June 30,</u>					
	2012			2011		
	Regulated	Non-Regulated	Total	Regulated	Non-Regulated	Total
Revenues	\$24,389	\$ 3,012	\$27,401	\$23,381	\$ 2,721	\$26,102
Operations and maintenance expenses	12,207	2,558	14,765	11,867	2,195	14,062
Depreciation expense	2,541	41	2,582	2,380	37	2,417
Other taxes	2,763	81	2,844	2,817	68	2,885
Operating income	6,878	332	7,210	6,317	421	6,738
Other income, net	235	16	251	229	59	288
Interest expense	1,754	25	1,779	1,689	25	1,714
Income taxes	1,802	155	1,957	1,485	202	1,687
Net income	\$3,557	\$ 168	\$3,725	\$3,372	\$ 253	\$3,625

Operating revenues for the three months ended June 30, 2012 increased \$1.3 million from the same period in 2011. This increase was primarily related to the following factors:

Middlesex System revenues increased \$0.1 million, primarily due to:

- o Sales to General Metered Service (GMS) customers increased by \$0.2 million due to increased customer demand for water and implementation of a purchased water adjustment clause in August 2011; and
  - o Contract Sales to Municipalities decreased by \$0.1 million due to lower customer demand for water;
- Tidewater System revenues increased \$0.7 million, primarily due to the 10.49% interim rate increase that went into effect in November 2011 and increased connection fees;
- USA-PA's revenues increased \$0.2 million, primarily from scheduled increases in the fixed fees paid under contract with the City of Perth Amboy;

Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

Southern Shores' revenues increased \$0.1 million, primarily due to rate increases that went into effect in June 2011 and January 2012; and

Revenues from all other subsidiaries increased \$0.2 million.

Index

*Operation and Maintenance Expense*

Operation and maintenance expenses for the three months ended June 30, 2012 increased \$0.7 million from the same period in 2011. This increase was primarily related to the following factors:

Employee benefit expenses increased \$0.6 million, primarily due to changes in certain postretirement benefit plan actuarial assumptions, including a lower discount rate and revised plan participant mortality factors, as well as a lower actual return on assets held in our retirement plan funds;

Reserves for bad debts increased \$0.1 million;

Costs associated with main breaks decreased \$0.1 million, due to more favorable weather conditions, which led to below average number of main breaks in 2012;

Labor costs decreased \$0.2 million primarily due to higher capitalized payroll and decreased headcount; and

Operation and maintenance expenses for all other categories increased \$0.3 million.

*Depreciation*

Depreciation expense for the three months ended June 30, 2012 increased \$0.2 million from the same period in 2011 due to a higher level of utility plant in service.

*Other Taxes*

Other taxes for the three months ended June 30, 2012 was consistent with the same period in 2011.

*Interest Charges*

Interest charges for the three months ended June 30, 2012 increased \$0.1 million from the same period in 2011, primarily due to higher average short and long term debt outstanding in the second quarter of 2012 as compared to the second quarter of 2011.

*Other Income, net*

Other Income, net for the three months ended June 30, 2012 was consistent with the same period in 2011.

*Income Taxes*

Income taxes for the three months ended June 30, 2012 increased \$0.3 million from the same period in 2011, due to increased operating income in 2012 as compared to 2011.

*Net Income and Earnings Per Share*

Net income for the three months ended June 30, 2012 increased \$0.1 million from the same period in 2011. Basic and diluted earnings per share was \$0.23 for the each of the three months ended June 30, 2012 and 2011.

Index**Results of Operations – Six Months Ended June 30, 2012**

	(In Thousands)					
	<u>Six Months Ended June 30,</u>					
	2012			2011		
	Regulated	Non-Regulated	Total	Regulated	Non-Regulated	Total
Revenues	\$45,230	\$ 5,717	\$50,947	\$44,589	\$ 5,509	\$50,098
Operations and maintenance expenses	24,363	4,777	29,140	23,647	4,446	28,093
Depreciation expense	5,053	77	5,130	4,755	74	4,829
Other taxes	5,433	157	5,590	5,535	135	5,670
Operating income	10,381	706	11,087	10,652	854	11,506
Other income, net	376	63	439	475	115	590
Interest expense	3,086	47	3,133	2,877	51	2,928
Income taxes	2,527	334	2,861	2,505	408	2,913
Net income	\$5,144	\$ 388	\$5,532	\$5,745	\$ 510	\$6,255

*Operating Revenues*

Operating revenues for the six months ended June 30, 2012 increased \$0.8 million from the same period in 2011. This increase was primarily related to the following factors:

Middlesex System revenues decreased \$0.7 million, primarily due to:

Sales to GMS customers decreased by \$0.3 million due to decreased customer demand for water. The decline in water use by our GMS customers includes commercial and industrial (C&I) customers. Several of the larger industrial customers' consumption demands have decreased due to reduced output from their production processes. We have also seen a decline in consumption from our commercial customers, which are generally office facilities, guest facilities and multi-family residential facilities. Certain of our C&I customers are unable to determine when their water demands may return to previous levels or if the declines will continue; and

o Contract Sales to Municipalities decreased by \$0.4 million due to lower customer demand for water; Tidewater System revenues increased \$1.1 million, primarily due to the 10.49% interim rate increase that went into effect in November 2011 and increased connection fees;

USA-PA's revenues increased \$0.2 million, primarily from scheduled increases in the fixed fees paid under contract with the City of Perth Amboy;

Southern Shores' revenues increased \$0.1 million, primarily due to rate increases that went into effect in June 2011 and January 2012; and

Revenues from all other subsidiaries increased \$0.1 million.



Index

*Operation and Maintenance Expense*

Operation and maintenance expenses for the six months ended June 30, 2012 increased \$1.0 million from the same period in 2011. This increase was primarily related to the following factors:

Employee benefit expenses increased \$1.1 million, primarily due to changes in certain postretirement benefit plan actuarial assumptions, including a lower discount rate and revised plan participant mortality factors, as well as a lower actual return on assets held in our retirement plan funds;

Reserves for bad debts increased \$0.1 million;

Costs associated with main breaks decreased \$0.2 million, due to more favorable weather conditions, which led to below average number of main breaks in 2012;

Labor costs decreased \$0.3 million primarily due to higher capitalized payroll and less overtime expended on main breaks; and

Operation and maintenance expenses for all other categories increased \$0.3 million.

*Depreciation*

Depreciation expense for the six months ended June 30, 2012 increased \$0.3 million from the same period in 2011 due to a higher level of utility plant in service.

*Other Taxes*

Other taxes for the six months ended June 30, 2012 decreased \$0.1 million from the same period in 2011 primarily due to lower revenue related taxes for our New Jersey operations compared to the same period in 2011.

*Interest Charges*

Interest charges for the six months ended June 30, 2012 increased \$0.2 million from the same period in 2011, primarily due to primarily due to higher average short and long term debt outstanding in 2012 as compared to 2011.

*Other Income, net*



Other Income, net for the six months ended June 30, 2012 decreased \$0.2 million from the same period in 2011, primarily due to lower Allowance for Funds Used During Construction, resulting from lower average construction work in progress balances.

*Income Taxes*

Income taxes for the six months ended June 30, 2012 decreased \$0.1 million from the same period in 2011, due to decreased operating income in 2012 as compared to 2011.

*Net Income and Earnings Per Share*

Net income for the six months ended June 30, 2012 decreased \$0.7 million from the same period in 2011. Basic and diluted earnings per share decreased to \$0.35 for the six months ended June 30, 2012 as compared to \$0.40 for the six months ended June 30, 2011.

Index

**Liquidity and Capital Resources**

*Operating Cash Flows*

Cash flows from operations are largely based on four factors: weather, adequate and timely rate increases, effective cost management and customer growth. The effect of those factors on net income is discussed in “Results of Operations.”

For the six months ended June 30, 2012, cash flows from operating activities increased \$3.7 million to \$15.8 million. Decreased accounts receivable and timing of certain income tax payments were the primary reason for the increase in cash flow. The \$15.8 million of net cash flow from operations enabled us to fund 100% of our utility plant expenditures internally for the period.

*Capital Expenditures and Commitments*

To fund our capital program, we use internally generated funds, short-term and long-term debt borrowings and, when market conditions are favorable, proceeds from sales of common stock under our Amended and Restated Dividend Reinvestment and Common Stock Purchase Plan (DRP) and common stock offerings. See below for a more detailed discussion regarding the funding of our capital program.

The capital investment program for 2012 is currently estimated to be \$21.8 million. Through June 30, 2012, we have expended \$12.6 million and expect to incur approximately \$9.2 million for capital projects for the remainder of 2012.

We currently project that we may be required to expend approximately \$34.0 million for capital projects in 2013 and 2014. The actual amount and timing of capital expenditures is dependent on project scheduling and refinement of engineering estimates for certain capital projects.

To fund our capital program for the remainder of 2012, we plan on utilizing:

Internally generated funds

Proceeds from the sale of common stock through the DRP

Funds available and held in trust under existing New Jersey and Delaware State Revolving Fund (SRF) loans (currently, \$3.7 million and \$0.9 million, respectively). The SRF programs provide low cost financing for projects that meet certain water quality and system improvement benchmarks.

Short-term borrowings, if necessary, through \$60.0 million of available lines of credit with several financial institutions. As of June 30, 2012, the outstanding borrowings under these credit lines were \$25.3 million.

**Recent Accounting Pronouncements** – See Note 1 of the Notes to Unaudited Condensed Consolidated Financial Statements for a discussion of recent accounting pronouncements.

**Item 3. Quantitative and Qualitative Disclosures of Market Risk**

The Company is subject to the risk of fluctuating interest rates in the normal course of business. Our policy is to manage interest rates through the use of fixed rate long-term debt and, to a lesser extent, short-term debt. The Company's interest rate risk related to existing fixed rate, long-term debt is not material due to the term of the majority of our First Mortgage Bonds, which have final maturity dates ranging from 2018 to 2038. Over the next twelve months, approximately \$5.0 million of the current portion of 34 existing long-term debt instruments will mature. Applying a hypothetical change in the rate of interest charged by 10% on those borrowings, would not have a material effect on our earnings.

Index

**Item 4. Controls and Procedures**

*Disclosure Controls and Procedures*

As required by Rule 13a-15 under the Securities and Exchange Act of 1934 (the Exchange Act), an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures was conducted by the Company's Chief Executive Officer along with the Company's Chief Financial Officer. Based upon that evaluation, the Company's Chief Executive Officer and the Company's Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective as of the end of the period covered by this Report.

Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed in Company reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in Company reports filed under the Exchange Act is accumulated and communicated to management, including the Company's Chief Executive Officer and Chief Financial Officer as appropriate, to allow timely decisions regarding disclosure.

*Material Change in Internal Controls*

In the second quarter of 2012, the Company implemented the work and asset management module of an enterprise resource planning (ERP) system. As previously disclosed, the Company had implemented various other modules of the ERP system in 2010.

The implementation of the work and asset management module and the related workflow changes have resulted in material changes to the Company's internal controls over financial reporting (as that term is defined in Rule 13(a)-15 under the Exchange Act). In connection with the implementation of the work and asset management module, the Company is continuing to replace and supplement existing internal controls over financial reporting, as appropriate. The decision to implement the ERP system was made to improve the efficiency and effectiveness of our management and financial reporting systems and was not made in response to any actual or perceived deficiencies in the Company's internal control over financial reporting.

We continually review our disclosure controls and procedures and make changes, as necessary, to ensure the quality of our financial reporting. Other than the changes made related to the implementation of the work and asset

management module and the related work flow changes, there have been no changes in internal control over financial reporting that occurred in the second quarter of 2012 that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

Index

**PART II. OTHER INFORMATION**

Item 1. Legal Proceedings

None.

Item 1A. Risk Factors

The information about risk factors does not differ materially from those set forth in Part I, Item 1A. of the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Exhibits

Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

- Item  
6.
- 10.43 Copy of Loan Agreement By and Between The State of New Jersey, Acting By and Through The New Jersey Department of Environmental Protection and Middlesex Water Company, dated as of May 1, 2012 (Series 00).
- 10.44 Copy of Loan Agreement by and Between New Jersey Environmental Infrastructure Trust and Middlesex Water Company dated as of May 1, 2012 (Series PP).
- 31.1 Section 302 Certification by Dennis W. Doll pursuant to Rules 13a-14 and 15d-14 of the Securities Exchange Act of 1934.
- 31.2 Section 302 Certification by A. Bruce O'Connor pursuant to Rules 13a-14 and 15d-14 of the Securities Exchange Act of 1934.
- 32.1 Section 906 Certification by Dennis W. Doll pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.2 Section 906 Certification by A. Bruce O'Connor pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 101.INS XBRL Instance Document
- 101.SCHXBRL Schema Document
- 101.CALXBRL Calculation Linkbase Document
- 101.LABXBRL Labels Linkbase Document
- 101.PRE XBRL Presentation Linkbase Document
- 101.DEF XBRL Definition Linkbase Document

Index

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MIDDLESEX WATER  
COMPANY

By: /s/ A. Bruce O'Connor  
A. Bruce O'Connor  
Vice President and  
Chief Financial Officer  
(Principal Accounting Officer)

Dated: August 2, 2012