

MIDDLESEX WATER CO  
Form 10-Q  
May 08, 2007

---

---

**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 March 31, 2007**

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**  
(State of incorporation)

**22-1114430**  
(IRS employer identification no.)

**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 is large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

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 May 7, 2007: Common Stock, No Par Value: 13,187,763 shares outstanding.

---

---

---

INDEX

<b><u>PART I.</u></b>	<b><u>FINANCIAL INFORMATION</u></b>	<b><u>PAGE</u></b>
<u>Item 1.</u>	<u>Financial Statements:</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.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	12
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures of Market Risk</u>	16
<u>Item 4.</u>	<u>Controls and Procedures</u>	16
<b><u>PART II.</u></b>	<b><u>OTHER INFORMATION</u></b>	
<u>Item 1.</u>	<u>Legal Proceedings</u>	17
<u>Item 1A.</u>	<u>Risk Factors</u>	17
<u>Item 2.</u>	<u>Changes in Securities</u>	17
<u>Item 3.</u>	<u>Defaults Upon Senior Securities</u>	17
<u>Item 4.</u>	<u>Submission of Matters to a Vote of Security Holders</u>	17
<u>Item 5.</u>	<u>Other Information</u>	17
<u>Item 6.</u>	<u>Exhibits</u>	18
<b><u>SIGNATURE</u></b>		19



Index

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

	Three Months Ended March	
	2007	2006
Operating Revenues	\$ 18,988	\$ 18,230
Operating Expenses:		
Operations	10,192	9,646
Maintenance	978	739
Depreciation	1,845	1,668
Other Taxes	2,251	2,204
Total Operating Expenses	15,266	14,257
Operating Income	3,722	3,973
Other Income (Expense):		
Allowance for Funds Used During Construction	112	113
Other Income	226	58
Other Expense	(5)	(2)
Total Other Income, net	333	169
Interest Charges	1,384	1,515
Income before Income Taxes	2,671	2,627
Income Taxes	902	815
Net Income	1,769	1,812
Preferred Stock Dividend Requirements	62	62
Earnings Applicable to Common Stock	\$ 1,707	\$ 1,750
Basic	\$ 0.13	\$ 0.15
Diluted	\$ 0.13	\$ 0.15
Average Number of Common Shares Outstanding:		
Basic	13,176	11,594
Diluted	13,507	11,925
Cash Dividends Paid per Common Share	\$ 0.1725	\$ 0.1700

See Notes to Condensed Consolidated Financial Statements.

1

---

Index

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

ASSETS		March 31, 2007	December 31, 2006
<b>UTILITY PLANT:</b>	Water Production	\$ 96,840	\$ 95,324
	Transmission and Distribution	247,955	243,959
	General	24,154	25,153
	Construction Work in Progress	6,113	6,131
	<b>TOTAL</b>	<b>375,062</b>	<b>370,567</b>
	Less Accumulated Depreciation	61,026	59,694
	<b>UTILITY PLANT - NET</b>	<b>314,036</b>	<b>310,873</b>
<b>CURRENT ASSETS:</b>	Cash and Cash Equivalents	5,238	5,826
	Accounts Receivable, net	9,124	8,538
	Unbilled Revenues	4,078	4,013
	Materials and Supplies (at average cost)	1,425	1,306
	Prepayments	910	1,229
	<b>TOTAL CURRENT ASSETS</b>	<b>20,775</b>	<b>20,912</b>
<b>DEFERRED CHARGES</b>	Unamortized Debt Expense	2,999	3,014
	Preliminary Survey and		
<b>AND OTHER ASSETS:</b>	Investigation Charges	4,099	3,436
	Regulatory Assets	20,336	18,342
	Restricted Cash	6,275	6,850
	Non-utility Assets - Net	6,527	6,255
	Other	417	585
	<b>TOTAL DEFERRED CHARGES AND OTHER ASSETS</b>	<b>40,653</b>	<b>38,482</b>
	<b>TOTAL ASSETS</b>	<b>\$ 375,464</b>	<b>\$ 370,267</b>
<b>CAPITALIZATION AND LIABILITIES</b>			
<b>CAPITALIZATION:</b>	Common Stock, No Par Value	\$ 104,597	\$ 104,248
	Retained Earnings	24,421	25,001
	Accumulated Other Comprehensive Income (Loss), net of tax	103	94
	<b>TOTAL COMMON EQUITY</b>	<b>129,121</b>	<b>129,343</b>
	Preferred Stock	3,958	3,958
	Long-term Debt	130,270	130,706
	<b>TOTAL CAPITALIZATION</b>	<b>263,349</b>	<b>264,007</b>
<b>CURRENT LIABILITIES:</b>	Current Portion of Long-term Debt	2,553	2,501
	Accounts Payable	5,023	5,491
	Accrued Taxes	9,057	6,684
	Accrued Interest	896	1,880
		<b>608</b>	<b>601</b>

	Unearned Revenues and Advanced Service Fees		
	Other	1,240	984
	<b>TOTAL CURRENT LIABILITIES</b>	<b>19,377</b>	<b>18,141</b>
<b>COMMITMENTS AND CONTINGENT LIABILITIES</b>			
<b>(Note 7)</b>			
<b>DEFERRED CREDITS AND OTHER LIABILITIES:</b>	Customer Advances for Construction	19,671	19,246
	Accumulated Deferred Investment Tax Credits	1,793	1,813
	Accumulated Deferred Income Taxes	17,788	15,779
	Employee Benefit Plans	17,093	16,388
	Regulatory Liability - Cost of Utility Plant Removal	6,366	6,200
	Other	538	527
	<b>TOTAL DEFERRED CREDITS AND OTHER LIABILITIES</b>	<b>63,249</b>	<b>59,953</b>
	<b>CONTRIBUTIONS IN AID OF CONSTRUCTION</b>	<b>29,489</b>	<b>28,166</b>
	<b>TOTAL CAPITALIZATION AND LIABILITIES</b>	<b>\$ 375,464</b>	<b>\$ 370,267</b>

See Notes to Condensed Consolidated Financial Statements.



Index

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

	Three Months Ended March	
	2007	31, 2006
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net Income	\$ 1,769	\$ 1,812
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	1,995	1,865
Provision for Deferred Income Taxes and ITC	128	(44)
Cash Surrender Value of Life Insurance	(56)	(104)
Equity Portion of AFUDC	(54)	(52)
Changes in Assets and Liabilities:		
Accounts Receivable	(209)	1,506
Unbilled Revenues	(65)	(126)
Materials & Supplies	(119)	(110)
Prepayments	319	302
Other Assets	(210)	(229)
Accounts Payable	(468)	(1,938)
Accrued Taxes	2,369	2,415
Accrued Interest	(984)	(979)
Employee Benefit Plans	706	269
Unearned Revenue & Advanced Service Fees	8	33
Other Liabilities	267	7
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>5,396</b>	<b>4,627</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Utility Plant Expenditures, Including AFUDC of \$58 in 2007 and \$61 in 2006	(3,620)	(4,610)
Restricted Cash	599	98
Preliminary Survey & Investigation Charges	(663)	(574)
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>(3,684)</b>	<b>(5,086)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Redemption of Long-term Debt	(425)	(343)
Proceeds from Issuance of Long-term Debt	41	-
Net Short-term Bank Borrowings (Repayments)	-	3,200
Deferred Debt Issuance Expenses	(30)	-
Common Stock Issuance Expense	(15)	-
Restricted Cash	(23)	(6)
Proceeds from Issuance of Common Stock	349	406
Payment of Common Dividends	(2,272)	(1,970)
Payment of Preferred Dividends	(62)	(62)
Construction Advances and Contributions-Net	137	(451)

Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	<b>(2,300)</b>	774
NET CHANGES IN CASH AND CASH EQUIVALENTS	<b>(588)</b>	315
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	<b>5,826</b>	2,984
CASH AND CASH EQUIVALENTS AT END OF PERIOD	<b>\$ 5,238</b>	<b>\$ 3,299</b>

SUPPLEMENTAL DISCLOSURE OF NON-CASH ACTIVITY:

Utility Plant received as Construction Advances and Contributions	<b>\$ 1,610</b>	<b>\$ 1,035</b>
---	-----------------	-----------------

SUPPLEMENTAL DISCLOSURE OF CASH FLOWS INFORMATION:

Cash Paid During the Year for:

Interest	<b>\$ 2,461</b>	<b>\$ 2,562</b>
Interest Capitalized	<b>\$ (58)</b>	<b>\$ (61)</b>
Income Taxes	<b>\$ 15</b>	<b>\$ 100</b>

See Notes to Condensed Consolidated Financial Statements.

Index

**MIDDLESEX WATER COMPANY**  
**CONDENSED CONSOLIDATED STATEMENTS OF CAPITAL STOCK**  
**AND LONG-TERM DEBT**  
**(Unaudited)**

(In thousands except share and per share amounts)

	March 31, 2007	December 31, 2006
<b>Common Stock, No Par Value</b>		
Shares Authorized - 20,000,000		
Shares Outstanding - 2007 - 13,184,376	\$ 104,597	\$ 104,248
2006 - 13,168,081		
Retained Earnings	24,421	25,001
Accumulated Other Comprehensive Income (Loss), net of tax	103	94
<b>TOTAL COMMON EQUITY</b>	<b>\$ 129,121</b>	<b>\$ 129,343</b>
<b>Cumulative Preference Stock, No Par Value:</b>		
Shares Authorized - 100,000		
Shares Outstanding - None		
<b>Cumulative Preferred Stock, No Par Value</b>		
Shares Authorized - 139,497		
Convertible:		
Shares Outstanding, \$7.00 Series - 13,881	1,457	1,457
Shares Outstanding, \$8.00 Series - 12,000	1,399	1,399
Nonredeemable:		
Shares Outstanding, \$7.00 Series - 1,017	102	102
Shares Outstanding, \$4.75 Series - 10,000	1,000	1,000
<b>TOTAL PREFERRED STOCK</b>	<b>\$ 3,958</b>	<b>\$ 3,958</b>
<b>Long-term Debt</b>		
8.05%, Amortizing Secured Note, due December 20, 2021	\$ 2,873	\$ 2,896
6.25%, Amortizing Secured Note, due May 22, 2028	8,890	8,995
6.44%, Amortizing Secured Note, due August 25, 2030	6,556	6,627
6.46%, Amortizing Secured Note, due September 19, 2031	6,837	6,907
4.22%, State Revolving Trust Note, due December 31, 2022	723	739
3.30% to 3.60%, State Revolving Trust Note, due May 1, 2025	3,100	3,100
3.49%, State Revolving Trust Note, due January 25, 2027	603	598
4.03%, State Revolving Trust Note, due December 1, 2026	951	914
4.00% to 5.00%, State Revolving Trust Bond, due September 1, 2021	730	730
0.00%, State Revolving Fund Bond, due September 1, 2021	567	577
First Mortgage Bonds:		
5.20%, Series S, due October 1, 2022	12,000	12,000
5.25%, Series T, due October 1, 2023	6,500	6,500
6.40%, Series U, due February 1, 2009	15,000	15,000
5.25%, Series V, due February 1, 2029	10,000	10,000
5.35%, Series W, due February 1, 2038	23,000	23,000

Edgar Filing: MIDDLESEX WATER CO - Form 10-Q

0.00%, Series X, due September 1, 2018	<b>636</b>	647
4.25% to 4.63%, Series Y, due September 1, 2018	<b>820</b>	820
0.00%, Series Z, due September 1, 2019	<b>1,428</b>	1,455
5.25% to 5.75%, Series AA, due September 1, 2019	<b>1,890</b>	1,890
0.00%, Series BB, due September 1, 2021	<b>1,774</b>	1,805
4.00% to 5.00%, Series CC, due September 1, 2021	<b>2,090</b>	2,090
5.10%, Series DD, due January 1, 2032	<b>6,000</b>	6,000
0.00%, Series EE, due September 1, 2024	<b>7,420</b>	7,482
3.00% to 5.50%, Series FF, due September 1, 2024	<b>8,735</b>	8,735
0.00%, Series GG, due September 1, 2026	<b>1,750</b>	1,750
4.00% to 5.00%, Series HH, due September 1, 2026	<b>1,950</b>	1,950
<b>SUBTOTAL LONG-TERM DEBT</b>	<b>132,823</b>	133,207
Less: Current Portion of Long-term Debt	<b>(2,553)</b>	(2,501)
<b>TOTAL LONG-TERM DEBT</b>	<b>\$ 130,270</b>	\$ 130,706

See Notes to Condensed Consolidated Financial Statements.

Index

**MIDDLESEX WATER COMPANY**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1 – Summary of Significant Accounting Policies**

Organization – 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), and Utility Service Affiliates (Perth Amboy) Inc. (USA-PA). 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 2006 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 March 31, 2007 and the results of operations for the three month periods ended March 31, 2007 and 2006, and cash flows for the three month periods ended March 31, 2007 and 2006. Information included in the Balance Sheet as of December 31, 2006 has been derived from the Company's audited consolidated financial statements for the year ended December 31, 2006.

Certain reclassifications have been made to the prior year financial statements to conform with the current period presentation.

**Recent Accounting Pronouncements**– In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48) “Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109,” to clarify certain aspects of accounting for uncertain tax positions, including recognition and measurement of those tax positions. This interpretation was effective for fiscal years beginning after December 15, 2006 (January 1, 2007 for the Company). The adoption of this interpretation had no impact on the Company's financial position, results of operations, or cash flows.

In September 2006, the FASB'S Emerging Issues Task Force reached a consensus on EITF Issue No. 06-5, “Accounting for Purchases of Life Insurance - Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin No. 85-4, Accounting for Purchases of Life Insurance” (“EITF 06-5”). EITF 06-5 provides clarification for determining the amounts that could be realized by policyholders in accounting for life insurance contracts. EITF 06-5 is effective for fiscal years beginning after December 15, 2006 (January 1, 2007 for the Company). Adoption of EITF 06-5 had no material impact on the Company's consolidated financial statements.

**Note 2 – Rate Matters**

Middlesex filed for an \$8.9 million, or 16.5% base rate increase with the New Jersey Board of Public Utilities (BPU) on April 18, 2007. The requested increase is intended to recover increased costs of operations, maintenance, labor and benefits, purchased power, purchased water and taxes, as well as capital investment of approximately \$23.0 million since June 2005. We cannot predict whether the BPU will ultimately approve, deny, or reduce the amount of our request. We do not expect a decision on this matter until the first quarter of 2008.

In accordance with the tariff established for Southern Shores, an annual rate increase of 3% was implemented on January 1, 2007. The increase cannot exceed the lesser of the regional Consumer Price Index or 3%. The contracted rate schedule is set to expire on December 31, 2007. The Company is in the process of renegotiating the rate schedule.

5

---

Index**Note 3 – Capitalization**

**Common Stock**—During the three months ended March 31, 2007, there were 16,295 common shares (\$0.3 million) issued under the Company's Dividend Reinvestment and Common Stock Purchase Plan (DRP). Middlesex has filed with the BPU an application to increase the number of shares authorized under the DRP from 1.7 million to 2.3 million shares. A decision on this matter is expected during the second quarter of 2007.

**Long-term Debt**— Middlesex filed an application with the BPU seeking approval to issue up to \$4.0 million of first mortgage bonds through the New Jersey Environmental Infrastructure Trust under the New Jersey State Revolving Fund (SRF) program. If approved by the BPU, the Company expects to complete the transaction in November 2007. Proceeds from this financing will be used for the ongoing main cleaning and lining project in 2008.

**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 March 31,			
<b>Basic:</b>	2007	Shares	2006	Shares
Net Income	\$ 1,769	13,176	\$ 1,812	11,594
Preferred Dividend	(62)		(62)	
Earnings Applicable to Common Stock	\$ 1,707	13,176	\$ 1,750	11,594
<b>Basic EPS</b>	<b>\$ 0.13</b>		<b>\$ 0.15</b>	
<b>Diluted:</b>				
Earnings Applicable to Common Stock	\$ 1,707	13,176	\$ 1,750	11,594
\$7.00 Series Preferred Dividend	24	167	24	167
\$8.00 Series Preferred Dividend	24	164	24	164
Adjusted Earnings Applicable to Common Stock	\$ 1,755	13,507	\$ 1,798	11,925
<b>Diluted EPS</b>	<b>\$ 0.13</b>		<b>\$ 0.15</b>	

Index**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 and Delaware. 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 the states of New Jersey and Delaware with respect to utility service 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.

	(In Thousands)	
	Three Months Ended	
	March 31,	
	2007	2006
Operations by Segments:		
Revenues:		
Regulated	\$ 16,688	\$ 16,001
Non – Regulated	2,345	2,259
Inter-segment Elimination	(45)	(30)
Consolidated Revenues	\$ 18,988	\$ 18,230
Operating Income:		
Regulated	\$ 3,466	\$ 3,703
Non – Regulated	256	270
Consolidated Operating Income	\$ 3,722	\$ 3,973
Net Income:		
Regulated	\$ 1,636	\$ 1,666
Non – Regulated	133	146
Consolidated Net Income	\$ 1,769	\$ 1,812
Capital Expenditures:		
Regulated	\$ 3,525	\$ 4,591
Non – Regulated	95	19
Total Capital Expenditures	\$ 3,620	\$ 4,610
	As of	As of
	March	December 31,
	31,	<u>2006</u>
	<u>2007</u>	
Assets:		
Regulated	\$ 371,182	\$ 366,149
Non – Regulated	7,105	6,808
Inter-segment Elimination	(2,823)	(2,690)
Consolidated Assets	\$ 375,464	\$ 370,267





Index

**Note 6 – Short-term Borrowings**

As of March 31, 2007, the Company had established lines of credit aggregating \$37.0 million. At March 31, 2007, the Company had no outstanding borrowings under these credit lines.

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**

Guarantees - USA-PA operates the City of Perth Amboy, New Jersey (Perth Amboy) water and wastewater systems under contract through June 30, 2018. The agreement was effected under New Jersey's Water Supply Public/Private Contracting Act and the New Jersey Wastewater Public/Private Contracting Act. Under the agreement, USA-PA receives a fixed fee and in addition, a variable fee based on increased system billing. Scheduled fixed fee payments for 2007 are \$7.8 million. The fixed fees will increase over the term of the contract to \$10.2 million.

In connection with the agreement Perth Amboy, through the Middlesex County Improvement Authority, issued approximately \$68.0 million in three series of bonds. Middlesex guaranteed one of those series of bonds, designated the Series C Serial Bonds, in the principal amount of approximately \$26.3 million. Perth Amboy guaranteed the two other series of bonds. The Series C Serial Bonds have various maturity dates with the final maturity date on September 1, 2015. As of March 31, 2007, approximately \$23.4 million of the Series C Serial Bonds remained outstanding.

Middlesex is obligated to perform under the guarantee in the event notice is received from the Series C Serial Bonds trustee of an impending debt service deficiency. If Middlesex funds any debt service obligations as guarantor, Perth Amboy is required to reimburse the Company. There are other provisions in the agreement that make it unlikely that we would be required to perform under the guarantee, such as scheduled annual rate increases for water and wastewater services as well as rate increases that may be implemented at anytime by Perth Amboy. In the event revenues from customers could not satisfy the reimbursement requirements, Perth Amboy has Ad Valorem taxing powers, which could be used to raise the needed amount.

Water Supply - Middlesex has an agreement with the New Jersey Water Supply Authority (NJWSA) for the purchase of untreated water through November 30, 2023, which provides for an average purchase of 27 million gallons per 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, 2011, provides for the minimum purchase of 3 mgd of treated water with provisions for additional purchases.

Index

Purchased water costs are shown below:

	(In Thousands)	
	Three Months Ended March 31,	
	2007	2006
<b>Purchased Water</b>		
Treated	\$ 460	\$ 462
Untreated	598	567
<b>Total Costs</b>	<b>\$ 1,058</b>	<b>\$ 1,029</b>

Construction – The Company may spend up to \$32.1 million on its construction program in 2007.

Litigation – In July 2005, Tidewater received a notice of violation and request for corrective action issued by the Delaware State Fire Marshal regarding the alleged failure of one of the community water systems operated by Tidewater to meet Delaware fire protection requirements. Tidewater appealed the Fire Marshal’s decision with the Delaware State Fire Prevention Commission (the “SFPC”) and, in November 2005, the SFPC denied Tidewater’s appeal. In December 2005, Tidewater filed an appeal of the SFPC’s decision with the Sussex County Superior Court in Delaware, which is still pending. There are approximately 67 of our other systems that may not meet the Delaware Fire Marshal’s recent interpretation of the fire protection requirements. If the Delaware Fire Marshal’s interpretation of the regulations is upheld upon appeal, we may be required to make corrections to the system at issue and the Delaware Fire Marshal could issue notices of violation and requests for corrective action for some or all of the approximately 67 other community systems. At this time, we cannot predict how many community water systems would ultimately require corrective action if our appeal is unsuccessful nor can we predict the timing and the cost of any required corrective actions. We will apply to the PSC to increase base rates to recover the costs of any such corrective actions. However, if corrective actions need to be taken at several community water systems, our costs could be significant, and to the extent the PSC does not approve rate increases to offset these costs, or if there is a significant delay in receiving approval for such rate increases, such costs could have a material adverse effect on our operating results.

The Court action is currently on hold while the parties, with the assistance of a mediator, have met in an attempt to resolve as many open issues as possible. If any significant issues remain open after these discussions, they will be referred back to the Court for ultimate decision.

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.

#### **Note 8 – Employee Retirement Benefit Plans**

**Pension** – The Company has a noncontributory defined benefit pension plan, which covers all employees with more than 1,000 hours of service. The Company expects to make cash contributions of \$1.5 million to the plan in the second quarter of 2007. The Company also maintains an unfunded supplemental retirement benefit plan



Index

for certain active and retired company officers and currently pays \$0.3 million in annual benefits to the retired participants.

**Postretirement Benefits Other Than Pensions**– The Company maintains a postretirement benefit plan other than pensions for substantially all of its retired employees. Coverage includes healthcare and life insurance. Retiree contributions are dependent on credited years of service. The Company expects to make cash contributions to the plan of approximately \$1.6 million beginning in the third quarter of 2007.

The following table sets forth information relating to the Company's periodic costs for its retirement plans.

	(In Thousands)			
	<u>Pension Benefits</u>		<u>Other Benefits</u>	
	Three Months Ended March 31,			
	2007	2006	2007	2006
Service Cost	\$ 320	\$ 310	\$ 185	\$ 177
Interest Cost	453	430	212	217
Expected Return on Assets	(456)	(415)	(135)	(90)
Amortization of Unrecognized Losses	66	57	68	129
Amortization of Unrecognized Prior Service Cost	2	-	-	-
Amortization of Transition Obligation	-	-	34	34
Net Periodic Benefit Cost	\$ 385	\$ 382	\$ 364	\$ 467

**Note 9 – Stock Based Compensation**

The Company maintains a Restricted Stock Plan, under which 63,837 shares of the Company's common stock are held in escrow by the Company as of March 31, 2007 for key employees. Such stock is subject to forfeiture by the employee in the event of termination of employment within five years of the award other than as a result of retirement, death, disability or change in control. The maximum number of shares authorized for grant under this plan is 240,000 shares. There were no grants, vesting or forfeitures of restricted stock during the three months ended March 31, 2007.

The Company recognizes compensation expense at fair value for its restricted stock awards in accordance with SFAS 123(R). Compensation expense is determined by the market value of the stock on the date of the award and is being amortized over a five-year period. Compensation expense for the three months ended March 31, 2007 and 2006 was \$0.1 million. Total unearned compensation related to restricted stock was \$0.7 million at March 31, 2007.

Index**Note 10 – Other Comprehensive Income**

Comprehensive income was as follows:

	(In Thousands)	
	Three Months Ended	
	March 31,	
	2007	2006
Net Income	\$ 1,769	\$ 1,812
Other Comprehensive Income:		
Change in Value of Equity Investments, Net of Income Tax	8	1
Other Comprehensive Income	8	1
Comprehensive Income	\$ 1,777	\$ 1,813

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 the Company included elsewhere herein and with the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

**Forward-Looking Statements**

Certain statements contained in this quarterly 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;
- statements as to the Company’s expected liquidity needs during fiscal 2007 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 base rate increase requests;
  - new or additional water quality standards;
  - weather variations and other natural phenomena;
- the existence of attractive acquisition candidates and the risks involved in pursuing those acquisitions;
  - acts of war or terrorism;
  - significant changes in the housing starts in Delaware;
  - the availability and cost of capital resources; and
  - other factors discussed elsewhere in this prospectus.





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, 2006.

**Overview**

The Company has operated as a water utility in New Jersey since 1897, and in Delaware, through our wholly-owned subsidiary, Tidewater, since 1992. We are in the business of collecting, treating, distributing and selling water for residential, irrigation, 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. Our utility companies are regulated as to rates charged to customers for water and wastewater services in New Jersey and Delaware, as to the quality of service provided and as to certain other matters. Our USA, USA-PA and White Marsh subsidiaries are not regulated utilities.

Our New Jersey water utility system (the Middlesex System) provides water services to approximately 59,200 retail customers, primarily in central New Jersey. The Middlesex System also provides water service under contract to municipalities in central New Jersey with a total population of approximately 303,000. Through our subsidiary, USA-PA, we operate the water supply system and wastewater collection system for the City of Perth Amboy, New Jersey. Pinelands Water and Pinelands Wastewater provide water and wastewater services to residents in Southampton Township, New Jersey.

Tidewater and Southern Shores provide water services to approximately 30,000 retail customers in New Castle, Kent, and Sussex Counties, Delaware. Our TESI subsidiary provides regulated wastewater service to approximately 120 residential retail customers. White Marsh serves approximately 5,000 customers under unregulated operating contracts with various owners of small water and wastewater systems in Kent and Sussex Counties.

Our USA subsidiary provides customers both inside and outside of our service territories a service line maintenance program called LineCare<sup>SM</sup>. In the first quarter of 2007 we introduced a similar program for wastewater customers called LineCare+<sup>SM</sup>.

The majority of our revenue is generated from regulated water services to customers in our franchise 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 since the end of 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.

Index**Recent Developments***Rate Increases*

Middlesex filed for an \$8.9 million, or 16.5% base rate increase with the New Jersey Board of Public Utilities (BPU) on April 18, 2007. The requested increase is intended to recover increased costs of operations, maintenance, labor and benefits, purchased power, purchased water and taxes, as well as capital investment of approximately \$23.0 million since June 2005. We cannot predict whether the BPU will ultimately approve, deny, or reduce the amount of our request. We do not expect a decision on this matter until the first quarter of 2008.

In accordance with the tariff established for Southern Shores, an annual rate increase of 3% was implemented on January 1, 2007. The increase cannot exceed the lesser of the regional Consumer Price Index or 3%. The contracted rate schedule is set to expire on December 31, 2007. The Company is in the process of renegotiating the rate schedule.

**Operating Results by Segment**

The Company has two operating segments, Regulated and Non-Regulated. Our Regulated segment contributed 88% of total revenues and 92% of net income for the three months ended March 31, 2007 and 2006. The discussion of the Company's results of operations is on a consolidated basis, and includes significant factors by subsidiary. The segments in the tables included below consist of the following companies: Regulated- Middlesex, Tidewater, Pinelands, Southern Shores, and TESI; Non-Regulated- USA, USA-PA, and White Marsh.

**Results of Operations – Three Months Ended March 31, 2007**

	(In Thousands)					
	<u>Three Months Ended March 31,</u>					
	<u>2007</u>		<u>2006</u>			
	Regulated	Non-Regulated	Total	Regulated	Non-Regulated	Total
Revenues	\$ 16,688	\$ 2,300	\$ 18,988	\$ 16,001	\$ 2,229	\$ 18,230
Operations and maintenance expenses	9,216	1,954	11,170	8,512	1,873	10,385
Depreciation expense	1,814	31	1,845	1,641	27	1,668
Other taxes	2,192	59	2,251	2,145	59	2,204
<b>Operating income</b>	<b>3,466</b>	<b>256</b>	<b>3,722</b>	<b>3,703</b>	<b>270</b>	<b>3,973</b>
Other income	333	---	333	169	---	169
Interest expense	1,359	25	1,384	1,488	27	1,515
Income taxes	804	98	902	718	97	815
<b>Net income</b>	<b>\$ 1,636</b>	<b>\$ 133</b>	<b>\$ 1,769</b>	<b>\$ 1,666</b>	<b>\$ 146</b>	<b>\$ 1,812</b>

Operating revenues for the three months ended March 31, 2007 increased \$0.8 million, or 4.2%, from the same period in 2006 due to customer growth and rate relief in our Delaware service territories. The implementation of a 15% interim rate increase in June 2006 and the 12% final increase on February 28, 2007 provided an additional \$0.5 million of revenues. Customer growth contributed \$0.3 million of revenues. Consumption



Index

revenues in our Middlesex system were lower by \$0.1 million. This decline was offset by revenue increases in our other subsidiaries.

While we anticipate continued organic customer and consumption growth, particularly in our Delaware systems, such growth and increased consumption cannot be guaranteed. Revenues from our water systems are highly dependent on the effects of weather, which may adversely impact future consumption despite customer growth. Customer growth in both the regulated water and wastewater businesses are dependent upon economic conditions surrounding new housing as well as developer construction timetables. Appreciable organic customer and consumption growth is less likely in our New Jersey systems due to the extent to which our service territory is developed.

Operation and maintenance expenses for the three months ended March 31, 2007 increased \$0.8 million or 7.6%, compared to the same period in 2006 with labor and benefit costs accounting for \$0.6 million of the increase. Continued growth of our Delaware systems required additional personnel, while severe winter weather related system repairs resulted in increased overtime costs in New Jersey. All other operation expenses increased \$0.2 million.

Depreciation expense increased \$0.2 million, or 10.6%, primarily as a result of a higher level of utility plant in service since March 31, 2006.

Interest expense decreased \$0.1 million, primarily due to no short-term borrowings for the quarter compared to the prior year.

Although net income decreased for the quarter ended March 31, 2007 compared to the same period in 2006, income taxes increased \$0.1 million. This increase was due to a higher level of financial reporting expenses that are excluded as deductions in the calculation of our income tax liability.

Net income decreased by less than \$0.1 million. Basic and diluted earnings per share decreased from \$0.15 to \$0.13 due to the higher number of shares outstanding. Middlesex sold and issued 1.5 million shares of its common stock in November 2006.

**Liquidity and Capital Resources**

Cash flows from operations are largely dependent on three factors: the impact of weather on water sales, adequate and timely rate increases, and customer growth. The effect of those factors on net income is discussed in results of operations. For the three months ended March 31, 2007, cash flows from operating activities were \$5.4 million, an increase of \$0.7 million from the prior year. This increase was mostly attributable to the timing of payments for employee medical retirement benefits. The \$5.4 million of net cash flow from operations enabled us to fund all of our utility plant expenditures internally for the period.

Our capital spending program for 2007 is currently estimated to be \$32.1 million, which is lower by \$22.5 million than the amount previously reported in our 2006 Annual Report on Form 10-K. This decrease is due primarily to the slowing of new residential and commercial development in our Delaware service territories. Included in our revised estimate for 2007 are: \$12.1 million for additions and improvements to our Delaware water systems, including the construction of several storage tanks and the creation of new wells and interconnections. We expect to spend approximately \$6.0 million for infrastructure additions and acquisitions for our Delaware wastewater systems. We expect to spend \$3.9 million for the RENEW program, to clean and

Index

cement line approximately nine miles of unlined water mains in the Middlesex system. There remains a total of approximately 120 miles of unlined mains in the 732-mile Middlesex system. The capital program also includes \$10.1 million for scheduled upgrades to our existing systems in New Jersey. These upgrades consist of \$1.9 million for improvements to existing utility plant, \$5.6 million for mains, \$0.7 million for service lines, \$0.4 million for meters, \$0.5 million for hydrants, and \$1.0 million for other infrastructure needs.

To fund our capital program in 2007, we will utilize remaining proceeds from the November 2006 common stock offering, internally generated funds and funds available under existing New Jersey State Revolving Fund (SRF) program loans (currently, \$3.4 million) and Delaware SRF program loans (currently, \$2.1 million). These programs provide low cost financing for projects that meet certain water quality and system improvement benchmarks. We also expect to utilize short-term borrowings through \$37.0 million of available lines of credit with several financial institutions. As of March 31, 2007, there were no amounts outstanding against the lines of credit.

We periodically issue shares of common stock in connection with our dividend reinvestment and stock purchase plan (DRP). From time to time, we may issue additional equity to reduce short-term indebtedness, fund our capital program, and for other general corporate purposes.

We currently project that we may be required to expend between \$70 million and \$100 million for capital projects in 2008 and 2009 combined. To the extent possible and because of the favorable interest rates available to regulated water utilities, we will finance our capital expenditures under SRF loan programs. We also expect to use internally generated funds, proceeds from the DRP and proceeds from additional common stock offerings, as needed to maintain an appropriate capital structure balance.

In addition to the effect of weather conditions on revenues, increases in certain operating costs will impact our liquidity and capital resources. As described above, we have recently received rate relief for Tidewater and Southern Shores. Changes in operating costs and timing of capital projects will have an impact on revenues, earnings, and cash flows and will also impact the timing of filings for future rate increases.

**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 capital program is partially financed with 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 Amortizing Secured Notes and First Mortgage Bonds, which have maturity dates ranging from 2009 to 2038. Over the next twelve months, approximately \$2.6 million of the current portion of sixteen existing long-term debt instruments will mature. Applying a hypothetical change in the rate of interest of 10% on those borrowings would not have a material effect on earnings.

**Item 4. Controls and Procedures**

As required by Rule 13a-15 under 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



Index

disclosure controls and procedures are effective as of the end of the period covered by this Report. There have been no changes in the Company's internal controls, or in other factors which materially affected internal controls during the quarter ended March 31, 2007.

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.

**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

Reference is made to the Company's Annual Report on Form 10-K for the year ended December 31, 2006. Note 7 to the unaudited Condensed Consolidated Financial Statements for the period ended March 31, 2007, included in Part I of this Quarterly Report on Form 10-Q, is hereby incorporated by reference.

**Item 1A. Risk Factors**

We expect our revenues to increase from customer growth in Delaware for our regulated water operations and, to a lesser degree, our regulated wastewater operations as a result of the anticipated construction and sale of new housing units in the territories we serve. Although the residential building market in Delaware has experienced growth in recent years, this growth may not continue in the future. If housing starts in the Delaware territories we serve decline significantly as a result of economic conditions or otherwise, our revenue growth may not meet our expectations and our financial results could be negatively impacted.

Except as described above, information about risk factors for the three months ended March 31, 2007 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, 2006.

**Item 2. Changes in Securities**

None.

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Submission of Matters to a Vote of Security Holders**

None.

**Item 5. Other Information**

None.





*Index*

**Item 6.**

**Exhibits**

31 Section 302 Certification by Dennis W. Doll pursuant to Rules 13a-14 and 15d-14 of the Securities Exchange Act of 1934.

31.1 Section 302 Certification by A. Bruce O'Connor pursuant to Rules 13a-14 and 15d-14 of the Securities Exchange Act of 1934.

32 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.

32.1 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.

*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

Date: May 8, 2007