Joint Venture of the Charter Municipalities of the Municipal Review Committee, Inc.

Management's Discussion and Analysis of Financial Statements for Calendar Year 2011

This report provides a discussion and analysis of the financial performance of the Joint Venture of the Charter Municipalities of the Municipal Review Committee, Inc. (MRC), for the fiscal year ended December 31, 2011. Please review it in conjunction with the financial statements and associated notes for the Joint Venture that follow this section.

1.0 Financial Highlights

- Distributed $4.76 million to Charter Municipalities, thereby achieving the target values for per-ton waste disposal costs for the Equity Charter Municipalities of $45 per ton in the first two quarters of 2011 and $46 per ton in the last two quarters of 2011; and for the New Charter Municipalities of $54 per ton throughout the year.
- Sustained ownership interest in the PERC partnership at 25.5214 percent of the limited partnership shares.
- Supported refinancing of PERC's outstanding debt with a bank loan from TDBank. The refinancing enabled PERC to reduce its requirement for cash reserves from $10.0 million to $2.0 million. Consistent with the financing agreements, the MRC received one-third of the cash released when the reserve requirement was reduced ($2.667 million).
- Maintained a balance of $20.965 million in the Tip Fee Stabilization Fund as of the end of 2011 and managed the investment of the fund balance. The MRC remains positioned to utilize the Tip Fee Stabilization Fund to stabilize tipping fees through and beyond the expiration of existing business arrangements for waste disposal in 2018.
- Increased the balance in the MRC Operating Budget Stabilization Fund to $2,658,750 by the end of 2011, largely through a deposit into the fund of $2.0 million of the MRC's share of funds released from reserve after the PERC refinancing. The MRC Operating Budget Stabilization Fund provides the MRC with resources to be prepared for the costs of unforeseen contingencies.
- Sustained Net Assets of $37.243 million at the close of 2011.

2.0 Overview of the Financial Statements

The basic financial statements of the Joint Venture are presented herein in a format that is consistent with the requirements of the Government Accounting Standards Board. The financial statements present the following two different views of the Joint Venture:

1. The Government Funds Balance Sheet / Statement of Net Assets (Balance Sheet) identifies and presents values for the key general fund assets and liabilities of the Joint Venture as of the end of the calendar year (see Table 1). The Balance Sheet also identifies and presents adjustments for long-term assets and fund balances that are not readily available for application to expenditures, and identifies and presents Net Assets after application of the adjustments.

   The key General Fund assets shown on the Balance Sheet include the following:

   - Cash and cash equivalents, which are held in a Custody Account at Bangor Savings Bank.
   - The Tip Fee Stabilization Fund and the MRC Operating Budget Stabilization Fund, which are invested in a set of bonds of varying maturities and managed by an investment advisor, Merrill Bank.

   The Balance Sheet presents the Equity Charter Municipality investment in PERC as a long-term asset that is not readily available for use to meet expenditures. This investment is valued on the basis of the equity investment method as of the start of 2011.

   The Balance Sheet does not account for the Charter Municipalities' share of the reserve funds held by the Trustee as part of the security for the bonds, which are likely to continue to be held until those bonds are retired. Such funds are considered contingent assets under generally accepted accounting principles and are therefore presented in a footnote rather than as a General Fund asset.

   The key General Fund liability shown on the Balance Sheet for the end of 2011 is the distributions payable to the Charter Municipalities in the first quarter of 2012. The remaining assets include the value of the investment in PERC and the values of the various funds in excess of the distributions payable.

2. The Statement of Governmental Fund Revenue, Expenditures and Changes in Fund Balances / Statement of Activities (Income Statement) identifies and presents revenues and expenditures over the course of calendar year 2011 (see Table 2). The Income Statement also identifies and presents the changes in Net Assets over the course of 2011.

   The General Fund revenues shown on the Income Statement include the following:

   - Performance Credits as a result of PERC operations that were distributed to the MRC on behalf of the Charter Municipalities.
   - Partnership distributions as a result of PERC operations (Net Cash Flow) that were distributed to the MRC on behalf of the Equity Charter Municipalities that own limited partnership shares in the PERC partnership.

- Appreciation of investments, interest income and changes in investment fund values.

The General Fund expenditures include only the distributions to the Charter Municipalities. The Income Statement includes one adjustment to reconcile the excess of revenues over expenditures with the change in Net Assets: namely, the change in the cash distributions payable each quarter.

3.0 Analysis of Overall Financial Position and Results of Operations

The MRC manages the assets of the Charter Municipalities in order to achieve two key objectives. First, the MRC seeks to distribute sufficient cash on a quarterly basis to the Charter Municipalities in order to reduce their net cost for disposal of waste at the PERC facility to a pre-determined system-wide average per-ton net cost known as the "target value." In 2011, the target values for Equity Charter Municipalities were $45 per ton in the first two quarters and $46 per ton in the last two quarters, which represented the first increase in the target value since 1998. The target value for the New Charter Municipalities was $54 per ton throughout the year. Second, the MRC seeks to position the Charter Municipalities to continue to achieve target values to be determined by the MRC Board of Directors through 2018 by (a) ensuring that the Facility maintains its performance in providing waste disposal services; (b) maintaining an appropriate ownership position in the PERC partnership; (c) setting aside sufficient funds in the Tip Fee Stabilization Fund, and (d) managing other Net Assets,

The MRC distributed sufficient cash in each of the four quarters of 2011 to achieve the target values as shown in the following table:

Quarter	*1*	*2*	*3*	*4*
Tip fee, prior quarter	$73.00	$74.20	$71.50	$71.00
Distribution to Equity Charter Municipalities	$28.00	$29.20	$25.50	$25.00
Net disposal cost for Equity Charter Municipalities, system weighted average	$45.00	$45.00	$46.00	$46.00
Target value for Equity Charter Municipalities	$45.00	$45.00	$46.00	$46.00
Distribution to New Charter Municipalities	$19.00	$20.20	$17.50	$17.00
Net disposal cost for New Charter Municipalities	$54.00	$54.00	$54.00	$54.00
Target value for New Charter Municipalities	$54.00	$54.00	$54.00	$54.00

All values are in dollars per ton.

At the end of 2011, the balance in the Tip Fee Stabilization Fund was $20.965 million. Accounting for this balance, and accounting for anticipated Performance Credits, and PERC partnership distributions (assuming that the PERC facility will continue to perform in the future as it has in the past few years), as of the end of 2011 the MRC continued to project that the Charter Municipalities would have sufficient resources to continue to achieve the existing target values through 2018.

The MRC has recognized that maintaining the existing target values unchanged would draw down almost entirely the balance in the Tip Fee Stabilization Fund by 2018, thereby depleting the capability to stabilize tip fees should the existing arrangements be extended beyond 2018. Note that the MRC is projecting that tipping fees in any extended arrangement would need to be significantly higher than the current target values for a variety of reasons, most particularly the projected decline in electricity revenues after the expiration in 2018 of the existing sales agreement.

In this context, at its October 2010 meeting, the MRC Board of Directors voted to adopt a Target Value Step Increase Implementation Plan (the "Plan") to implement an increase in target values on an annual basis through 2018. The Plan establishes increased target values for the Equity Charter Municipalities as follows:

$46 per ton as of July 1, 2011
$48 per ton as of July 1, 2012
$51 per ton as of July 1, 2013
$55 per ton as of July 1, 2014
$59 per ton as of July 1, 2015
$63 per ton as of July 1, 2016
$67 per ton as of July 1, 2017

The target value for the New Charter Municipalities would stay at $54 per ton through July 1, 2014, then increase in accordance with the scheduled set forth above thereafter.

The intent of these increases is to avoid a spike in disposal costs and prepare the Charter Municipalities for higher post-2018 disposal costs; and to maintain funds in reserve for use in enhancing the negotiating position and capacity of the MRC to make available the best possible post-2018 extension/purchase terms for the Charter Municipalities.

4.0 Significant Transactions

The MRC managed the following transactions on a routine basis during the year:

- Receipt of Performance Credits from PERC on a monthly basis.
- Receipt of partnership distributions from PERC on a monthly basis.
- Distribution of cash to Charter Municipalities to achieve the target values on a quarterly basis.
- Transfers of funds to the Custody Account from the Tip Fee Stabilization Fund in the first and second quarters of 2011.

The MRC managed the following significant one-time transactions related to the refinancing of the outstanding bonds associated with the PERC facility, which occurred in June 2011:

- Received into the Custody Account \$2.667 million in cash that had been released from reserve funds held by the trustee to the bond financing.
- Transferred \$2.0 million of such cash into the MRC Operating Budget Stabilization Fund.

As of the end of 2011, the remaining \$0.667 million in cash that had been released from reserve funds held by the trustee to the bond financing remained in the Custody Account. The MRC Board was negotiating with the private partners in PERC an agreement to swap such cash that had been released to the MRC from reserves for an identical amount of cash being held by the private partners as part of the reserves for the loan financing. No such agreement had been fully negotiated as of the end of 2011.

During 2011, the Charter Municipalities incurred a penalty of \$98,326.82 to PERC for a shortfall in deliveries of municipal solid waste as compared to the Guaranteed Annual Tonnage. The penalty was initially paid by the MRC, then reimbursed by the Charter Municipalities having shortfalls through direct payments, offsets, and debits against account balances.

5.0 Capital Assets and Debt Administration

The MRC had no outstanding debt in 2011.

The MRC no longer receives payments of principal and interest on the Promissory Note from Bangor Hydro as had been the case in 2008 and previous years. Bangor Hydro made the last payment of principal and interest on the Note in May 2008.

6.0 Economic Factors and Significant Foreseeable Future Conditions

The MRC notes the following significant foreseeable future conditions with the potential to affect performance in 2011:

- <u>Facility maintenance costs.</u> The Facility Operator, acting for PERC, LP, is planning to incur major maintenance expenditures for the Facility to ensure that operations continue through and beyond 2018. Implementation of capital and maintenance investments in the Facility's major processing and production systems will continue to be an integral factor in maintaining economic performance in 2012 and thereafter. The costs of such investments have increased in recent years. There is no assurance that the level of future investment in capital and major maintenance projects at the Facility as required to maintain current levels of performance will not exceed projections in the coming years.

As a facility with a nameplate generating capacity of more than 20 MW, the Facility is required to comply with new requirements for the reliability and security of the regional electric grid as overseen by the Northeast Power Coordinating Council (NPCC), the North American Electricity Reliability Corporation (NERC) and other related organizations of applicable jurisdiction. These requirements, which can require changes to physical plant as well as development and documentation of operating procedures, continue to evolve and expand. There is no assurance regarding the nature of the full set of NPCC and NERC requirements that the Facility might be required to implement, nor is there assurance regarding the cost and impact on performance of satisfying such requirements.

- Waste acquisition. In 2011, PERC received 117,088 tons of municipal solid waste (MSW) from commercial and spot market arrangements to supplement the 183,274 tons of MSW delivered by Charter Municipalities and 13,426 tons of MSW delivered by other municipalities. MSW deliveries to PERC by Charter Municipalities declined by 3,583 tons from 2010 to 2011, a drop of 2.0 percent, and, per PERC's records, fell short by 2,561 tons of the guaranteed annual tonnage (GAT) that the Charter Municipalities, in aggregate, were obligated to deliver to PERC in 2011 to avoid shortfall penalties. Whether such shortfall penalties will be assessed, and the magnitude of such penalties, had not been finalized as of this writing.

  Quantities of MSW available to the PERC facility have declined for a number of reasons, including lingering effects of the economic downturn; waste reduction or diversion through pay-as-you-throw and similar programs; and increased recycling resulting from new single-stream programs. There is no assurance that MSW from the commercial and spot market arrangements will continue to be available to PERC in the future in the same quantities as it was acquired in the past, nor is there assurance that the quantities of MSW delivered by the Charter Municipalities, which include significant amounts of MSW originating from commercial sources within their borders and delivered to the account of the municipalities, will not decline from delivery levels in prior years. Thus, there is no assurance that the Charter Municipalities will not be exposed to further delivery shortfall penalties in future years. Moreover, there is no assurance that the Charter Municipalities will not be exposed to reduced Performance Credits and partnership distributions due to reduced economic performance at PERC as a result of declines in waste deliveries.

- Competition with other disposal facilities. PERC actively competes with other disposal facilities to acquire MSW as needed to allow the facility to operate at capacity. Competing disposal facilities include the three other operating municipal waste combustion facilities in Maine; operating landfills that are permitted to accept MSW in Maine; and facilities that are located outside of Maine. Failure of PERC to attract sufficient MSW to allow the facility to operate at capacity, or loss of significant quantities of MSW to competing disposal facilities, could have a significant adverse impact on the economic performance of PERC in 2011 and thereafter, and could adversely affect the capability for Charter Municipalities to achieve the target values through 2018.

- Regulatory limits on competition. The development of new capacity for MSW disposal in Maine is restrained by two regulatory factors: namely, a regulatory ban on the permitting of new commercial solid waste disposal facilities, and contract terms and permit conditions that restrict the disposal of MSW at existing landfills. There are two landfills that, by virtue of their locations, might compete with the PERC Facility for MSW: the state-owned Juniper Ridge Landfill, which is located in Old Town, Maine, within 25 miles of the PERC Facility; and the privately-owned Crossroads Landfill, which is located in Norridgewock, Maine, approximately 75 miles from the PERC Facility. If such regulatory ban is modified or repealed, or if the contract terms and permit conditions that control how the Juniper Ridge Landfill and/or the Norridgewock Landfill accept MSW for disposal are modified, then the PERC Facility might lose significant quantities of MSW to competing disposal facilities. Such a loss could have a significant adverse impact on the economic performance of PERC in 2012 and thereafter, and could adversely affect the capability for Charter Municipalities to achieve the target values at current levels through 2018.

  On September 10, 2010, the Maine Department of Environmental Protection (Maine DEP) issued a regulatory decision that allows the Juniper Ridge Landfill to accept additional amounts of MSW for disposal. In particular, the decision allows MSW to be deposited into the landfill as "soft layer" material, which is the first layer of material to be deposited directly onto the liner that is placed at the bottom of each new landfill base cell. As a consequence of this decision, in 2011 the Juniper Ridge Landfill accepted 22,229 tons of MSW that it would not previously been allowed to accept. Appeals of this order by the MRC were unsuccessful.

  The MRC views this order by the Maine DEP as a threat that might cause significant quantities of MSW to be diverted from the PERC Facility. Such loss could have a significant adverse impact on the economic performance of PERC, and, consequently, on the Charter Municipalities, in 2012 and thereafter.

  The MRC is monitoring the progress of legislative proposals carried-over from the 2011 First Regular Legislative Session to the 2012 Second Regular Legislative Session. One legislative proposal would allow the private owner of the Crossroads Landfill, which is located in Norridgewock, Maine, approximately 75 miles from the PERC Facility, the ability to seek a significant expansion that is precluded under current law. If the legislation is passed into law in a manner that provides for the acceptance of MSW without limitation, then significant quantities of MSW might be diverted from PERC to the expanded facility. Such a loss could have a significant adverse impact on the economic performance of PERC, and, consequently, on the Charter Municipalities, in 2012 and thereafter.

- Environmental regulation. Many aspects of the operation of the Facility are subject to stringent regulation of the Maine Department of Environmental Protection (the DEP) and by other federal, state and local agencies. Thus, there is always a risk that changes in applicable, law, regulations, or regulatory policies and enforcement practices will have an adverse impact on the Facility's performance or the economics of continuing Facility operation. The Facility works diligently to comply with all applicable environmental laws, regulations, permits and policies. In addition, the MRC works jointly with PERC on an ongoing basis to monitor potential changes in applicable laws, regulations, permits and policies in order to identify initiatives that might have an adverse impact on the Facility and to ensure that such impacts are recognized and given due consideration. Nevertheless, there is no assurance that the Facility will not be adversely affected in the future by changes in applicable law, regulation, regulatory policy or enforcement practices

The products of combustion at the Facility that are emitted to the atmosphere include, among other things, carbon dioxide, which is considered a contributor to global warming and, pursuant to a 2009 ruling of the U.S. Environmental Protection Agency, is also considered a regulated pollutant. The contributions to global warming of the Facility's emissions of carbon dioxide are more than offset by two factors of its operation. First, the Facility combusts municipal solid waste that, had it been deposited in a landfill, might have caused emission to the atmosphere of methane and other greenhouse gases with a greater overall contribution to global warming than the carbon dioxide emitted from the Facility. Second, the Facility generates electricity from the combustion of waste that displaces a like amount of electricity that might have been generated from combustion of fossil fuels at facilities with emissions that contribute proportionately more to global warming than the Facility. Nonetheless, both the U.S. Congress and the U.S. Environmental Protection Agency are considering new measures to control carbon dioxide emissions and global warming that might have an adverse impact on Facility operations. There is no assurance as to what the nature or magnitude of such impacts might be.

- Electric utility regulation. In 2011, approximately 56 percent of all revenue realized by PERC was in the form of payments for electricity purchased by Bangor Hydro pursuant to a Power Purchase Agreement (PPA) that was originally executed in 1984 and is expected to remain in effect through March 31, 2018. Such purchases undertaken pursuant to the PPA in 2011 were at prices generally in excess of market rates for electricity and associated products. In recognition of the PPA prices for electricity and related contract terms, in 1998 the PPA was amended to provide cost mitigation to Bangor Hydro. Such amendment was reviewed and approved by the Maine Public Utilities Commission (the Maine PUC), which has regulatory jurisdiction over Bangor Hydro and its power purchase arrangements. The Maine PUC ruled that the above-market purchases of electricity by Bangor Hydro pursuant to the PPA qualify as "stranded costs" and has set forth a procedure for recovery of such costs on an ongoing basis. Nevertheless, there is no assurance that the Facility might not be adversely affected in the future by changes in the regulatory treatment of electricity purchases pursuant to the PPA or by changes in the procedures for recovery of stranded costs.

- Emerging technologies. The MRC is aware of numerous new technologies that are being developed to process and dispose of municipal solid waste, including approaches that utilize gasification, pyrolysis, plasma arc destruction, anaerobic digestion, thermal de-polymerization and other methods. At this point, none of these technologies has been demonstrated on a commercial basis to provide substantial economic, technical and environmental advantages for solid waste management as compared to the PERC Facility, and, although a facility has been proposed for development in Augusta, Maine, there are no facilities applying such technologies to solid waste management that are operating or under construction in Maine. Nevertheless, it is possible that such a technology will be developed and emerge in the future as a disruptive technology that is competitive with the PERC Facility, with adverse economic consequences on the Facility.