



Vallecitos Water District
Annual Financial Report
Fiscal Years Ended June 30, 2008 and 2007

Vallecitos Water District
Annual Financial Report
Fiscal Years Ended June 30, 2008 and 2007

Board of Directors as of June 30, 2008:

Tim Shell –President

Trish Hannan – Vice-President

Margaret E. Ferguson – Director

Darrell Gentry – Director

James W. Poltl – Director

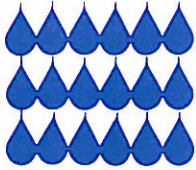
William W. Rucker – General Manager

Vallecitos Water District
Annual Financial Report
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Financial Section



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Independent Auditor's Report

Board of Directors
Vallecitos Water District
San Marcos, California

We have audited the accompanying financial statements of the Vallecitos Water District (District) as of and for the years ended June 30, 2008 and 2007, which collectively comprise the District's basic financial statements as listed in the table of contents. These basic financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these basic financial statements based on our audits.

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

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the respective financial position of the Vallecitos Water District as of June 30, 2008 and 2007, and the respective changes in net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 20, 2008 on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Management's discussion and analysis is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit this information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the District's basic financial statements. The supplemental information section is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements, and in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

October 20, 2008
Cypress, California

Charles Z. Fedak, CPA
An Accountancy Corporation

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Vallecitos Water District
Management's Discussion and Analysis
For the Years Ended June 30, 2008 and 2007

Our discussion and analysis of the Vallecitos Water District's financial performance provides an overview of the District's financial activities for the fiscal year ended June 30, 2008. Management's Discussion and Analysis (MD&A) presents financial highlights; an overview of the accompanying financial statements; an analysis of financial position and results of operations; a current-to-prior year analysis; a discussion on restrictions, commitments and limitations; a discussion on significant activity involving capital assets and long-term debt.

FINANCIAL HIGHLIGHTS

During the fiscal year ended June 30, 2008, the following highlights impacted, or have the potential to impact, the finances of the District.

- On July 12, 2007, the District converted its remaining \$63.8 million in certificates of participation from variable auction rate to fixed rate debt to reduce interest rate risk. At the time of conversion the auction rate was 3.5%. Within two months of the conversion most auction-rate issuances experienced increases to rates in the double digits. The total-all-in-cost is 4.736%. The \$1.6 million realized in the issue premium was expended toward the Meadowlark Treatment Plant expansion. The District paid debt service of \$3.0 million during the year.
- The District completed construction on the Twin Oaks 40-million-gallon reservoir and the Meadowlark Treatment Plant Expansion. Total capital spending for the year amounted to \$27.3 million compared to \$50.6 million in the prior year, \$31.8 million two years prior, and \$12.7 million three years prior.
- During the fiscal year ended June 30, 2008, new development contributed \$3.7 million in capital assets and cash to be used to fund planned capital facilities, compared to \$8.5 million in the prior year, \$9.7 million two years prior, and \$20.3 million three years prior.
- Interest earnings for 2007/08 totaled \$1.5 million compared to \$3.1 million in 2006/07 due to declining interest yields and a declining investment portfolio balance.
- Increased sewer rates, growth, and switching business customers from count-based formulas to a flow basis attributed to an increase in sewer revenues of \$1.2 million, or 14.1%, and helped offset the fiscal burden of increased regulations.
- The District added 409 active meters during the fiscal year ended June 30, 2008 – (a 2.1% increase), compared to 371 meters (a 1.9% increase) in the prior year, 492 meters (a 2.6% increase) two years prior, and 1,117 meters (a 6.2% increase) three years prior. The City of San Marcos issued building permits for 2,320 residential units in 2004, 1,344 in 2005, 447 in 2006, 273 in 2007, and 50 through September 2008.
- On June 20, 2007, the District adopted two years of rate increases – effective July 1, 2007, 6% sewer and 7.2% ready-to-serve increase, effective January 1, 2008, 6.4% increase in water commodity (mostly the wholesale pass-through), effective July 1, 2008, 10% increase in sewer and 6.7% increase in ready-to-serve, and effective January 1, 2009, 6% increase in water commodity (mostly the wholesale pass-through).
- On June 4, 2008, the District adjusted its January 1, 2009, commodity rate increase from 6% to 14% to accommodate a revised wholesale projection from Metropolitan Water District and the San Diego County Water Authority.
- Anticipated mandatory conservation due to the continued water supply shortage will have a significant impact on rate structures, revenues, and costs associated with administering programs and public awareness. Half way through the 2007/08 fiscal year, customers participating in the Interim Agricultural Water Program (IAWP) became subject to a mandatory 30% water usage cut-back.

Vallecitos Water District
Management's Discussion and Analysis
For the Years Ended June 30, 2008 and 2007

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial statements present the financial position, results of operations, and changes in cash flow from the economic resources measurement focus using the accrual basis of accounting, which is similar to the accounting basis used by for-profit entities. Each financial statement is identified and defined in this section and analyzed in subsequent sections of this MD&A.

Statements of Net Assets

The Statements of Net Assets present the District's financial position (assets and liabilities) as of June 30, 2008, and 2007. Assets in excess of liabilities (Net Assets) were \$239,818,042 and \$235,430,125 as of June 30, 2008, and 2007, respectively. In accordance with generally accepted accounting principles, capital assets acquired through purchase or construction by the District are recorded at historical cost. Capital assets contributed by development are record at fair value or developers' construction cost.

Statements of Revenues, Expenses, and Changes in Net Assets

The Statements of Revenues, Expenses, and Changes in Net Assets present the District's results of operations for the years ended June 30, 2008, and 2007. Revenues are recognized (recorded) when water or services are provided, and expenses are recognized when incurred. Operating revenues and expenses are related to the District's core activities (providing water and related services, wastewater services, and processing and delivering recycled water). Non-operating revenues and expenses (e.g. interest income, interest expenses, etc.) are not directly related to the core activities of the District. The operating loss for the year ended June 30, 2008, of \$2,945,764 is combined with net non-operating revenues of \$3,624,488 and capital contributions of \$3,709,193 to arrive at the change in net assets of \$4,387,917. The increase in net assets is added to beginning net assets of \$235,430,125 to arrive at ending net assets of \$239,818,042 as of June 30, 2008.

Operating income / (loss)	\$ (2,945,764)
Nonoperating revenues / (expenses)	3,624,488
Capital contributions	<u>3,709,193</u>
Change in net assets	4,387,917
Beginning net assets	<u>235,430,125</u>
Ending net assets	<u>\$ 239,818,042</u>

Statements of Cash Flows

The Statements of Cash Flows presents the amounts of cash provided or used by the District's operating, financing, and investing activities. Every cash flow has been categorized into one of the following activities: operating, non-capital financing, capital and related financing, or investing. The total of these categories for the year ended June 30, 2008, represents the decrease in cash and cash equivalents of \$8,502,006, which is combined with beginning cash and cash equivalents of \$16,940,203, to arrive at ending cash and cash

Beginning cash & cash equivalents	\$ 16,940,203
Decrease in cash & cash equivalents	<u>(8,502,006)</u>
Ending cash & cash equivalents	<u>\$ 8,438,197</u>

equivalents of \$8,438,197. Investments in the California Local Agency Investment Fund, San Diego County Investment Pool, open-ended money market mutual funds, and commercial paper and agency obligations maturities of 90 days or less are the only cash equivalents held by the District at June 30, 2008. As of June 30, 2008, the ending cash and cash equivalents are represented on the Statements of Net Assets as follows:

Unrestricted cash & cash equivalents	\$ 8,416,402
Cash & cash equivalents restricted - current	<u>21,795</u>
Total cash & cash equivalents	<u>\$ 8,438,197</u>

Vallecitos Water District
Management's Discussion and Analysis
For the Years Ended June 30, 2008 and 2007

ANALYSIS OF FINANCIAL POSITION AND RESULTS OF OPERATIONS

During the fiscal year ended June 30, 2008, the increase in total assets of \$333 thousand and the decrease in total liabilities of \$4.1 million resulted in an increase in net assets of \$4.4 million.

In 2008, \$18.5 million of the District's cash and investments were utilized to fund construction of capital projects. The District expended \$8.1 million in progress payments for the Encina Wastewater Authority (EWA) expansion, \$3.1 million for the 40 million-gallon Twin Oaks Reservoir, \$2.4 to the City of Carlsbad for road improvement projects, \$2.3 million for the Meadowlark Plant expansion, \$2.2 million for North Twin Oaks Reservoirs, \$1.7 million for EWA's administration building and other projects, and \$7.5 million for the construction and acquisition of other capital assets. These cash funded projects provide for needed capacity, replacement, and operating efficiencies that will result in long-term cost savings to the District. The following table summarizes how these capital projects and debt service were financed during the year.

Sources (in millions)		Uses (in millions)	
Decrease in cash and investment balances	\$18.5	Capital construction and acquisition	\$27.3
Operating activities	2.8	Debt service	3.0
Property taxes	2.8		
Capital facility fees	2.6		
Investment earnings	1.8		
Premium on converted debt	1.5		
Annexation fees and other receipts	0.3		
	<u>\$30.3</u>		<u>\$30.3</u>

The operating loss of \$2,945,760 includes the non-cash depreciation expense of \$5,933,135. Depreciation is the systematic allocation of a capital asset's cost to expense over a specified period of time. Depreciation on contributed assets, for which the District never realized cash outflows, is also included in the \$5.9 million of depreciation. Accounting pronouncements do not recognize that operating losses of growth agencies created by depreciation on contributed assets have no negative impact on financial performance. The District has established reserve floors for the replacement of aging infrastructure.

On July 12, 2007, the remaining \$63.8 million in Certificates of Participation were converted from variable auction rate (3.5% at the time of conversion) to a 4.736% all-inclusive fixed-rate debt to reduce interest rate risk as investment balances declined past the point of maintaining a hedge from interest on short term investments. This proved to be a prudent decision given auction-rate debt accelerated to as much as 20% in months following the conversion. Debt service on the fixed rate converted debt will amount to about \$4.4 million each year until maturity in 2035.

CURRENT-TO-PRIOR YEAR ANALYSIS

Analysis of Net Assets

As noted in the table on the following page, cash and investments have decreased by \$19.9 million from the prior fiscal year. This decrease differs from the decrease in cash and investment noted above because of non-cash mark-to-market adjustments included in the value of investments per accounting pronouncements. This spend-down provided for the \$18.2 million increase in capital assets (see discussion above under "Analysis of Financial Position and Results of Operations"). Net assets increased by \$4.4 million from the prior year.

Vallecitos Water District
Management's Discussion and Analysis
For the Years Ended June 30, 2008 and 2007

CURRENT-TO-PRIOR YEAR ANALYSIS (Continued)

Analysis of Net Assets (continued)

Vallecitos Water District's Net Assets				
	2008	2007	Change	
			Amount	%
Cash and investments	\$ 21,768,530	\$ 41,638,522	\$ (19,869,992)	-47.7%
Capital assets	286,296,154	268,073,883	18,222,271	6.8%
Other assets	10,534,223	8,553,461	1,980,762	23.2%
Total Assets	<u>318,598,907</u>	<u>318,265,866</u>	<u>333,041</u>	0.1%
Current liabilities	14,114,919	18,943,375	(4,828,456)	-25.5%
Noncurrent liabilities	64,665,946	63,892,366	773,580	1.2%
Total Liabilities	<u>78,780,865</u>	<u>82,835,741</u>	<u>(4,054,876)</u>	-4.9%
Net Assets				
Invested in capital assets, net of related debt	222,133,895	202,307,708	19,826,187	9.8%
Restricted	1,535,963	19,748,742	(18,212,779)	-92.2%
Unrestricted	16,148,184	13,373,675	2,774,509	20.7%
Total Net Assets	<u>\$ 239,818,042</u>	<u>\$ 235,430,125</u>	<u>\$ 4,387,917</u>	1.9%

Vallecitos Water District Selected Financial Ratios		
	2008	2007
Current ratio	2.05	1.46
Quick ratio	1.97	1.41
Capital assets-to-Long-term liabilities	4.43 / 1	4.20 / 1
Debt-to-equity	1 / 3.04	1 / 2.84

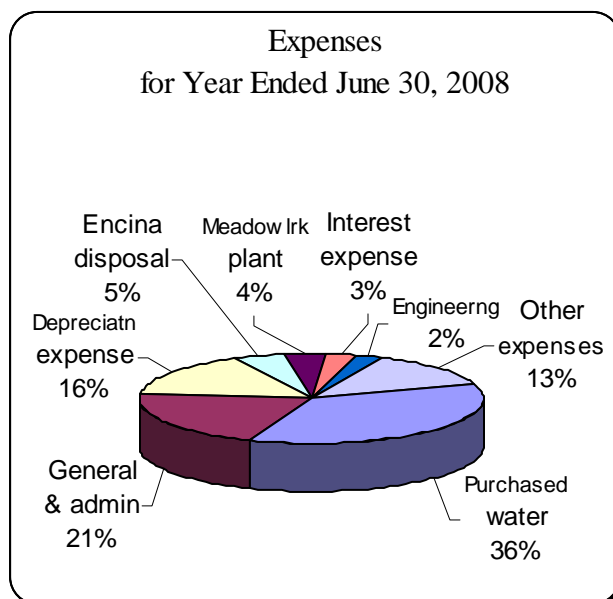
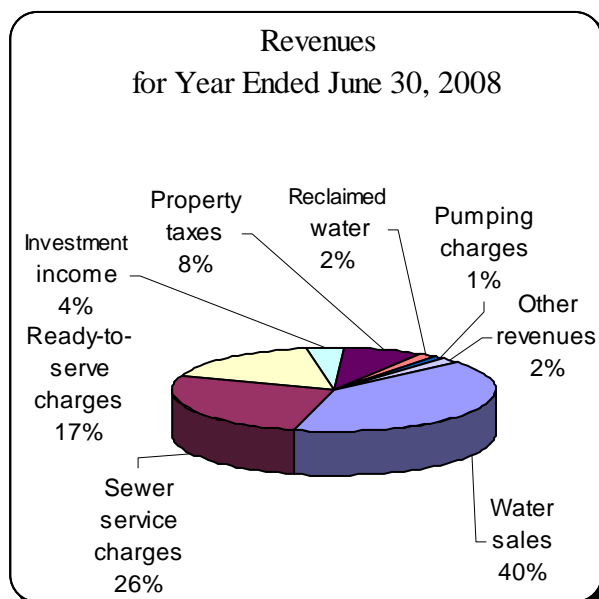
The table at the left illustrates how effectively the District can meet its current obligations and the margin of safety to creditors. The current ratio (current assets divided by current liabilities) indicates that the District can pay 2.05 times its current debt from current assets. However, some current assets are not as easily, or may never be, converted to cash (e.g. inventories and prepaid insurance). The quick

ratio, quick assets (cash, liquid investments, accounts receivable) divided by current liabilities, measures how effectively the District can meet current obligations with assets that are readily convertible to cash. The District can pay 1.97 times its current obligations with assets readily convertible to cash. The District's increased current and quick ratios indicate a high degree of solvency and a strong current position. The capital-assets-to-long-term-liabilities ratio indicates that for every dollar of debt the District has \$4.43 in capital assets (infrastructure, land, building, vehicles, equipment, furniture, etc.). The increases to this ratio and the debt-to-equity ratio indicate the District's ability to cash fund some degree of capital projects. The debt-to-equity ratio indicates that for every dollar of debt the District has \$3.04 of net assets (equity).

Vallecitos Water District
Management's Discussion and Analysis
For the Years Ended June 30, 2008 and 2007

CURRENT-TO-PRIOR YEAR ANALYSIS (Continued)

Analysis of Revenues and Expenses



A comparative analysis of revenues and expenses is presented below. Significant and unanticipated variances from the prior year are discussed on the following page.

Vallecitos Water District's Revenues and Expenses				
	For Fiscal Year:		Change	
	2008	2007	Amount	%
Water sales	\$ 15,310,847	\$ 14,945,265	\$ 365,582	2.4%
Wastewater service charges	10,090,243	8,845,156	1,245,087	14.1%
Ready-to-serve charges	6,405,368	5,808,110	597,258	10.3%
Property taxes	2,984,878	2,511,616	473,262	18.8%
Investment income	1,470,087	3,134,320	(1,664,233)	-53.1%
Other revenues	1,902,409	1,694,511	207,898	12.3%
Total Revenues	38,163,832	36,938,978	1,224,854	3.3%
Purchased water	13,917,279	13,626,626	290,653	2.1%
General and administrative	8,045,234	7,674,817	370,417	4.8%
Depreciation expense	5,933,135	5,528,101	405,034	7.3%
Encina disposal	1,876,099	2,966,331	(1,090,232)	-36.8%
Meadowlark plant	1,535,912	1,528,436	7,476	0.5%
Interest expense	1,073,597	1,769,483	(695,886)	-39.3%
Engineering	907,457	735,694	171,763	23.3%
Other expenses	4,196,395	3,965,735	230,660	5.8%
Total Expenses	37,485,108	37,795,223	(310,115)	-0.8%
Income / (Loss) before contributions	678,724	(856,245)	1,534,969	na
Capital contributions	3,709,193	8,547,531	(4,838,338)	-56.6%
Change in Net Assets	4,387,917	7,691,286	(3,303,369)	-42.9%
Beginning Net Assets	235,430,125	227,738,839	7,691,286	3.4%
Ending Net Assets	\$ 239,818,042	\$ 235,430,125	4,387,917	1.9%

Vallecitos Water District
Management's Discussion and Analysis
For the Years Ended June 30, 2008 and 2007

CURRENT-TO-PRIOR YEAR ANALYSIS (Continued)

Analysis of Revenues and Expenses (continued)

The composition of revenues and expenses for the 2007/08 fiscal year is graphically illustrated on the preceding page. Water sales, ready-to-serve charges, and wastewater service charges continue to be the main sources of revenue funding District operations. Water sales are commodity charges assessed to cover the variable costs of purchasing and delivering water to customers. Ready-to-serve charges are intended to cover fixed costs in the wholesale water rate, and costs related to being able to provide water to customers.

- Water sales and purchased water volume decreased from the previous year (by 4.2% and 5.8%, respectively) due to the efforts of Agricultural customers to comply with the 30% mandatory cut-back called for in the 2008 calendar year. However, increased rates caused increases in sales revenues and water costs of 2.4% and 2.1%, respectively.
- The \$1.2 million increase in wastewater service charges was anticipated due to an increase in customers and rates (6% effective in July of 2007), and changing commercial customers from a fixed count-based formula (based on employees, seats, etc.) to more equitable flow based charges.
- Ready-to-serve revenue increased \$597,258, or 10.3%, due to growth and a 7.2% rate increase effective in July of 2007.
- Increased property values and growth attributed to an 18.8% increase in property taxes.
- Encina disposal costs include the increase or decrease in book value of the District's investment in EWA. Prior year costs reflect a decrease in the book value on the District's investment in EWA of \$943,954. The book value of the investment in EWA is EWA's net assets times the District's ownership percentage. The current year Encina disposal costs have been reduced for an increase in book value the investment in EWA of \$226,013.
- The interest expense decrease was due to more interest being capitalized (recorded to assets in construction) during the 2007/08 fiscal year as compared to interest being capitalized in the 2006/07 fiscal year.
- The 2007/08 decrease in capital contributions (capital facility fees and developer contributed assets and deposits) was caused by a continued slow-down in growth in the San Marcos area as discussed in the Financial Highlights.

RESTRICTIONS, COMMITMENTS, AND LIMITATIONS

2005 Certificates of Participation – 2007 Conversion

On July 12, 2007, the District converted its remaining \$63.8 million in certificates of participation from variable auction rate to fixed rate debt to reduce interest rate risk. At the time of conversion the auction rate was 3.5%. Within two months of the conversion most auction-rate issuances experienced increases to rates in the double digits. The total-all-in-cost is 4.736%. The \$1.6 million realized in the issue premium was expended toward the Meadowlark Treatment Plant expansion. The District paid debt service of \$3.0 million during the year. The net revenue requirement is 1.15 times debt service. The District's 2007/08 net revenue was 2.27 times debt service. The District is required to pay principal each July 1 from 2008 through 2035 when the COPs mature. Interest is payable semi-annually. The COPs are payable from net combined water and sewer revenue of the District.

Vallecitos Water District
Management's Discussion and Analysis
For the Years Ended June 30, 2008 and 2007

RESTRICTIONS, COMMITMENTS, AND LIMITATIONS (Continued)

Capital Facility Fees

The District collects capital facility fees from new development and increased demands from existing customers, maintains the collected fees in separate funds (one for water and one for wastewater), and uses the funds exclusively to provide capacity to serve new development and fund future construction of facilities identified in the District's Master Plan and budget. As of June 30, 2008, the balances of cash and investments held in the capacity funds were \$4,745,296 for water and a \$4,621,446 deficit balance for wastewater. (The District maintains separate funds for specific purposes. Funds are combined for financial statement presentation.)

Capital Projects

The following budgeted projects have been contracted for at least the design phase before the 2008 fiscal year end:

<u>Project Description</u>	<u>2008/09 Budget</u>	<u>Spent Through</u>	
		<u>June 30, 2008</u>	<u>Remaining</u>
Encina Wastewater Authority Phase V expansion	\$ 18,227,000	\$ 16,465,500	\$ 1,761,500
San Marcos interceptor sewer line	16,400,000	3,323,700	13,076,300
Meadowlark Tank #3	4,335,000	300,000	4,035,000
Mountain Belle pump station and pipeline	3,860,000	97,300	3,762,700
Discovery Street sewer	1,985,000	255,000	1,730,000

The budget amounts above indicate the amount anticipated for completion of the projects. For some of these projects, the District has only committed to the design phase through contractual obligations and the contract for construction has not yet been through the bidding process. Details are provided in the District's 2008/09 Budget on these and several other committed projects less than \$1 million in scope.

CAPITAL ASSETS AND LONG-TERM DEBT

The following represents the most significant net additions to capital assets which were largely the result of development:

Pump stations and pumping equipment	\$3,488,594
Sewer mains	2,926,888
Enterprise Resource Plan	2,291,156
Water service lines	1,396,593
Meters	1,376,795
Water transmission and distribution mains	720,555

At June 30, 2008, the \$63.8 million in re-issued COPs are the only long-term debt obligation of the District.

Vallecitos Water District
Management's Discussion and Analysis
For the Years Ended June 30, 2008 and 2007

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The District considered the following economic factors in establishing 2008/09 budget amounts and rates:

- Slowed but continued growth - the District anticipates adding 303 meters and seven additional employment positions in the 2009 fiscal year.
- A continued 30% mandatory cut-back for agricultural customers.
- The need for improved and expanded facilities.
- Increases to wholesale water rates.
- Increased requirements related to regulatory compliance.
- The need to stay technologically current.

As a result of these factors, the 2008/09 budget includes:

- Increased water sales and water purchases from growth and rate increases offset by decreased water demand per customer due to higher projected (average) rainfall and the agricultural cut-back.
- Increased wastewater service charges from an adopted 10% increase in rates effective July 1, 2008, to cover costs incurred to comply with increasing regulations.
- A 13.4% increase in salaries and benefits due to additional hires, cost of living adjustments, step increases, and anticipated increases in group insurance costs.
- \$47.3 million in budgeted capital expenditures, including \$36.2 million in expansion costs.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to give ratepayers, customers, investors, and creditors a general overview of the District's finances and to demonstrate the District's accountability for the money it receives and the stewardship of the facilities it maintains. If you have questions about this report or need additional information, contact the Vallecitos Water District's Finance Department, 201 Vallecitos de Oro, San Marcos, CA 92069, call (760) 744-0460, or visit our website at www.vwd.org.

Basic Financial Statements

Vallecitos Water District
Statements of Net Assets
June 30, 2008 and 2007

<i>Assets</i>	2008	2007
Current Assets:		
Cash and cash equivalents (note 2)	\$ 8,416,402	\$ 10,817,423
Restricted cash and cash equivalents (note 2)	21,795	1,522,954
Investments (note 2)	13,181,388	8,886,323
Accounts receivable:		
Water and wastewater sales and services, net (note 3)	4,238,347	4,059,358
Taxes and assessments	1,138,596	932,826
From other governmental entities	586,567	334,618
Other	239,184	130,755
Accrued interest receivable	177,132	276,891
Current portion of note receivable (note 6)	87,176	82,632
Inventories	529,503	555,525
Prepaid expenses	261,768	118,570
Total current assets	<u>28,877,858</u>	<u>27,717,875</u>
Non-current assets:		
Restricted cash and cash equivalents (note 2)	-	4,599,826
Restricted investments (note 2)	1,489,944	15,811,996
Restricted accrued interest receivable	8,997	157,030
Restricted capital facility fees receivable	36,990	34,062
Note receivable from City of San Marcos, net of current portion (note 6)	1,035,246	1,122,422
Debt issuance costs, net (note 7)	635,294	520,852
Deferred charges from debt retirement, net (note 8)	218,424	227,920
Investment in Encina Wastewater Authority capital assets (note 5)	33,621,939	24,180,604
Capital assets not being depreciated (note 4)	80,310,079	78,818,207
Net capital assets being depreciated (note 4)	172,364,136	165,075,072
Total non-current assets	<u>289,721,049</u>	<u>290,547,991</u>
Total assets	<u>318,598,907</u>	<u>318,265,866</u>
<i>Liabilities</i>		
Current liabilities:		
Accounts payable	8,277,118	11,625,792
Accounts payable from restricted assets	-	854,172
Accrued compensation	1,291,046	1,229,064
Construction & service deposits	1,720,861	3,711,395
Accrued interest payable from restricted assets	1,570,894	47,952
Current portion of long term debt (note 9)	1,255,000	1,475,000
Total current liabilities	<u>14,114,919</u>	<u>18,943,375</u>
Non-current liabilities:		
Deposit from San Marcos Unified School District	189,400	189,400
Other post employment benefits obligation, net (note 13)	715,565	351,575
Certificates of participation, net of amortized discount & current portion (note 9)	63,760,981	63,351,391
Total non-current liabilities	<u>64,665,946</u>	<u>63,892,366</u>
Total liabilities	<u>78,780,865</u>	<u>82,835,741</u>
<i>Net Assets</i>		
Invested in capital assets, net of related debt (note 10)	222,133,895	202,307,708
Restricted for future capital facilities	1,535,963	19,748,742
Unrestricted	16,148,184	13,373,675
Total Net Assets	<u>\$ 239,818,042</u>	<u>\$ 235,430,125</u>

See accompanying notes to the financial statements

Vallecitos Water District
Statements of Revenues, Expenses and Changes in Net Assets
For the Years Ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Operating revenues:		
Water sales	\$ 15,310,847	\$ 14,945,265
Wastewater service charges	10,090,243	8,845,156
Ready-to-serve charges	6,405,368	5,808,110
Reclaimed water sales	736,828	648,566
Pumping charges	414,050	524,043
Other services and abatements	494,483	375,579
Total operating revenues	<u>33,451,819</u>	<u>31,146,719</u>
Operating expenses:		
Purchased water	13,917,279	13,626,626
General and administrative	8,045,234	7,674,817
Encina disposal	1,876,099	2,966,331
Meadowlark wastewater treatment plant	1,535,912	1,528,436
Transmission and distribution	843,345	952,967
Engineering	907,457	735,694
Customer accounts	630,716	566,390
Pumping	475,798	456,767
Collection and conveyance	762,177	722,966
Buildings and grounds	432,557	401,096
Equipment and vehicles	312,816	297,076
Meter reading and repairs	145,972	157,125
Tanks and reservoirs	284,093	228,569
Water quality and treatment	167,816	185,836
Information technology	304,967	138,791
Other wastewater operating expenses	217,887	239,876
Other water operating expenses	327,548	262,862
Total operating expenses	<u>31,187,673</u>	<u>31,142,225</u>
Operating income before overhead absorption	2,264,146	4,494
Overhead absorption	723,225	680,658
Operating income before depreciation and amortization	2,987,371	685,152
Depreciation and amortization	<u>(5,933,135)</u>	<u>(5,528,101)</u>
Operating loss	<u>(2,945,764)</u>	<u>(4,842,949)</u>
Non-operating revenues (expenses):		
Property taxes	2,984,878	2,511,616
Investment income	1,470,087	3,134,320
Annexation fees	257,048	146,323
Interest expense	(1,073,597)	(1,769,483)
Other, net	(13,928)	(36,072)
Total non-operating revenues and expenses	<u>3,624,488</u>	<u>3,986,704</u>
Income (loss) before contributions	678,724	(856,245)
Capital contributions	<u>3,709,193</u>	<u>8,547,531</u>
Change in net assets	4,387,917	7,691,286
Net assets, beginning of year	<u>235,430,125</u>	<u>227,738,839</u>
Net assets, end of year	<u>\$ 239,818,042</u>	<u>\$ 235,430,125</u>

See accompanying notes to the financial statements

Vallecitos Water District
Statements of Cash Flows
For the Years Ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Cash flows from operating activities:		
Receipts from water and wastewater customers	\$ 32,912,452	\$ 31,164,598
Payments for water	(13,707,820)	(13,237,750)
Payments for services and supplies	(4,341,953)	(3,199,567)
Payments for employee wages, benefits and related costs	(12,059,817)	(11,515,619)
Net cash provided by operating activities	<u>2,802,862</u>	<u>3,211,662</u>
Cash Flows from non-capital financing activities:		
Receipts from taxes and assessments	<u>2,779,108</u>	<u>2,405,059</u>
Net cash provided by non-capital financing activities	<u>2,779,108</u>	<u>2,405,059</u>
Cash flows from capital and related financing activities:		
Receipts from annexation fees	257,048	146,323
Acquisition and construction of utility plant	(17,479,876)	(43,852,778)
Proceeds from certifications of participation	1,550,018	-
Principal paid on long term debt	(1,475,000)	(1,425,000)
Interest payments on long-term debt	(1,530,230)	(1,745,641)
Investment in Encina Wastewater Authority	(9,813,212)	(6,746,476)
Capacity fees received	<u>2,579,775</u>	<u>4,570,909</u>
Net cash used in capital and related financing activities	<u>(25,911,477)</u>	<u>(49,052,663)</u>
Cash flows from investing activities:		
Purchase of investments	(22,658,706)	(81,853,508)
Proceeds from sale, call and maturity of investments	32,576,646	100,078,224
Interest received	1,826,925	3,257,655
Collections on Note receivable from City of San Marcos	<u>82,636</u>	<u>78,322</u>
Net cash provided by investing activities	<u>11,827,501</u>	<u>21,560,693</u>
Net decrease in cash and cash equivalents	(8,502,006)	(21,875,249)
Cash and cash equivalents, beginning of year	<u>16,940,203</u>	<u>38,815,452</u>
Cash and cash equivalents, end of year	<u>\$ 8,438,197</u>	<u>\$ 16,940,203</u>
Reconciliation of cash and cash equivalents to statement of net assets:		
Cash and cash equivalents	\$ 8,416,402	\$ 10,817,423
Restricted cash and cash equivalents - current	21,795	1,522,954
Restricted cash and cash equivalents - non-current	<u>-</u>	<u>4,599,826</u>
Total cash and cash equivalents	<u>\$ 8,438,197</u>	<u>\$ 16,940,203</u>
Reconciliation of operating loss to net cash provided by operating activities:		
Net cash provided by operating activities:		
Operating loss	\$ (2,945,764)	\$ (4,842,949)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation & amortization expense	5,933,135	5,528,101
Changes in operating assets and liabilities:		
Accounts receivable from water and wastewater sales and services	(178,989)	(710,137)
Accounts receivable from other governmental entities	(251,949)	(304,817)
Accounts receivable - other	(108,429)	321,766
Inventories	26,022	(48,431)
Prepaid expenses	(143,198)	63,565
Investment in Encina Wastewater Authority	(226,013)	943,954
Accounts payable	272,075	1,093,713
Accrued compensation	61,982	104,255
Other post employment benefits obligation, net	363,990	351,575
Construction and service deposits	<u>-</u>	<u>711,067</u>
Net cash provided by operating activities	<u>\$ 2,802,862</u>	<u>\$ 3,211,662</u>
Non-cash investing capital and financing activities:		
Contributions of assets by developers	<u>\$ 758,080</u>	<u>\$ 3,661,706</u>
Amortization related to long-term debt	<u>\$ 32,186</u>	<u>\$ 14,396</u>
Unrealized appreciation (depreciation) of investments	<u>\$ 109,044</u>	<u>\$ 244,478</u>

See accompanying notes to the financial statements

Vallecitos Water District
Notes to the Basic Financial Statements
For the Years Ended June 30, 2008 and 2007

(1) Reporting Entity and Summary of Significant Accounting Policies

A. Organization and Operations of the Reporting Entity

The Vallecitos Water District was organized in March of 1955 under the provisions of the California Water Code. By Board action in 1989, the District's name changed from the San Marcos County Water District to the Vallecitos Water District. The District was organized to finance, construct, operate, and maintain a water and wastewater system serving portions of northern San Diego County. Currently, the District services approximately 29,000 acres and provides water and wastewater service to the City of San Marcos, portions of the cities of Escondido and Carlsbad, and portions of surrounding unincorporated areas.

The criteria used in determining the scope of the financial reporting entity is based on the provisions of Governmental Accounting Statements No. 14, *The Financial Reporting Entity*, and No. 39, *Determining Whether Certain Organizations Are Component Units* (an amendment of No. 14). The District is the primary governmental unit based on the foundation of a separately elected governing board that is elected by the citizens in a general popular election. Component units are legally separate organizations for which the elected officials of the primary government are financially accountable. The District is financially accountable if it appoints a voting majority of the organization's governing body and: 1) It is able to impose its will on that organization, or 2) There is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary government.

The Vallecitos Water District Financing Corporation (Corporation) was incorporated in March 1998. The Corporation is a California nonprofit public benefit corporation formed to assist the District by acquiring, constructing, operating and maintaining facilities, equipment, or other property needed by the District and leasing or selling such property to the District and as such has no employees or other operations. Although the Corporation is legally separate, it is included as a blended component unit of the District, as it is in substance part of the District's operations. No separate financial statements are prepared for the Corporation.

B. Basis of Accounting and Measurement Focus

The District reports its activities as an enterprise fund and accounts for operations that are financed and operated in a manner similar to a private business enterprise. The intent of the District is to provide water, wastewater and recycled water services to its customers on a continuing basis and finance or recover costs of providing services primarily through user charges (water and wastewater sales and services). Revenues and expenses are recognized on the full accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred, regardless of when the related cash flows take place.

Operating revenues and expenses, such as water sales and water purchases, result from exchange transactions associated with the principal activity of the District. Exchange transactions are those in which each party receives and gives up essentially equal values. Management, administration and depreciation expenses are also considered operating expenses. Other revenues and expenses not included in the above categories are reported as non-operating revenues and expenses.

C. Financial Reporting

The District's basic financial statements are presented in conformance with the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* (GASB No. 34). This statement established revised financial reporting requirements for state and local governments throughout the United States for the purpose of enhancing the understandability and usefulness of financial reports.

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(1) Reporting Entity and Summary of Significant Accounting Policies, continued

C. Financial Reporting, continued

GASB No. 34 and its related GASB pronouncements provide for a revised view of financial information and restructure the format of financial information provided prior to its adoption. A statement of net assets replaces the balance sheet and reports assets, liabilities, and the difference between them as net assets, not equity. A statement of revenues, expenses and changes in net assets replaces both the income statement and the statement of changes in retained earnings and contributed capital. GASB No. 34 also requires that the statement of cash flows be prepared using the direct method. Under the direct method, cash flows from operating activities are presented by major categories.

Under GASB No. 20, enterprise funds, such as the District, have the option of consistently following or not following pronouncements issued by the Financial Accounting Standards Board (FASB) subsequent to November 30, 1989. The District has elected not to follow FASB standards issued after that date, unless such standards are specifically adopted by GASB.

D. Implementation of New Governmental Accounting Standards Board Statements

Governmental Accounting Standards Board Statement No. 45

In June 2004, the GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions*. This Statement establishes standards for the measurement, recognition, and display of OPEB expense/expenditures and related liabilities (assets), note disclosures, and, if applicable, required supplementary information (RSI) in the financial reports of state and local government employers. The District elected to adopt this statement for fiscal year 2007 and has accordingly recorded a liability and the related expense for post-employment benefits other than pensions, for the past two fiscal years.

E. Assets, Liabilities, and Net Assets

1. Use of Estimates

The preparation of the basic financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported changes in net assets during the reporting period. Actual results could differ from those estimates.

2. Cash and Cash Equivalents

Substantially all of the District's cash is invested in interest bearing accounts. The District considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

3. Investments and Investment Policy

The District has adopted an investment policy directing the Treasurer to deposit funds in financial institutions.

Changes in fair value that occur during a fiscal year are recognized as investment income reported for that fiscal year. Investment income includes interest earnings, changes in fair value, and any gains or losses realized upon the liquidation or sale of investments.

4. Accounts Receivable and Allowance for Uncollectible Accounts

The District extends credit to customers in the normal course of operations. When management deems customer accounts uncollectible, the District uses the allowance method for the reservation and write-off of those accounts.

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(1) Reporting Entity and Summary of Significant Accounting Policies, continued

E. Assets, Liabilities, and Net Assets, continued

5. Federal and State Capital and Operating Grants

If a grant agreement were approved and eligible expenditures were incurred, the amount is recorded as a capital or operating grant receivable on the statement of net assets and as capital grant contribution or operating grant revenue, as appropriate, on the statement of revenues, expenses and changes in net assets.

6. Property Taxes and Assessments

Property taxes and assessments are billed by the County of San Diego to property owners. The District's property tax calendar is as follows:

Lien date	January 1
Levy date	July 1
Due date	
First installment	November 1
Second installment	February 1
Delinquent date	
First installment	December 10
Second installment	April 10

Taxes and assessments receivable of \$1,138,596 and \$932,826 have been reduced by an allowance for estimated uncollectible taxes of \$17,485 and \$14,167 at June 30, 2008 and 2007, respectively.

7. Water-In-Storage Inventory

The District owns the water within its transmission and distribution system. This water has been recorded on the District's books at the cost at which the water was purchased using the FIFO method.

8. Materials and Supplies Inventory

Materials and supplies inventory consists primarily of water meters, pipe and pipefittings for construction and repair to the District's water transmission and distribution system and wastewater system. Inventory is valued at cost using a weighted average cost method. Inventory items are charged to expense or work-in-process at the time that individual items are withdrawn from inventory or consumed.

9. Prepaid Expenses

Certain payments to vendors reflects costs or deposits applicable to future accounting periods and are recorded as prepaid items in the basic financial statements.

10. Restricted Assets

Certain assets of the District are restricted in use by law or debt covenant and, accordingly are shown as restricted assets on the accompanying statement of net assets. Certificates of Participation construction funds set aside from Certificates of Participation proceeds are restricted for construction projects. The District uses restricted resources, prior to using unrestricted resources, to pay expenditures meeting the criteria imposed on the use of restricted resources by a third party.

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(1) Reporting Entity and Summary of Significant Accounting Policies, continued

E. Assets, Liabilities, and Net Assets, continued

11. Capital Assets

Capital assets acquired and/or constructed are capitalized at historical cost. District policy has set the capitalization threshold for reporting capital assets at \$5,000. Donated assets are recorded at estimated fair market value at the date of donation. Upon retirement or other disposition of capital assets, the cost and related accumulated depreciation are removed from the respective balances and any gains or losses are recognized. Depreciation is recorded on a straight-line basis over the estimated useful lives of the assets as follows:

Transmission and distribution system	10 - 75 years
Wastewater system	5 - 50 years
Buildings	50 years
Transportation equipment	8 - 15 years
Field and shop equipment	5 - 20 years
Office equipment	5 - 10 years

12. Encina Wastewater Authority

The District's participation in the Encina Wastewater Authority (EWA) is included in the accompanying financial statements. The District's investment in EWA is capitalized as a percentage of ownership of current year capital expenditures incurred by EWA. Ownership percentages are determined by joint agreements at the time the assets are acquired.

13. Deferred Charges

Deferred charges from bond issuance costs are amortized using the straight-line method over the remaining life of the respective debt service.

14. Compensated Absences

The District's personnel policies provide for accumulation of vacation and sick leave. Liabilities for vacation and sick leave are recorded when benefits are earned. Cash payment equal to 100% of unused vacation and 25% or 50% of sick leave, depending on length of service, is available upon retirement or termination.

15. Construction Advances and Deposits

Construction advances represent deposits received in aid of construction, which are refundable if the applicable construction does not take place. Construction advances are transferred to contributed capital when the applicable construction project is completed.

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(1) Reporting Entity and Summary of Significant Accounting Policies, continued

E. Assets, Liabilities, and Net Assets, continued

16. Net Assets

The financial statements utilize a net assets presentation. Net assets are categorized as follows:

- **Net Investment in Capital Assets** – This component of net assets consists of capital assets, net of accumulated depreciation and reduced by any debt outstanding against the acquisition, construction or improvement of those assets.
- **Restricted Net Assets** – This component of net assets consists of constraints placed on net assets use through external constraints imposed by creditors, grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.
- **Unrestricted Net Assets** – This component of net assets consists of net assets that do not meet the definition of *restricted* or *net investment in capital assets*.

F. Water and Wastewater Sales and Services

Water and wastewater sales and services are billed on a monthly cyclical basis. Estimated unbilled water revenue through June 30 has been accrued at year-end.

G. Capital Contributions

Capital contributions represent cash and capital asset additions contributed to the District by property owners, granting agencies or real estate developers desiring services that require capital expenditures or capacity commitment.

H. Economic Dependency

The District purchases all of its water from the San Diego County Water Authority. A sustained interruption of this source could impact the District negatively.

I. Budgetary Policies

The District adopts an annual budget for planning, control, and evaluation purposes. Budgetary control and evaluation are affected by comparisons of actual revenues and expenses with planned revenues and expenses for the period. Encumbrance accounting is not used to account for commitments related to unperformed contracts for construction and services.

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(2) Cash and Investments

Cash and investments as of June 30, are classified in the accompanying financial statements as follows:

	<u>2008</u>	<u>2007</u>
Cash and cash equivalents	\$ 8,416,402	10,817,423
Restricted cash and cash equivalents – current portion	21,795	1,522,954
Investments – current portion	13,181,388	8,886,323
Restricted cash and cash equivalents – noncurrent portion	-	4,599,826
Restricted investments	<u>1,489,944</u>	<u>15,811,996</u>
Total cash and investments	<u>\$ 23,109,529</u>	<u>41,638,522</u>

Cash and investments as of June 30, consist of the following:

	<u>2008</u>	<u>2007</u>
Cash on hand	\$ 1,700	1,700
Deposits with financial institutions	267,518	102,307
Investments	<u>22,840,311</u>	<u>41,534,515</u>
Total cash and investments	<u>\$ 23,109,529</u>	<u>41,638,522</u>

Investments Authorized by the California Government Code and the District's Investment Policy

The table below identifies the investment types that are authorized by the District in accordance with the District's investment policy, which is more restrictive than the California Government Code. The table also identifies certain provisions of the District's investment policy that address interest rate risk, credit risk, and concentration of credit risk. This table does not address investments of debt proceeds that are governed by the provisions of debt agreements of the District, rather than the general provisions of the District's investment policy.

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Maximum Percentage Of Portfolio</u>	<u>Maximum Investment in One Issuer/Institution</u>
U.S. Treasury Obligations	5 years	75%	None
U.S. Agency Securities	5 years	60%	25%
Commercial Paper	270 days	20%	10%
Certificates of Deposit	4 years	20%	5%
Repurchase Agreements	1 year	10%	10%
San Diego County Pooled Investment Funds	N/A	20%	20%
Local Agency Investment Fund (LAIF)	N/A	60%	None
Savings Accounts	N/A	10%	10%

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(2) Cash and Investments, continued

Investments Authorized by Debt Agreements

Investment of debt proceeds are governed by provisions of the debt agreements, rather than the general provisions of the California Government Code or the District's investment policy. Appendix B of the official statements note the investment types that are authorized for investments and identifies certain provisions of these debt agreements that address interest rate risk, credit risk and concentration of credit risk. The District maintains and invests the 2005 Certificates of Participation debt proceeds in accordance with debt covenants.

Custodial Credit Risk

Custodial credit risk for *deposits* is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for *investments* is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. With respect to investments, custodial credit risk generally applies only to direct investments in marketable securities. Custodial credit risk does not apply to a local government's indirect investment in securities through the use of mutual funds or government investment pools (such as LAIF).

The District's investment policy considers aversion to custodial credit risk by requiring all participants in the investment process to invest no more than 25% of the portfolio with one financial institution, with the exception of LAIF, the U.S. Treasury and funds advanced or in trustee accounts for project construction. The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure District deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits. The District had deposits with bank balances of \$401,132 and \$346,203 as of June 30, 2008 and 2007, respectively. Of the bank balances, up to \$100,000 is federally insured and the remaining balance is collateralized in accordance with the Code; however, the collateralized securities are not held in the District's name.

Investment in State Investment Pool

The District is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by the California Government Code under the oversight of the Treasurer of the State of California. The fair value of the District's investment in this pool is reported in the accompanying financial statements at amounts based upon the District's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis.

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(2) Cash and Investments, continued

San Diego County Pooled Investment Fund

The San Diego County Pooled Investment Fund (SDCPIF) is a pooled investment fund program governed by the County of San Diego Board of Supervisors, and administered by the County of San Diego Treasurer and Tax Collector. Investments in SDCPIF are highly liquid as deposits and withdrawals can be made at anytime without penalty. SDCPIF does not impose a maximum investment limit; however, the District's investment policy limits investment in SDCPIF to 20% of the District's total portfolio.

The County of San Diego's bank deposits are either Federally insured or collateralized in accordance with the California Government Code. Pool detail is included in the County of San Diego Comprehensive Annual Financial Report (CAFR). Copies of the CAFR may be obtained from the County of San Diego Auditor-Controller's Office – 1600 Pacific Coast Highway – San Diego, CA 92101.

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The District manages interest rate risk by limiting terms of investment as noted in the Authorized Investment Type on page 18. The District also manages its exposure to interest rate risk by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio matures or comes close to maturity evenly over time as necessary to provide requirements for cash flow and liquidity needed for operations. Information about the sensitivity of the fair values of the District's investments to market interest rate fluctuations is provided by the following table that shows the distribution of the District's investments by maturity date:

Maturities of investments at June 30, 2008, are as follows:

<u>Investment Type</u>	<u>Total</u>	<u>Remaning Maturity (in Months)</u>		
		<u>12 Months Or Less</u>	<u>13 to 24 Months</u>	<u>25-60 Months</u>
U.S. Treasury bills	\$ 994,425	994,425	-	-
Federal Home Loan Bank	3,058,600	1,020,315	2,038,285	-
Federal Home Loan Mortgage Corporation	1,508,400	-	1,508,400	-
Federal National Mortgage Association	3,032,040	2,023,910	1,008,130	-
Certificates of Deposit	299,950	299,950	-	-
Commercial paper	2,951,995	2,951,995	-	-
Local Agency Investment Fund (LAIF)	6,619,337	6,619,337	-	-
San Diego County Investment Pool	1,549,639	1,549,639	-	-
Held by bond trustee:				
Money market funds	2,825,925	2,825,925	-	-
Total	\$ 22,840,311	18,285,496	4,554,815	-

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(2) Cash and Investments, continued

Maturities of investments at June 30, 2007, are as follows:

Investment Type	Total	Remaning Maturity (in Months)		
		12 Months Or Less	13 to 24 Months	25-60 Months
U.S. Treasury bills	\$ 3,963,550	3,963,550	-	-
Federal Home Loan Bank	7,912,933	7,912,933	-	-
Federal Farm Credit Bank	991,250	991,250	-	-
Federal Home Loan Mortgage Corporation	3,982,890	3,982,890	-	-
Federal National Mortgage Association	2,980,840	1,995,530	985,310	-
Federal Agricultural Mortgage Corporation	830,100	830,100	-	-
Certificates of Deposit	98,907	98,907	-	-
Commercial paper	4,935,800	4,935,800	-	-
Local Agency Investment Fund (LAIF)	12,847,748	12,847,748	-	-
San Diego County Investment Pool	1,467,545	1,467,545	-	-
Held by bond trustee:				
Money market funds	1,522,952	1,522,952	-	-
Total	\$ 41,534,515	40,549,205	985,310	-

Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the minimum rating required by (where applicable) the California Government Code, the District's investment policy, or debt agreements, and the actual rating as of year end for each investment type.

Credit ratings of investments as of June 30, 2008 were as follows:

Investment Types	Total	Minimum Legal Rating	Exempt From Disclosure	Rated as of Year End		
				AAA	AA+	Not Rated
U.S. Treasury bills	\$ 994,425	N/A	994,425	-	-	-
Federal Home Loan Bank	3,058,600	AA+	-	3,058,600	-	-
Federal Home Loan Mortgage Corporation	1,508,400	AA+	-	1,508,400	-	-
Federal National Mortgage Association	3,032,040	AA+	-	3,032,040	-	-
Certificates of Deposit	299,950	N/A	-	299,950	-	-
Commercial paper	2,951,995	AA+	-	-	2,951,995	-
Local Agency Investment Fund (LAIF)	6,619,337	N/A	-	-	-	6,619,337
San Diego County Investment Pool	1,549,639	N/A	-	1,549,639	-	-
Held by bond trustee:						
Money market funds	2,825,925	N/A	2,825,925	-	-	-
Total	\$ 22,840,311		3,820,350	9,448,629	2,951,995	6,619,337

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(2) Cash and Investments, continued

Credit ratings of investments as of June 30, 2007 were as follows:

Investment Types	Total	Minimum Legal Rating	Exempt From Disclosure	Rated as of Year End		
				AAA	AA+	Not Rated
U.S. Treasury bills	\$ 3,963,550	N/A	3,963,550	-	-	-
Federal Home Loan Bank	7,912,933	AA+	-	7,912,933	-	-
Federal Farm Credit Bank	991,250	AA+	-	991,250	-	-
Federal Home Loan Mortgage Corporation	3,982,890	AA+	-	3,982,890	-	-
Federal National Mortgage Association	2,980,840	AA+	-	2,980,840	-	-
Federal Agricultural Mortgage Corporation	830,100	AA+	-	830,100	-	-
Certificates of Deposit	98,907	N/A	-	98,907	-	-
Commercial paper	4,935,800	AA+	-	-	4,935,800	-
Local Agency Investment Fund (LAIF)	12,847,748	N/A	-	-	-	12,847,748
San Diego County Investment Pool	1,467,545	N/A	-	1,467,545	-	-
Held by bond trustee:						
Money market funds	1,522,952	N/A	1,522,952	-	-	-
	<u>\$ 41,534,515</u>		<u>5,486,502</u>	<u>18,264,465</u>	<u>4,935,800</u>	<u>12,847,748</u>

Concentration of Credit Risk

The investment policy of the District limits the amount that can be invested in any one issuer to 25% of the portfolio, other than U.S. Treasury securities. Investments in any one issuer, other than U.S. Treasury securities, that represent 5% or more of the total District investments are as follows:

Issuer	2008		2007	
	Reported Amount	Portfolio Percentage	Reported Amount	Portfolio Percentage
Federal Home Loan Bank	\$ 3,058,600	13%	7,912,933	19%
Federal Home Loan Mortgage Corp	1,508,400	7%	3,982,890	10%
Federal National Mortgage Association	3,032,040	13%	2,980,840	7%
Commercial Paper - GE	2,951,995	13%	2,930,008	7%

(3) Accounts Receivable – Water and Wastewater Sales and Services, Net

The balance at June 30, consists of the following:

	2008	2007
Accounts receivable – water and wastewater sales and services	\$ 4,261,607	4,074,118
Allowance for uncollectible accounts	(23,260)	(14,760)
Accounts receivable – water sales, net	<u>\$ 4,238,347</u>	<u>4,059,358</u>

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(4) Capital Assets

Changes in capital assets for the 2008 were as follows:

	<u>Balance 2007</u>	<u>Additions/ Transfers</u>	<u>Deletions/ Transfers</u>	<u>Balance 2008</u>
Non-depreciable assets:				
Land	\$ 4,674,034	70,474	-	4,744,508
Construction-in-process	<u>74,144,173</u>	<u>17,800,593</u>	<u>(16,379,195)</u>	<u>75,565,571</u>
Total non-depreciable assets	<u>78,818,207</u>	<u>17,871,067</u>	<u>(16,379,195)</u>	<u>80,310,079</u>
Depreciable assets:				
Water transmission and distribution system	136,404,221	7,275,009	(74,508)	143,604,722
Wastewater system	66,185,578	3,095,827	-	69,281,405
Buildings	14,898,399	-	-	14,898,399
Transportation equipment	2,645,268	67,524	-	2,712,792
Field and shop equipment	7,121,336	2,783,770	-	9,905,106
Office equipment	<u>1,116,742</u>	<u>86,031</u>	<u>(49,438)</u>	<u>1,153,335</u>
Total depreciable assets	<u>228,371,544</u>	<u>13,308,161</u>	<u>(123,946)</u>	<u>241,555,759</u>
Accumulated depreciation and amortization:				
Water transmission and distribution system	(31,065,669)	(3,076,438)	-	(34,142,107)
Wastewater system	(21,753,675)	(1,604,362)	-	(23,358,037)
Buildings	(2,799,589)	(328,659)	-	(3,128,248)
Transportation equipment	(1,453,907)	(263,890)	-	(1,717,797)
Field and shop equipment	(5,356,501)	(596,657)	-	(5,953,158)
Office equipment	<u>(867,131)</u>	<u>(25,145)</u>	<u>-</u>	<u>(892,276)</u>
Total accum depr. and amort.	<u>(63,296,472)</u>	<u>(5,895,151)</u>	<u>-</u>	<u>(69,191,623)</u>
Total depreciable assets, net	<u>165,075,072</u>	<u>7,413,010</u>	<u>(123,946)</u>	<u>172,364,136</u>
Total capital assets, net	<u>\$ 243,893,279</u>	<u>25,284,077</u>	<u>(16,503,141)</u>	<u>252,674,215</u>

In 2008, major capital assets additions during the year include the Phase V expansion at Encina Wastewater Authority, North Twin Oaks Reservoir #2, City of Carlsbad road improvement projects, sewer mains, Meadowlark Treatment Plant Expansion, Enterprise Resource Planning System and North Twin Oaks reservoirs. A significant portion of the District's transmission and distribution systems mains and pipelines rehabilitation were constructed by the District and transferred out of construction-in-process upon completion of these various projects.

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(4) Capital Assets, continued

Changes in capital assets for the 2007 were as follows:

	Restated Balance 2006	Additions/ Transfers	Deletions/ Transfers	Balance 2007
Non-depreciable assets:				
Land	\$ 4,674,034	-	-	4,674,034
Construction-in-process	43,433,213	44,391,237	(13,680,277)	74,144,173
Total non-depreciable assets	48,107,247	44,391,237	(13,680,277)	78,818,207
Depreciable assets:				
Water transmission and distribution system	127,281,119	9,803,998	(680,896)	136,404,221
Wastewater system	61,118,901	5,066,677	-	66,185,578
Buildings	13,832,579	1,065,820	-	14,898,399
Transportation equipment	2,424,994	220,274	-	2,645,268
Field and shop equipment	6,873,934	258,204	(10,802)	7,121,336
Office equipment	1,042,592	74,150	-	1,116,742
Total depreciable assets	212,574,119	16,489,123	(691,698)	228,371,544
Accumulated depreciation and amortization:				
Water transmission and distribution system	(28,232,378)	(2,833,291)	-	(31,065,669)
Wastewater system	(20,207,436)	(1,546,239)	-	(21,753,675)
Buildings	(2,470,930)	(328,659)	-	(2,799,589)
Transportation equipment	(1,190,858)	(263,049)	-	(1,453,907)
Field and shop equipment	(4,925,309)	(431,192)	-	(5,356,501)
Office equipment	(741,460)	(125,671)	-	(867,131)
Total accum depr. and amort.	(57,768,371)	(5,528,101)	-	(63,296,472)
Total depreciable assets, net	154,805,748	10,961,022	(691,698)	165,075,072
Total capital assets, net	\$ 202,912,995	55,352,259	(14,371,975)	243,893,279

In 2007, major capital assets additions during the year include the North Twin Oaks Reservoir #2 and the Meadowlark Treatment Plant Expansion along with rehabilitation of the District's transmission and distribution systems mains and pipelines. A significant portion of the District's transmission and distribution systems mains and pipelines rehabilitation were constructed by the District and transferred out of construction-in-process upon completion of these various projects

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(4) Capital Assets, continued

Construction-In-Process

The District has been involved in various construction projects throughout the year. The balances of the various construction projects that comprise the construction-in-process balances at June 30 are as follows:

<u>Project Name</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>
District Financed:			
Meadowlark Plant Expansion	\$ 13,105,775	28,551,828	32,248,741
Twin Oaks Reservoir	868,874	14,580,065	17,462,404
North Twin Oaks reservoir 2 & 3 San Marcos Mtn / Merriam Mtn	262,978	3,087,902	5,642,223
Twin Oaks reservoir number 2	2,086,649	3,455,664	3,472,808
SM interceptor - SM Blvd/Discovery	3,232,001	3,317,754	3,323,653
40 mg Twin Oaks Reservoir	12,453	42,577	2,145,587
Automated meter reading conversion	1,168,433	1,944,232	1,876,596
Lift Station #3	220,570	1,854,380	1,854,406
Wulff Reservoir	51,133	959,936	1,026,298
Finance & Customer Information Systems	-	303,323	733,626
San Elijo Road Facilities	-	641,204	641,279
Vactor	-	-	326,167
Meadowlark Tank #3	196,519	244,671	300,043
Discovery St Sewer Replacement	76,255	121,592	254,986
ERP Phase II	-	-	151,064
MXU Installations	-	58,718	125,712
Meadowlark Tank Refurbishment	37,889	79,546	106,880
Facility/Maintenance data management system	1,602,679	2,236,337	105,044
Land outfall replacement 24" & 54" Laurels to Carillo Ranch	775,855	2,596,117	-
Wulff Pump Station - Upgrade	262,978	1,897,260	-
North Twin Oaks pump station upgrade	1,112,420	1,588,819	-
Miscellaneous road improvements	280,847	280,847	-
Meadowlark Plant expansion design	3,270,011	-	-
Sewer main replacement- Linda Vista/Pacific	2,520,785	-	-
Sewer flow monitoring stations	1,600,260	-	-
Deer Springs pump station replacement	1,569,387	-	-
Radio read meters	900,669	-	-
Solar carport covers	829,156	-	-
Los Posas Rd. Improvements	570,642	-	-
Water wastewater reclamation FY 2000-2001 master plan update	335,650	-	-
Emergency replacement 24" RPM	295,795	-	-
Rancho Santa Fe Rd Phase 1	254,973	-	-
Subtotal - District Financed	\$ 37,501,636	67,842,772	71,797,517
Developer Financed:			
Rancho Santalina plan	\$ 31,114	43,704	577,340
Oceanside-Escondido rail project-railroad right of way & CSUSM loop	310,216	323,472	352,625
San Elijo PH 3 & 5 Onsite	27,306	92,976	145,912
San Elijo Hills 1530 Zone Reservoir	132,637	145,020	145,265
Merriam Mtn / Stonegate WS Study	39,194	105,038	114,290
Altmann Subdivision	16,332	106,127	106,127
La Costa Ridge 2.3 / 2.5 & Street Improvements	-	425,252	-
Las Posas widening - Las Posas drainage Grand to Mission	213,633	221,781	-
Univ. Commons, San Elijo Hills Rd. improvement water/sewer plan check	1,198,823	-	-
University Commons TSM 421, Unit 1 water/sewer plan check	304,005	-	-
Rancho Coronado Village B-4 water/sewer plan check Twin Oaks Valley Rd	217,761	-	-
University Commons, Unit 3, San Elijo Rd, water/sewer plan check	212,451	-	-
University Commons Unit 5	115,465	-	-
Subtotal - Developer Financed	\$ 2,818,937	1,463,370	1,441,559
Various Other Projects	\$ 3,112,640	4,838,031	2,326,495
Total	\$ 43,433,213	74,144,173	75,565,571

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(5) Encina Wastewater Authority

The Revised Basic Agreement is a joint exercise of powers agreement by and among the cities of Carlsbad, Vista, and Encinitas, the Buena Sanitation District, the Vallecitos Water District, and the Leucadia Wastewater District for the ownership and operation of a joint sewerage system. The Encina Wastewater Authority (EWA) board is composed of representatives of these Member Agencies. Each Member Agency has an investment in EWA's assets and owns a corresponding proportion of the capacity of the joint system. As of June 30, 2008, the Member Agencies have the following approximate ownership interest:

City of Vista	22%
City of Carlsbad	25%
Buena Sanitation District	8%
Vallecitos Water District	20%
Leucadia Wastewater District	20%
City of Encinitas	5%

The latest available financial statements of EWA, dated June 30, 2008 and 2007, are available directly from EWA (6200 Avenida Encinas, Carlsbad, California 92009), and show the following:

	<u>2008</u>	<u>2007</u>
Total assets	\$ 106,498,723	75,229,524
Total liabilities	<u>6,441,743</u>	<u>2,945,630</u>
Total net assets	<u>\$ 100,056,980</u>	<u>72,283,894</u>
Increase(decrease) in net assets	<u>\$ 27,773,086</u>	<u>9,446,188</u>

(6) Note Receivable from City of San Marcos

In February 1998, the District sold 23.6 acres of excess land to the City of San Marcos for \$1,829,520. The District received \$50,000 and an installment note of \$1,779,520. The note is payable in twenty annual installments of \$148,909 including interest of 5.5%. As of June 30, 2008, the following amounts are due to the District:

<u>Fiscal Year</u>	<u>Principal Amount</u>
2009	\$ 87,176
2010	91,971
2011	97,029
2012	102,365
2013	107,996
2014-2018	<u>635,885</u>
Total	1,122,422
Current portion	<u>(87,176)</u>
Non-current portion	<u>\$ 1,035,246</u>

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(7) Debt Issuance Costs

The debt issuance costs balance relates to the issuance costs of the 2005A Refunding Certificates of Participation. The balance is being amortized over a thirty-two year period. The debt issuance costs, net balances are as follows:

The balance at June 30, consists of the following:	<u>2008</u>	<u>2007</u>
Debt issuance costs	\$ 657,983	538,214
Accumulated amortization	<u>(22,689)</u>	<u>(17,362)</u>
Debt issuance costs, net	<u>\$ 635,294</u>	<u>520,852</u>

(8) Deferred Charges from Debt Retirement

The deferred charges from debt retirement balance relate to the defeasance costs of the District's 1998 Twin Oaks Certificates of Participation. The balance is being amortized over a twenty-six year period.

The deferred charges from debt retirement, net balances are as follows:

The balance at June 30, consists of the following:	<u>2008</u>	<u>2007</u>
Deferred charges from debt retirement	\$ 227,920	237,417
Accumulated amortization	<u>(9,496)</u>	<u>(9,497)</u>
Deferred charges from debt retirement, net	<u>\$ 218,424</u>	<u>227,920</u>

(9) Long-term Debt

2005 Certificates of Participation

On June 30, 2005, the District issued \$66,700,000 in Water and Wastewater Enterprise Certificates of Participation (Series 2005A COPs). The proceeds of the issue are being used to prepay the 1998 Twin Oaks Reservoir Certificates of Participation and to complete the construction of a second buried pre-stressed concrete reservoir at the Twin Oaks Reservoir site, including related grating and earthwork, and the upgrade of the District's Meadowlark Water Reclamation Facility, including the installation of new primary clarifiers, two new filter beds, the reconstruction of the operations and laboratory building, the installation of odor control systems throughout the site, and the addition of a larger emergency generator.

A total of \$23,000,000 from the Series 2005A COPs was used to pay off the outstanding principal, and call premium on the 1998 Twin Oaks Reservoir Certificates of Participation. As a result, the 1998 Twin Oaks Reservoir Certificates of Participation are considered retired and the liability for those obligations has been removed from the financial statements. The District completed the advance refunding to reduce the District's total debt service payments over the next 25 years by \$1,506,316 and to obtain an economic gain of approximately \$1,111,076.

The Series 2005A COPs are payable solely from the net revenues of the District's water and sewer systems as defined in the 2005 Certificates of Participation. The Certificates bear interest at a variable rate with principal maturities from 2007 to 2036.

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(9) Long-term Debt, continued

The balance at June 30, net of unamortized discount is as follows:

	<u>2007</u>	<u>Additions</u>	<u>Principal Pmts Amortization</u>	<u>2008</u>
2005 Series A COP	\$ 65,275,000	-	(1,475,000)	63,800,000
Add: Bond Premium	-	1,708,018	(58,897)	1,649,121
Less: Unamortized Discount	(448,609)	-	15,469	(433,140)
Total	<u>64,826,391</u>	<u>1,708,018</u>	<u>(1,518,428)</u>	<u>65,015,981</u>
Less: current portion	(1,475,000)			(1,255,000)
Long-term portion	<u>\$ 63,351,391</u>			<u>63,760,981</u>

Annual debt service payments are as follows:

<u>Fiscal Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	\$ 1,255,000	3,045,788	4,300,788
2010	1,305,000	3,091,588	4,396,588
2011	1,360,000	3,039,388	4,399,388
2012	1,420,000	2,981,588	4,401,588
2013	1,485,000	2,921,238	4,406,238
2014-2018	8,635,000	13,437,540	22,072,540
2019-2023	11,175,000	10,956,727	22,131,727
2024-2028	14,480,000	7,741,976	22,221,976
2029-2033	17,475,000	3,889,139	21,364,139
2034-2036	5,210,000	775,250	5,985,250
Total	<u>\$ 63,800,000</u>	<u>51,880,222</u>	<u>115,680,222</u>
Less: current portion	(1,255,000)		
Non-current portion	<u>\$ 62,545,000</u>		

In 2007, the District converted its remaining \$63.8 million in COPs from variable auction rate to a fixed rate debt to reduce interest rate risk. At the time of conversion the auction rate was 3.5%. The total-all-in-cost is 4.736%. The \$1.6 million realized in the issue premium was expended toward the Meadowlark Treatment Plant expansion.

(10) Net Investment in Capital Assets

The balance at June 30, consists of the following:

	<u>2008</u>	<u>2007</u>
Investment in Encina Wastewater Authority capital assets	\$ 33,621,939	24,180,604
Capital assets not being depreciated	80,310,079	78,818,207
Net capital assets being depreciated	172,364,136	165,075,072
Debt issuance costs net of amortization	635,294	520,852
Deferred charges from debt retirement	218,424	227,920
Certificates of participation – current portion	(1,255,000)	(1,475,000)
Deposit from San Marcos Unified School District	(189,400)	(189,400)
Portion of COPs attributable to spent proceeds	<u>(63,571,577)</u>	<u>(64,850,547)</u>
Net investment in capital assets	<u>\$ 222,133,895</u>	<u>202,307,708</u>

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(11) Deferred Compensation Savings Plan

For the benefit of its employees, the District participates in two 457 Deferred Compensation Programs (Programs). The purpose of these Programs is to provide deferred compensation for public employees that elect to participate in the Program. Generally, eligible employees may defer receipt of a portion of their salary until termination, retirement, death or unforeseeable emergency. Until the funds are paid or otherwise made available to the employee, the employee is not obligated to report the deferred salary for income tax purposes.

Federal law requires deferred compensation assets to be held in trust for the exclusive benefit of the participants. Accordingly, the District is in compliance with this legislation. Therefore, these assets are not the legal property of the District, and are not subject to claims of the District's general creditors. Market value of all plan assets held in trust by the District's two deferred compensation plans at June 30, 2008 and 2007 amounted to \$1,377,958 and \$1,347,001, respectively.

The District has implemented GASB Statement No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*. Since the District has little administrative involvement and does not perform the investing function for this plan, the assets and related liabilities are not shown on the statement of net assets.

(12) Defined Benefit Pension Plan

Plan Description

The Agency contributes to the California Public Employees Retirement System (CalPERS), a cost-sharing multi-employer defined benefit pension plan. CalPERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. CalPERS acts as a common investment and administrative agent for participating public agencies within the State of California. Benefit provisions and all other requirements are established by state statute and the Agency. Copies of CalPERS annual financial report may be obtained from their executive Office: 400 P Street, Sacramento, CA, 95814.

Funding Policy

The contribution rate for plan members in the CalPERS 3.0% at 60 Risk Pool Retirement Plan is 8% of their annual covered salary. The Agency makes these contributions required of Agency employees on their behalf and for their account. Also, the Agency is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The required employer contribution rates are equal to the annual pension costs (APC) percentage of payroll for fiscal years 2008, 2007 and 2006 as noted below. The contribution requirements of the plan members are established by State statute, and the employer contribution rate is established and may be amended by CalPERS. For fiscal years 2008, 2007 and 2006, the Agencies annual contributions for the CalPERS plan were equal to the Agencies required and actual contribution for each fiscal year as follows:

Three Year Funding Information:

Fiscal Year	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation	APC Percentage of Payroll
2006	\$ 1,072,497	100%	-	19.182%
2007	1,159,400	100%	-	19.688%
2008	1,163,896	100%	-	19.299%

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(13) Post Employment Benefits

The District provides post-employment health benefits in accordance with a resolution approved by the Board of Directors, to all employees who retire from the District under the retirement criteria established by CalPERS, up to age 65. Currently, there are twelve retired employees who meet these eligibility requirements and are therefore receiving the benefits. The post-retirement health care benefits are financed on a pay as you go basis.

The total expense incurred for these benefits for retired employees for the year ended June 30, 2008 and 2007 was \$119,791 and \$115,056, respectively.

Other Post-Employment Benefits Obligation

Plan Description

The District administers the Other Post-employment Benefit Plan, a single-employer defined benefit plan. The District's Other Post-employment Benefit Plan (OPEB) provides continued medical coverage for an eligible retired employee, spouse or registered domestic partner, and eligible dependent at no cost to the retired employee. Coverage will continue for the retiree and spouse or registered domestic partner until they become entitled to Medicare Benefits at age 65. Coverage for the retirees' eligible dependents will continue until they are eligible for coverage under any other health care plan or public health care program or are no longer eligible for coverage under the District's group health plans according to the terms and conditions of the agreement between the group health plan and the District.

Employees are eligible OPEB participants upon reaching age 50 with a minimum five years of eligible PERS service with the District. Board members are also eligible to participate. Eligible retirees and board members may enroll in any of the plans available through the ACWA Program or in an Aetna HMO plan provided by the District. The District's Resolution #788 establishes the authority for the plan. The activity and liability from the OPEB plan are included in these financial statements.

Funding Policy

The District's Resolution #788 provides that the District will pay 100% of the cost of the OPEB plan. The District funds the plan on a pay-as-you-go basis and maintains reserves (and records a liability) for the difference between pay-as-you-go and the actuarially determined annual OPEB cost.

Annual OPEB Cost

The following table shows the components of the District's annual OPEB cost for the year, the amount actually contributed to the plan, and the changes in the District's net OPEB obligation for the year ended June 30th as follows:

The balance at June 30, consists of the following:

	2008	2007
Annual required contribution	\$ 491,368	470,948
Interest on other post employment benefits obligation, net	14,063	-
Adjustment to annual required contribution	(20,701)	-
Annual post employment benefits payable obligation cost	484,730	470,948
Contributions made:		
Retired employees other post employment benefit payments	(120,740)	(119,373)
Increase in net other post employment benefits obligation	363,990	351,575
Other post employment benefits obligation, net – beginning of year	351,575	-
Other post employment benefits obligation, net – end of year	\$ 715,565	351,575

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(13) Post Employment Benefits, continued

Funded Status of the Plan

The most recent valuation (dated July 1, 2006) includes an Actuarial Accrued Liability and Unfunded Actuarial Accrued Liability of \$3,375,974. There are no plan assets because the District funds on a pay-as-you-go basis and maintains reserves equal to the remaining net OPEB obligation. The covered payroll (annual payroll of active employees covered by the plan) for the year ended June 30, 2008 is \$6,820,710. The ratio of the unfunded actuarial liability to annual payroll covered is 49%.

Two Year Trend Information

The District's annual OPEB cost, the percentage of annual OPEB cost contributions to the plan, and the net OPEB obligation for the following fiscal years ended were as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
June 30, 2007	\$ 470,948	25.35%	\$ 351,575
June 30, 2008	484,730	24.91%	715,565

Actuarial Methods and Assumptions

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. Calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and the pattern of sharing of costs between the employer and plan members to that point. Consistent with the long-term perspective of actuarial calculations, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities.

The District's valuation uses the Projected Unit Credit actuarial cost method to project the Annual Required Contribution and a 4% investment return assumption. The high rate of annual health care cost increases experienced in recent years is assumed to gradually decrease, 8% in 2009, 7% in 2010, 6% in 2011, and 5.5% in 2012. A level dollar amortization of the Unfunded Actuarial Accrued Liability is used over a closed 30-year period.

(14) Risk Management

The District is exposed to various risks of loss related to torts, theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District is a member of the Association of California Water Agencies/Joint Powers Insurance Authority (ACWA/JPIA), an intergovernmental risk sharing joint powers authority created to provide self-insurance programs for California water agencies. The purpose of the ACWA/JPIA is to arrange and administer programs of self-insured losses and to purchase excess insurance coverage. At June 30, 2008, the District participated in the liability and property programs of the ACWA/JPIA as follows:

- General and auto liability, public officials and employees' errors and omissions: Total risk financing self-insurance limits of \$1,000,000, combined single limit at \$1,000,000 per occurrence. The District purchased additional excess coverage layers: \$45 million for general, auto and public officials liability, which increases the limits on the insurance coverage noted above.

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(14) Risk Management, continued

In addition to the above, the District also has the following insurance coverage:

- Employee dishonesty coverage up to \$100,000 per loss includes public employee dishonesty, forgery or alteration and theft, disappearance and destruction coverage.
- Property loss is paid at the replacement cost for property on file, if replaced within two years after the loss, otherwise paid on an actual cash value basis, to a combined total of \$50 million per occurrence, subject to a \$10,000 deductible per occurrence.
- Boiler and machinery coverage for the replacement cost up to \$50 million per occurrence, subject to various deductibles depending on the type of equipment.
- Public officials personal liability up to \$15 million each occurrence, with an annual aggregate of \$45 million per each elected/appointed official to which this coverage applies, subject to the terms, with a deductible of \$1,000 per claim.
- Workers' compensation insurance up to California statutory limits for all work related injuries/illnesses covered by California law.

Settled claims have not exceeded any of the coverage amounts in any of the last three fiscal years and there were no reductions in the District's insurance coverage during the years ending June 30, 2008 and 2007. Liabilities are recorded when it is probable that a loss has been incurred and the amount of the loss can be reasonably estimated net of the respective insurance coverage. Liabilities include an amount for claims that have been incurred but not reported (IBNR). There were no IBNR claims payable as of June 30, 2008 and 2007.

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(15) Segment Information

	Condensed Statement of Net Assets			2007
	2008			
	Water	Sewer	Total	
Assets:				
Current assets	\$ 15,400,814	13,477,044	28,877,858	27,717,875
Internal balance	4,202,474	(4,202,474)	-	-
Non-current assets	1,769,466	1,655,429	3,424,895	22,474,108
Capital assets, net	161,710,139	124,586,015	286,296,154	268,073,883
Total assets	\$ 183,082,893	135,516,014	318,598,907	318,265,866
Liabilities:				
Current liabilities	7,752,180	6,362,739	14,114,919	18,943,375
Non-current liabilities	37,977,913	26,688,033	64,665,946	63,892,366
Total liabilities	\$ 45,730,093	33,050,772	78,780,865	82,835,741
Net assets:				
Invested in capital assets, net of related debt	124,154,836	97,979,059	222,133,895	202,307,708
Restricted for future capital facilities	4,821,702	(3,285,739)	1,535,963	19,748,742
Unrestricted	8,376,262	7,771,922	16,148,184	13,373,675
Total net assets	\$ 137,352,800	102,465,242	239,818,042	235,430,125

	Condensed Statement of Revenues, Expenses and Changes in Net Assets			2007
	2008			
	Water	Sewer	Total	
Revenues:				
Operating revenues	\$ 22,536,193	10,915,626	33,451,819	31,146,719
Non-operating revenues	2,704,667	2,007,346	4,712,013	5,756,187
Total revenues	25,240,860	12,922,972	38,163,832	36,902,906
Expenses:				
Operating expenses	21,783,404	8,681,044	30,464,448	30,461,567
Depreciation and amortization	3,960,926	1,972,209	5,933,135	5,528,101
Non-operating expenses	544,564	542,961	1,087,525	1,769,483
Total expenses	26,288,894	11,196,214	37,485,108	37,759,151
Net income/(loss) before capital contributions	(1,048,034)	1,726,758	678,724	(856,245)
Capital contributions	2,099,149	1,610,044	3,709,193	8,547,531
Change in net assets	1,051,115	3,336,802	4,387,917	7,691,286
Net assets, beginning of year	136,301,685	99,128,440	235,430,125	227,738,839
Net assets, end of year	\$ 137,352,800	102,465,242	239,818,042	235,430,125

	Condensed Statement of Cash Flows			2007
	2008			
	Water	Sewer	Total	
Net cash provided (used) by:				
Operating activities	\$ 718,483	2,084,379	2,802,862	3,211,662
Non-capital financing activities	1,479,217	1,299,891	2,779,108	2,405,059
Capital and related financing activities	(13,093,662)	(12,817,815)	(25,911,477)	(49,052,663)
Investing activities	9,733,791	2,093,710	11,827,501	21,560,693
Net cash provided	(1,162,171)	(7,339,835)	(8,502,006)	(21,875,249)
Cash and cash equivalents, beginning of year	9,587,346	7,352,857	16,940,203	38,815,452
Cash and cash equivalents, end of year	\$ 8,425,175	13,022	8,438,197	16,940,203

Vallecitos Water District
Notes to the Basic Financial Statements, continued
For the Years Ended June 30, 2008 and 2007

(16) Commitments and Contingencies

Construction Contracts

The District has a variety of agreements with private parties relating to the installation, improvement or modification of water facilities and distribution systems within its service area. The financing of such construction contracts is being provided primarily from the District's replacement reserves and advances for construction. The District has committed to approximately \$2,026,659 in open construction contracts as of June 30, 2008. These include the following:

<u>Project Name</u>	<u>Contract[s]</u>	<u>To Date</u>	<u>Balance</u>
Meadowlark Reclamation Facility Expansion	\$ 27,265,364	25,342,476	1,922,888
Twin Oaks No. 2 Reservoir Phase III	<u>1,880,160</u>	<u>1,776,389</u>	<u>103,771</u>
	<u>\$ 29,145,524</u>	<u>27,118,865</u>	<u>2,026,659</u>

Grant Awards

Grant funds received by the District are subject to audit by the grantor agencies. Such audit could lead to requests for reimbursements to the grantor agencies for expenditures disallowed under terms of the grant. Management of the District believes that such disallowances, if any, would not be significant.

Litigation

In the ordinary course of operations, the District is subject to claims and litigation from outside parties. After consultation with legal counsel, the District believes the ultimate outcome of such matters, if any, will not materially affect its financial condition.

Supplementary Information Section

Vallecitos Water District
Combining Schedule of Revenue, Expenses, and Changes in Net Assets
For the Year Ended June 30, 2008 with Comparative Totals for the Year Ended June 30, 2007

	2008			2007 Total
	Water	Wastewater	Total	
Operating Revenue	\$ 22,536,193	\$ 10,915,626	\$ 33,451,819	\$ 31,146,719
Operating Expenses:				
Water Division	21,783,404	-	21,783,404	21,265,696
Wastewater division	-	8,681,044	8,681,044	9,195,871
Depreciation	3,960,926	1,972,209	5,933,135	5,528,101
Total Operating Expenses	<u>25,744,330</u>	<u>10,653,253</u>	<u>36,397,583</u>	<u>35,989,668</u>
Operating Income (Loss)	<u>(3,208,137)</u>	<u>262,373</u>	<u>(2,945,764)</u>	<u>(4,842,949)</u>
Nonoperating Revenues:				
Property taxes	1,583,149	1,401,729	2,984,878	2,511,616
Investment income	1,113,901	356,186	1,470,087	3,134,320
Annexation fees	7,617	249,431	257,048	146,323
Total Nonoperating Revenues	<u>2,704,667</u>	<u>2,007,346</u>	<u>4,712,013</u>	<u>5,756,187</u>
Nonoperating Expenses:				
Interest	530,636	542,961	1,073,597	1,769,483
Other	13,928	-	13,928	36,072
Total Nonoperating Expenses	<u>544,564</u>	<u>542,961</u>	<u>1,087,525</u>	<u>1,805,555</u>
Capital Contributions	<u>2,099,149</u>	<u>1,610,044</u>	<u>3,709,193</u>	<u>8,547,531</u>
Total Change in Net Assets	<u><u>1,051,115</u></u>	<u><u>3,336,802</u></u>	<u><u>4,387,917</u></u>	<u><u>7,691,286</u></u>

Vallecitos Water District
Schedule of Operating Expenses – Water Division
For the Years Ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Purchased Water	\$ 13,917,279	13,626,626
Pumping:		
Labor	83,856	72,608
Materials and supplies	21,563	16,434
Outside repair	12,706	6,387
Power	357,671	361,338
Total Pumping	<u>475,796</u>	<u>456,767</u>
Water Quality and Treatment:		
Labor	100,835	85,715
Materials and supplies	23,102	25,119
Outside Repair	43,388	44,793
Power	491	30,209
Total Water Treatment	<u>167,816</u>	<u>185,836</u>
Tanks and Reservoirs:		
Labor	183,886	159,667
Materials and supplies	34,872	27,863
Outside repair	60,724	38,367
Telemetry and power	4,613	2,671
Total Tanks and Reservoirs	<u>284,095</u>	<u>228,569</u>
Transmission and Distribution:		
Labor	540,493	597,205
Materials and supplies	107,558	157,939
Outside repair	139,653	122,842
Telemetry and power	55,642	74,981
Total Transmission and Distribution	<u>843,346</u>	<u>952,967</u>
Services:		
Labor	85,582	79,596
Materials and supplies	51,024	44,412
Outside repair	89,053	60,651
Total Services	<u>225,659</u>	<u>184,659</u>
Meters:		
Labor	73,133	56,603
Materials and supplies	9,992	19,703
Outside repair	3,519	6,668
Total Meters	<u>86,644</u>	<u>82,974</u>

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Vallecitos Water District
Schedule of Operating Expenses – Water Division, continued
For the Years Ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Backflow Prevention:		
Labor	\$ 35,195	28,336
Materials and supplies	83	-
Total Backflow Prevention	<u>35,278</u>	<u>28,336</u>
Meter Reading:		
Labor	<u>59,329</u>	<u>74,151</u>
Customer Accounts:		
Labor	337,287	327,428
Materials and supplies	87,271	75,364
Uncollectible accounts	51,682	30,124
Outside Repair	316	-
Total Customer Accounts	<u>476,556</u>	<u>432,916</u>
Equipment and Vehicles:		
Labor, fuel and repairs	200,931	138,753
Materials and supplies	42,196	116,017
Allocated to wastewater division	<u>(96,675)</u>	<u>(101,358)</u>
Total Equipment and Vehicles	<u>146,452</u>	<u>153,412</u>
Building and Grounds:		
Labor	216,503	156,824
Materials and supplies	45,461	37,493
Outside Repair	104,377	129,441
Power	66,217	77,339
Allocated to wastewater division	<u>(169,474)</u>	<u>(162,030)</u>
Total Building and Grounds	<u>263,084</u>	<u>239,067</u>
Engineering:		
Labor	796,435	654,638
Materials and supplies	32,135	7,404
Outside Repair	78,887	73,652
Allocated to wastewater division	<u>(362,983)</u>	<u>(294,208)</u>
Total Engineering	<u>544,474</u>	<u>441,486</u>
Safety:		
Labor	61,542	49,396
Materials and supplies	36,766	18,961
Safety support	12,517	15,281
Allocated to wastewater division	<u>(44,217)</u>	<u>(33,775)</u>
Total Safety	<u>66,608</u>	<u>49,864</u>

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Vallecitos Water District
Schedule of Operating Expenses – Water Division, continued
For the Years Ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Information Technology		
Labor	\$ 135,392	88,192
Materials and supplies	53,264	4,869
Outside Repair	116,312	45,730
Allocated to wastewater division	(121,951)	(41,498)
Total Information Technology	<u>183,017</u>	<u>97,293</u>
General and Administration:		
Salaries	2,151,654	1,956,077
Other taxes/benefits	30,895	40,521
Social security	866,123	866,634
Group insurance	1,602,921	1,189,304
Public employees' retirement	1,431,347	1,742,498
Workers' compensation insurance	79,464	111,243
District insurance	263,798	252,747
Director's expense	72,552	67,949
Director's fees	49,500	52,500
Public awareness	142,822	95,224
Travel	14,679	20,459
Postage	8,968	20,039
Telephone	33,511	40,013
Office supplies	59,267	48,257
Dues and subscriptions	62,891	59,269
Meetings and seminars	42,508	70,997
Office equipment repair	26,924	28,148
Legal	98,745	146,064
Auditing	22,095	21,236
Outside services	65,426	58,368
Election and annexations	1,762	2,632
Other	72,020	38,153
Administrative credits transferred	(466,081)	(466,671)
Allocated to wastewater division	(2,725,820)	(2,430,888)
Total General and Administration	<u>4,007,971</u>	<u>4,030,773</u>
Total Water Division Expenses	<u>\$ 21,783,404</u>	<u>\$ 21,265,696</u>

Vallecitos Water District
Schedule of Operating Expenses – Wastewater Division
For the Years Ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Collection System:		
Labor	\$ 449,125	\$ 436,512
Materials and supplies	217,210	199,808
Outside repair	94,278	85,167
Power	1,564	1,480
Total Collection System	<u>762,177</u>	<u>722,967</u>
Lift Stations:		
Labor	60,496	57,563
Materials and supplies	6,106	21,243
Outside repair	9,424	3,218
Power	35,355	36,326
Telemetry	-	330
Total Lift Stations	<u>111,381</u>	<u>118,680</u>
Peroxide Station:		
Labor	8,305	9,419
Materials and supplies	1,860	449
Outside repair	-	197
Power	198	203
Telemetry	330	207
Total Peroxide Station	<u>10,693</u>	<u>10,475</u>
Industrial Waste:		
Labor	11,460	8,238
Materials and supplies	40,134	38,900
Total Industrial Waste	<u>51,594</u>	<u>47,138</u>
Encina Disposal	<u>1,876,099</u>	<u>2,966,331</u>
Meadowlark Lift Station:		
Labor	43,515	27,041
Materials and supplies	10,935	2,293
Outside repair	29,617	2,726
Power	40,460	43,141
Total Meadowlark Lift Station	<u>124,527</u>	<u>75,201</u>

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Vallecitos Water District
Schedule of Operating Expenses – Wastewater Division, continued
For the Years Ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Meadowlark Plant:		
Labor	\$ 397,625	300,450
Materials and supplies	555,002	806,413
Outside repair	102,516	61,106
Power	308,967	250,314
Telephone	4,691	2,852
Telemetry	479	409
Total Meadowlark Plant	<u>1,369,280</u>	<u>1,421,544</u>
Mahr Reservoir:		
Labor	22,064	18,732
Materials and supplies	14,707	10,984
Outside repairs	5,333	1,975
Total Mahr Reservoir	<u>42,104</u>	<u>31,691</u>
Customer Accounts:		
Labor	84,945	84,676
Materials and supplies	29,206	25,865
Uncollectible accounts	40,009	22,932
Total Customer Accounts	<u>154,160</u>	<u>133,473</u>
Equipment and Vehicles:		
Labor, fuel and repairs	69,689	42,306
Allocated from water division	96,675	101,358
Total Equipment and Vehicles	<u>166,364</u>	<u>143,664</u>
Buildings and Grounds:		
Allocated from water division	<u>169,474</u>	<u>162,030</u>
Engineering:		
Allocated from water division	<u>362,983</u>	<u>294,208</u>
Safety:		
Labor	-	29,808
Allocated from water division	44,217	33,775
Total Safety	<u>44,217</u>	<u>63,583</u>

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Vallecitos Water District
Schedule of Operating Expenses – Wastewater Division, continued
For the Years Ended June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Information Technology		
Allocated from water division	\$ 121,951	41,498
General and Administration:		
Salaries	148,268	119,317
Other taxes/benefits	3,732	3,357
Social security	164,139	142,381
Group insurance	258,327	181,832
Public employees' retirement	232,603	251,842
Workers' compensation insurance	20,747	25,005
Travel	162	737
Dues and subscriptions	2,649	2,629
Meetings and seminars	998	4,979
Outside services	171	169
Miscellaneous	13,568	14,239
Transfer from water division	2,725,820	2,430,888
Administrative credits transferred	(257,144)	(213,987)
Total General and Administration	<u>3,314,040</u>	<u>2,963,388</u>
Total Wastewater Division Expenses	\$ <u>8,681,044</u>	\$ <u>9,195,871</u>

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Report on Internal Controls and Compliance

