

In the opinion of Sidley Austin LLP, San Francisco, California, Bond Counsel, based on existing statutes, regulations, rulings and judicial decisions and assuming compliance with certain covenants in the documents pertaining to the Bonds and requirements of the Internal Revenue Code of 1986, as amended (the “Code”), as described herein, interest on the Bonds is not includable in the gross income of the owners of the Bonds for federal income tax purposes. In the further opinion of Bond Counsel, interest on the Bonds is not treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals and corporations. Interest on the Bonds, however, is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation’s alternative minimum tax liability. In the further opinion of Bond Counsel, interest on the Bonds is exempt from personal income taxes imposed by the State of California. See “TAX MATTERS” herein.



\$45,315,000
VALLECITOS WATER DISTRICT
WATER AND WASTEWATER ENTERPRISE
2015 REFUNDING REVENUE BONDS

Dated: Date of Issuance

Due: July 1, as set forth below

The 2015 Bonds are being issued to provide funds to provide a portion of the money to prepay a portion of the currently outstanding Vallecitos Water District Water and Wastewater Enterprise Certificates of Participation, Series 2005A, and to pay costs of issuance of the 2015 Bonds, all as more fully described herein.

The 2015 Bonds are being issued in fully registered form and when issued will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York. Purchasers of the 2015 Bonds will not receive securities representing their beneficial ownership in the 2015 Bonds purchased. Interest on the 2015 Bonds is payable on January 1 and July 1 of each year, commencing January 1, 2016, until the maturity thereof. The principal of and interest on the 2015 Bonds are payable by the Trustee to Cede & Co. and such interest and principal payments are to be disbursed to the beneficial owners of the 2015 Bonds through their nominees.

The 2015 Bonds are subject to optional redemption as more fully described herein.

The 2015 Bonds are being issued as a Parity Obligation under the terms of the Master Installment Purchase Contract, dated June 15, 2005, by and between the Vallecitos Water District and the Vallecitos Water District Financing Corporation. The 2015 Bonds are being issued pursuant to the Indenture of Trust, dated as of June 1, 2015, by and between the Vallecitos Water District and MUFJ Union Bank, N.A., as trustee, and a First Supplement to Indenture of Trust, dated June 1, 2015, by and between the same parties. The 2015 Bonds are limited obligations of the District payable solely from Net Revenues of the District’s Water and Wastewater System, which amounts consist of Revenues remaining after payment of Maintenance and Operations Costs of the Water and Wastewater System, subject to certain restrictions described herein, and amounts on deposit in certain funds and accounts created under the Indenture, including amounts in the Rate Stabilization Account, if any. After the refunding contemplated herein, the District will have approximately \$9,515,000 aggregate principal amount of Parity Obligations outstanding payable from Net Revenues on a parity with the 2015 Bonds. The District may incur additional obligations payable from Net Revenues on a parity with the obligation to pay principal of and interest on the 2015 Bonds, subject to the terms and conditions of the Indenture and the Master Contract, and may designate certain obligations as Maintenance and Operation Costs, as more fully described herein.

THE 2015 BONDS ARE A LIMITED OBLIGATION OF THE DISTRICT PAYABLE SOLELY FROM THE REVENUES OF ITS WATER SYSTEM AND WASTEWATER SYSTEM LESS MAINTENANCE AND OPERATIONS COSTS THEREOF (AS DEFINED IN THE MASTER INSTALLMENT PURCHASE CONTRACT), ALL AS FURTHER DESCRIBED HEREIN. SAID OBLIGATION DOES NOT CONSTITUTE A DEBT OF THE DISTRICT OR THE STATE OF CALIFORNIA, OR ANY POLITICAL SUBDIVISION THEREOF, IN CONTRAVENTION OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE DISTRICT OR THE STATE, OR ANY POLITICAL SUBDIVISION THEREOF, IS PLEDGED TO THE PAYMENT OF PRINCIPAL AND INTEREST ON THE 2015 BONDS.

THIS COVER PAGE CONTAINS CERTAIN INFORMATION FOR REFERENCE ONLY. IT IS NOT A SUMMARY OF THIS ISSUE. INVESTORS ARE ADVISED TO READ THE ENTIRE OFFICIAL STATEMENT TO OBTAIN INFORMATION ESSENTIAL TO THE MAKING OF AN INFORMED INVESTMENT DECISION.

MATURITY SCHEDULE – See Inside Cover Page

The 2015 Bonds are offered when, as and if issued and received by the Underwriter, subject to the approval of the valid, legal and binding nature of the 2015 Bonds by Sidley Austin LLP, San Francisco, California, Bond Counsel, and certain other conditions. Certain legal matters will be passed upon for the District by The Law Offices of Jeffrey G. Scott, San Diego, California, General Counsel to the District, and by Stradling Yocca Carlson & Rauth, a Professional Corporation, as Disclosure Counsel, and for the Trustee by its counsel. Ballard Spahr LLP has acted as counsel to the Underwriter in connection with the issuance of the 2015 Bonds. It is anticipated that the 2015 Bonds will be available for delivery through the facilities of The Depository Trust Company on or about July 9, 2015.

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MATURITY SCHEDULE

\$45,315,000
VALLECITOS WATER DISTRICT
WATER AND WASTEWATER ENTERPRISE
2015 REFUNDING REVENUE BONDS

<i><u>Maturity Date</u></i> <i><u>(July 1)</u></i>	<i><u>Principal</u></i> <i><u>Amount</u></i>	<i><u>Interest</u></i> <i><u>Rate</u></i>	<i><u>Price</u></i>	<i><u>Yield</u></i>	<i><u>CUSIP</u></i> [†]
2018	\$1,905,000	4.000%	108.380	1.130%	919176AA5
2019	2,020,000	5.000	113.922	1.390	919176AB3
2020	2,125,000	5.000	116.049	1.630	919176AC1
2021	2,235,000	5.000	117.562	1.880	919176AD9
2022	2,345,000	5.000	118.659	2.110	919176AE7
2023	2,465,000	5.000	119.818	2.270	919176AF4
2024	2,590,000	5.000	120.170	2.480	919176AG2
2025	2,720,000	5.000	120.777	2.620	919176AH0
2026	2,865,000	5.000	118.939 ^(c)	2.810	919176AJ6
2027	3,010,000	5.000	117.796 ^(c)	2.930	919176AK3
2028	3,160,000	5.000	116.759 ^(c)	3.040	919176AL1
2029	3,325,000	5.000	115.826 ^(c)	3.140	919176AM9
2030	3,490,000	5.000	114.810 ^(c)	3.250	919176AN7
2031	1,995,000	5.000	114.077 ^(c)	3.330	919176AP2
2032	2,095,000	5.000	113.623 ^(c)	3.380	919176AQ0
2033	2,210,000	5.000	113.170 ^(c)	3.430	919176AR8
2034	2,320,000	5.000	112.809 ^(c)	3.470	919176AS6
2035	2,440,000	5.000	112.540 ^(c)	3.500	919176AT4

[†] Copyright 2015, American Bankers Association. CUSIP data herein is provided by the CUSIP Service Bureau, managed on behalf of the American Bankers Association by Standard & Poor's. This data is not intended to create a database and does not serve in any way as a substitute for the CUSIP service. CUSIP numbers are provided for reference only. The District, the Financial Advisor and the Underwriter do not assume any responsibility for the accuracy of such numbers.

^(c) Yield to par call on July 1, 2025.

No dealer, broker, salesperson or other person has been authorized by the District or the Underwriter to give any information or to make any representations other than those contained in this Official Statement in connection with the offering made hereby and, if given or made, such other information or representations must not be relied upon as having been authorized by the District or the Underwriter. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of the 2015 Bonds by a person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale.

This Official Statement is not to be construed as a contract with the purchasers of the 2015 Bonds. Statements contained in this Official Statement which involve estimates, forecasts or matters of opinion, whether or not expressly so described herein, are intended solely as such and are not to be construed as a representation of facts.

The Underwriter has provided the following sentence for inclusion in this Official Statement:

The Underwriter has reviewed the information in this Official Statement in accordance with, and as a part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriter does not guarantee the accuracy or completeness of such information.

The information set forth herein has been obtained from official sources which are believed to be reliable but it is not guaranteed as to accuracy or completeness, and is not to be construed as a representation by the Underwriter. The information and expression of opinions herein are subject to change without notice and neither delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the District since the date hereof.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITER MAY OVERALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE 2015 BONDS AT A LEVEL THAT MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME. THE UNDERWRITER MAY OFFER AND SELL THE 2015 BONDS TO CERTAIN DEALERS AND DEALER BANKS AND BANKS ACTING AS AGENT AND OTHERS AT PRICES LOWER THAN THE PUBLIC OFFERING PRICES STATED ON THE INSIDE FRONT COVER PAGE HEREOF AND SAID PUBLIC OFFERING PRICES MAY BE CHANGED FROM TIME TO TIME BY THE UNDERWRITER.

CERTAIN STATEMENTS CONTAINED IN THIS OFFICIAL STATEMENT REFLECT NOT HISTORICAL FACTS BUT FORECASTS AND “FORWARD-LOOKING STATEMENTS.” NO ASSURANCE CAN BE GIVEN THAT THE FUTURE RESULTS DISCUSSED HEREIN WILL BE ACHIEVED, AND ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THE FORECASTS DESCRIBED HEREIN. IN THIS RESPECT, THE WORDS “ESTIMATE,” “PROJECT,” “ANTICIPATE,” “EXPECT,” “INTEND,” “BELIEVE” AND SIMILAR EXPRESSIONS ARE INTENDED TO IDENTIFY FORWARD-LOOKING STATEMENTS. ALL PROJECTIONS, FORECASTS, ASSUMPTIONS, EXPRESSIONS OF OPINIONS, ESTIMATES AND OTHER FORWARD-LOOKING STATEMENTS ARE EXPRESSLY QUALIFIED IN THEIR ENTIRETY BY THE CAUTIONARY STATEMENTS SET FORTH IN THIS OFFICIAL STATEMENT.

THE 2015 BONDS HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, IN RELIANCE UPON AN EXEMPTION CONTAINED IN SUCH ACT. THE 2015 BONDS HAVE NOT BEEN REGISTERED OR QUALIFIED UNDER THE SECURITIES LAWS OF ANY STATE.

The District maintains a website. However, the information presented there is not part of this Official Statement and should not be relied upon in making an investment decision with respect to the 2015 Bonds.

VALLECITOS WATER DISTRICT

BOARD OF DIRECTORS

Betty Evans, President
Mike Sannella, Vice President
Jim Hernandez, Director
Craig Elitharp, Director
Hal Martin, Director

DISTRICT STAFF

Dennis O. Lamb, General Manager
Tom Scaglione, Assistant General Manager
Rhondi Emmanuel, Administrative Services Manager
John Fusco, Finance Manager
Ken Gerdes, Director of Engineering and Operations
James Gumpel, District Engineer
Ed Pedrazzi, Operations and Maintenance Manager

SPECIAL SERVICES

General Counsel

Law Offices of Jeffrey G. Scott
San Diego, California

Bond Counsel

Sidley Austin LLP
San Francisco, California

Disclosure Counsel

Stradling Yocca Carlson & Rauth, a Professional Corporation
Newport Beach, California

Financial Advisor

Fieldman, Rolapp & Associates
Irvine, California

Trustee

MUFG Union Bank, N.A.
Los Angeles, California

Verification Agent

Grant Thornton LLP
Irvine, California

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SUMMARY STATEMENT

This summary is subject in all respects to the more complete information contained in this Official Statement, and the offering of the 2015 Bonds to potential investors is made only by means of the entire Official Statement. Capitalized terms used and not otherwise defined in this Summary Statement have the meanings ascribed to them in this Official Statement.

Purpose. The 2015 Bonds are being issued to provide funds to refund a portion of the currently outstanding Vallecitos Water District Water and Wastewater Enterprise Certificates of Participation Series 2005A, and to pay costs of issuance of the 2015 Bonds, all as more fully described herein.

Security for the 2015 Bonds. The 2015 Bonds are being issued as Parity Obligations within the meaning of the Master Installment Purchase Contract dated as of June 15, 2005 by and between the Vallecitos Water District and the Vallecitos Water District Financing Corporation, as amended. The 2015 Bonds are secured by a pledge of all Net Revenues of the District's Water and Wastewater System. The 2015 Bonds are limited obligations of the District payable solely from Net Revenues of the District's Water and Wastewater System consisting of Revenues remaining after payment of Maintenance and Operation Costs of the Water and Wastewater System, and amounts on deposit in certain funds and accounts created under the Indenture, including amounts in the Rate Stabilization Account, if any. The District may incur additional obligations payable on a parity with the obligation to pay principal of and interest on the 2015 Bonds in the future, and may also designate certain obligations as Maintenance and Operation Costs, as described herein. See the caption "SECURITY FOR THE 2015 BONDS—The Master Contract—Additional Parity Obligations" herein.

THE 2015 BONDS ARE A LIMITED OBLIGATION OF THE DISTRICT PAYABLE SOLELY FROM THE REVENUES OF ITS WATER SYSTEM AND WASTEWATER SYSTEM LESS MAINTENANCE AND OPERATIONS COSTS THEREOF (AS DEFINED IN THE MASTER INSTALLMENT PURCHASE CONTRACT), ALL AS FURTHER DESCRIBED HEREIN. SAID OBLIGATION DOES NOT CONSTITUTE A DEBT OF THE DISTRICT OR THE STATE OF CALIFORNIA, OR ANY POLITICAL SUBDIVISION THEREOF, IN CONTRAVENTION OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE DISTRICT OR THE STATE, OR ANY POLITICAL SUBDIVISION THEREOF, IS PLEDGED TO THE PAYMENT OF PRINCIPAL AND INTEREST ON THE 2015 BONDS.

Refunding Plan. A portion of the proceeds of the 2015 Bonds and certain other money will be transferred to MUFJ Union Bank, N.A., formerly known as Union Bank of California, N.A., as trustee with respect to the 2005A COPs, to refund the \$48,340,000 currently outstanding aggregate principal amount of the 2005A COPs maturing on and after July 1, 2018, on or about the date of issuance of the 2015 Bonds.

Parity Payments. After the refunding contemplated herein, the District will have approximately \$9,515,000 aggregate principal amount of Parity Obligations payable from Net Revenues on a parity with the 2015 Bonds, comprising \$5,795,000 aggregate principal amount due under the 2012 Installment Purchase Contract, and \$3,720,000 aggregate principal amount due under the 2005 Contract corresponding to the 2005A COPs maturing on July 1, 2016 and July 1, 2017. See the caption "THE DISTRICT-Outstanding District Obligations." The District may incur additional obligations on a parity with the 2015 Bonds, subject to the terms and conditions described under the caption "SECURITY FOR THE 2015 BONDS—The Master Contract—Additional Parity Obligations."

Rate Covenant Under the Master Contract. Under the Master Contract, the District has covenanted to fix, prescribe and collect rates, fees and charges for the Service of the Enterprise during each Fiscal Year which are reasonably fair and non-discriminatory and which are estimated to yield Adjusted Annual Net Revenues equal to 115% of Adjusted Annual Debt Service for such Fiscal Year or twelve (12) calendar month period, and Net Revenues equal to 100% of all Payments and all other amounts which are payable from net

Revenues payable in such Fiscal Year or twelve (12) calendar month period (the “Coverage Requirements”), for such Fiscal Year in an amount not less than the Coverage Requirement for such Fiscal Year. The District may make adjustments from time to time in such fees and charges and may make such classification thereof as it deems necessary, but has covenanted under the Master Contract not to reduce rates, fees and charges then in effect, unless the Adjusted Annual Net Revenues from such reduced rates, fees and charges are estimated to be sufficient to meet the Coverage Requirements. See Appendix B—“DEFINITIONS AND SUMMARY OF PRINCIPAL LEGAL DOCUMENTS and see “BOND OWNERS’ RISKS — Issuance of Senior Obligations” for a discussion of the legal ability of the District to designate certain obligations as Maintenance and Operation Costs, and how such designation may reduce the level of coverage otherwise required.

Reserve Fund. No Reserve Fund has been created under the Master Contract or the Indenture for the benefit of the 2015 Bonds.

Rate Stabilization Account. The Master Contract permits the District to establish a Rate Stabilization Account which would be held by the District. The District has not currently established a Rate Stabilization Account as contemplated under the Master Contract. See the caption “SECURITY FOR THE 2015 BONDS—The Master Contract—Rate Stabilization Account.”

Redemption. The 2015 Bonds are subject to optional redemption as described herein.

The District. The District was formed on March 21, 1955, pursuant to the County Water District Law (Division 12, commencing at Section 30000, of the Water Code of the State of California). It was originally named the San Marcos County Water District, but its name was changed to the Vallecitos Water District in 1989. The District includes an area of approximately 45 square miles in the northwestern part of San Diego County. It is located about ten miles east of the Pacific Ocean, 30 miles north of San Diego and 100 miles south of Los Angeles. It currently provides water, wastewater and water reclamation services to nearly all of the City of San Marcos, portions of the cities of Escondido and Carlsbad, and unincorporated areas of San Diego County north and south of the City of San Marcos including the community of Lake San Marcos.

The District currently provides water services to a population of approximately 97,000 people through approximately 21,358 active metered service connections. The District currently purchases substantially all water from the San Diego County Water Authority. The District expects to receive treated water from the Olivenhain Municipal Water District, and desalinated water from the Carlsbad Desalter, in Fiscal Year 2016. The Water System consists of 19 reservoirs with a capacity of nearly 121.5 million gallons of water, approximately 356 miles of pipeline, and 9 pump stations. See the caption “THE ENTERPRISE—Water System.”

The District currently provides wastewater collection and treatment services to a population of approximately 97,000 people through 20,470 service connections and approximately 273 miles of pipeline. Wastewater collected by the District is treated at its Meadowlark Water Reclamation Facility or through treatment facilities owned by the Encina Wastewater Authority, of which the District is a member. See the caption “THE ENTERPRISE—Wastewater System.”

Changes Since the Date of the Preliminary Official Statement. The following changes have been made in “APPENDIX B - DEFINITIONS AND SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS” in this Official Statement since the Preliminary Official Statement, dated June 4, 2015, to reflect comments to the Indenture received from the Trustee including: the definition of “Permitted Investments” under the caption “Definitions,” and under the following captions under the heading “INDENTURE OF TRUST”: “Payments into Other Funds; Rate Stabilization Fund-Investment of Moneys in Funds and Accounts,” “Covenants-Continuing Disclosure Agreement,” “Default and Limitations of Liability-No Liability by the District to the Owners,” “Default and Limitations of Liability-Events of Default,” and “The Trustee-Liability of Trustee.”

\$45,315,000
VALLECITOS WATER DISTRICT
WATER AND WASTEWATER ENTERPRISE
2015 REFUNDING REVENUE BONDS

INTRODUCTION

General

This Official Statement, including the cover page, the inside cover page and all appendices hereto, provides certain information concerning the sale and delivery of the Vallecitos Water District Water and Wastewater Enterprise 2015 Refunding Revenue Bonds (the “2015 Bonds”). The 2015 Bonds will be issued as Parity Obligations within the meaning and subject to the terms of the Master Installment Purchase Contract, by and between the Vallecitos Water District (the “District”) and the Vallecitos Water District Financing Corporation (the “Corporation”). The 2015 Bonds will be issued pursuant to an Indenture of Trust, dated as of June 1, 2015 (the “Master Indenture”), by and between the District and MUFG Union Bank, N.A., as trustee (the “Trustee”), as supplemented by a First Supplement to Indenture of Trust, dated as of June 1, 2015, by and between the District and the Trustee (the “First Supplement” and, collectively, the “Indenture”). Capitalized terms used and not otherwise defined herein have the meanings ascribed to them in Appendix B—“DEFINITIONS AND SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS.”

The 2015 Bonds are being issued to provide funds to provide a portion of the money to prepay a portion of the currently outstanding Vallecitos Water District Water and Wastewater Revenue Enterprise Certificates of Participation Series 2005A (the “2005A COPs”) as described under the caption “REFUNDING PLAN”, and to pay costs of issuance of the 2015 Bonds. See the caption “ESTIMATED SOURCES AND USES OF FUNDS.”

The 2015 Bonds are limited obligations of the District payable solely from Net Revenues, which consist of Revenues of the District’s Water and Wastewater Systems (the “Enterprise”) remaining after payment of Maintenance and Operation Costs of the Enterprise, as such terms are defined in Appendix B hereto, and amounts on deposit in certain funds and accounts created under the Indenture, including amounts in the Rate Stabilization Account, if any. After the issuance of the 2015 Bonds, the District will have \$9,515,000 of Parity Obligations outstanding, comprising \$5,795,000 due under the 2012 Installment Purchase Contract, and \$3,720,000 aggregate principal amount due under the 2005 Contract (as defined herein) corresponding to the unrefunded 2005A COPs maturing on July 1, 2016 and July 1, 2017 (the “Unrefunded 2005A COPs”). The District may incur additional obligations payable on a parity with the obligation to pay principal of and interest on the 2015 Bonds in the future. See the caption “SECURITY FOR THE 2015 BONDS—Additional Indebtedness.” See Appendix B—“DEFINITIONS AND SUMMARY OF PRINCIPAL LEGAL DOCUMENTS” and see “BOND OWNERS’ RISKS — Issuance of Senior Obligations” for a discussion of the legal ability of the District to designate certain obligations as Maintenance and Operation Costs, and how such designation may reduce the level of coverage otherwise required.

The summaries and references to the Indenture, the Master Contract, and all documents, statutes, reports and other instruments referred to herein do not purport to be complete, comprehensive or definitive, and each such summary or reference is qualified in its entirety by reference to the full Indenture and each such document, statute, report or instrument, copies of which are available for inspection at the offices of the District in Encinitas, California and will be available from the Trustee upon request and payment of duplication cost. Unless otherwise indicated, all financial and statistical information herein has been provided by the District.

The District regularly prepares a variety of reports, including audits, budgets and related documents. Any registered owner of the 2015 Bonds (each, an “Owner”) may obtain a copy of such reports, as available,

from the Trustee or the District. Additional information regarding the Official Statement may be obtained by contacting the Trustee or Vallecitos Water District, 201 Vallecitos De Oro, San Marcos, CA 92069 Telephone: (760) 744-0460.

REFUNDING PLAN

General

The 2005A COPs represent the proportionate undivided interests of the registered owners thereof in installment payments (the “2005 Installment Payments”) payable by the District under the Master Installment Purchase Contract, dated as of June 15, 2005, by and between the District and Vallecitos Water District Financing Corporation, a nonprofit public benefit corporation (the “Corporation”), as supplemented by the First Supplemental Installment Purchase Contract, dated as of June 15, 2005 (the “2005 Contract”) by and between the District and the Corporation (as supplemented, the “Master Contract”). The 2005 COPs were executed and delivered pursuant to the Trust Agreement, dated as of June 15, 2005, by and among the District, the Corporation and Union Bank of California, N.A., as trustee (currently known as MUFJ Union Bank, N.A.), as supplemented by the First Supplemental Trust Agreement, dated as of June 1, 2007, by and among said parties (the “Trust Agreement”). Pursuant to the Trust Agreement, the Corporation has assigned to the Trustee for the benefit of the owners of the 2005A COPs substantially all its rights under the 2005 Contract, including its right to receive 2005 Installment Payments payable under the 2005 Contract and its right to enforce payment by the District of the 2005 Installment Payments when due. The 2005A COPs are currently outstanding in the aggregate principal amount of \$53,775,000.

The District plans to apply a portion of the proceeds of the 2015 Bonds and certain other moneys to prepay a portion of the outstanding obligations with respect to the Refunded 2005A COPs (as defined below):

<i>Principal Payment Date (July 1)⁽¹⁾</i>	<i>Original Principal Amount of 2005A COPs</i>	<i>Refunded Principal Amount of 2005A COPs</i>	<i>Outstanding Principal Amount of 2005A COPs after Refunding</i>
2016	\$ 1,810,000	--	\$ 1,810,000
2017	1,910,000	--	1,910,000
2018	1,985,000	\$ 1,985,000	--
2019	2,120,000	2,120,000	--
2020	2,235,000	2,235,000	--
2021	2,355,000	2,355,000	--
2022	2,480,000	2,480,000	--
2023	2,610,000	2,610,000	--
2024	2,745,000	2,745,000	--
2027	9,125,000	9,125,000	--
2032	15,060,000	15,060,000	--
2035	<u>7,625,000</u>	<u>7,625,000</u>	<u>--</u>
TOTAL	\$ 52,060,000	\$ 48,340,000	<u>\$ 3,720,000</u>

⁽¹⁾ Assumes the District makes regularly scheduled July 1, 2015 payment under the 2005 Contract.

Source: District

The refunded principal amounts of each 2005A COP maturing on July 1, 2018 through July 1, 2035, inclusive, as set forth in the third column in the above table, constitute the “Refunded 2005A COPs.” Upon refunding the Refunded 2005A COPs, \$3,720,000 aggregate principal amount of the 2005 Contract which corresponds to the Unrefunded 2005A COPs, will remain outstanding. The Unrefunded 2005A COPs are payable from payments made by the District under the 2005 Contract from Net Revenues on a parity with payments due on the 2015 Bonds, and the 2012 Installment Payment.

To effect such refunding, the District will cause a portion of the proceeds of the 2015 Bonds and certain other moneys to be deposited into the Escrow Fund (the “2005A Escrow Fund”) established under the Escrow Agreement (2005A COPs), dated as of June 1, 2015 (the “2005A Escrow Agreement”), by and between the District and MUFG Union Bank, N.A. (previously known as Union Bank of California, N.A.), as escrow agent (the “Escrow Agent”). Such amounts will be held in cash or invested in direct general obligations of the United States of America (the “Government Obligations”). Sufficiency of the deposits in the 2005A Escrow Fund to pay such amounts will be verified by Grant Thornton LLP, Irvine, California (the “Verification Agent”).

With respect to the Refunded 2005A COPs, cash and certain Government Obligations will be scheduled to mature in such amounts and at such times and bear interest at such rates as to provide amounts sufficient to pay on or about the date of issuance of the 2015 Bonds, regularly scheduled principal and interest with respect to the Refunded 2005A COPs on and prior to July 1, 2017 and to pay on July 1, 2017 the prepayment price of the 2005A COPs maturing after July 1, 2017, without premium.

All cash and Government Obligations in the Escrow Fund will be irrevocably pledged to secure, when due, the payment of the principal, interest with respect to the 2005A COPs and will not be available to pay the principal or interest on the 2015 Bonds.

Verification

The Verification Agent will verify the mathematical accuracy of the information provided to the Verification Agent as of the date of the closing on the 2015 Bonds relating to the adequacy of the amounts deposited in the Escrow Fund to pay regularly scheduled principal and interest with respect to the Refunded 2005A COPs on and prior to July 1, 2017 and to pay on July 1, 2017 the prepayment price of the Refunded 2005A COPs maturing after July 1, 2017, and the computation of the yield of the Refunded 2005A COPs and the 2015 Bonds which support Bond Counsel’s opinion that interest with respect to the 2015 Bonds received by the Owners is excluded from gross income for federal income tax purposes.

THE 2015 BONDS

General Provisions

The 2015 Bonds will be issued in the aggregate principal amount of \$45,315,000. The 2015 Bonds will be dated the date of delivery (the “Issuance Date”), will be issued in denominations of \$5,000 or any integral multiple thereof, and will bear interest from such date at the rates per annum set forth on the inside cover page hereof, payable semiannually on July 1 and January 1 of each year, commencing January 1, 2016 (each, an “Interest Payment Date”), and will mature on the dates set forth on the inside cover page hereof. Interest on the 2015 Bonds will be computed on the basis of a 360 day year of twelve 30 day months.

The 2015 Bonds will be issued in fully registered form and will be initially registered in the name of “Cede & Co.,” as nominee of The Depository Trust Company (“DTC”). The 2015 Bonds will be evidenced by one 2015 Bond maturing on each of the maturity dates as set forth in the Indenture, in a denomination corresponding to the total principal amount of the 2015 Bonds of such maturity. See the caption “—Book Entry Only System” below and Appendix D attached hereto. Each 2015 Bond may be assigned by the Trustee a distinctive number or letter and number, and a record of the same shall be maintained by the Trustee. Registered ownership of the 2015 Bonds, or any portion thereof, may not thereafter be transferred except as provided for in the Indenture.

Interest on the 2015 Bonds shall be payable commencing on each Interest Payment Date in lawful money of the United States of America by check mailed by first class mail on each interest payment date to the Owner thereof as of the close of business on the fifteenth (15th) day of the calendar month immediately preceding such interest payment date (the “Record Date”); provided, that upon the written request of an Owner

of one million dollars (\$1,000,000) or more in aggregate principal amount of 2015 Bonds received by the Trustee prior to the applicable Record Date (which such request shall remain in effect until rescinded in writing by such Owner), interest shall be paid by wire transfer in immediately available funds. The principal of and premium, if any, on the 2015 Bonds are payable when due upon presentation thereof at the Corporate Trust Office of the Trustee, in lawful money of the United States of America.

Book-Entry Only System

The 2015 Bonds will be delivered in book-entry form only. Purchasers of the 2015 Bonds will not receive certificates representing their ownership interests therein. So long as the 2015 Bonds are maintained in book entry form, payments of principal, premium, if any, and interest shall be made by the Trustee to the DTC by wire transfer. DTC is expected to credit such payments to the respective accounts of its Direct Participants which, in turn, are expected to make payment thereof to the purchasers of the 2015 Bonds.

As long as Cede & Co. is the registered owner of the 2015 Bonds, references herein to the Owners of the 2015 Bonds shall refer to Cede & Co. and not to the beneficial owners of the 2015 Bonds (the “Beneficial Owners”). The District does not give any assurance that DTC, its Direct Participants or others will distribute payments with respect to the 2015 Bonds or notices concerning the 2015 Bonds to the Beneficial Owners thereof or that DTC will otherwise serve and act in the manner described in this Official Statement. See Appendix D — “INFORMATION CONCERNING DTC” for a further description of DTC and its book entry system. The information presented therein is based solely on information provided by DTC.

The District may determine that it is in the best interests of the Beneficial Owners of the 2015 Bonds that they be able to obtain securities certificates, in which event the Trustee shall, upon the written instruction of the District, notify DTC, and DTC will notify the Beneficial Owners of the availability through DTC of securities certificates. In such event, such 2015 Bonds will be transferable in accordance with the Indenture.

DTC may determine to discontinue providing its services with respect to the 2015 Bonds at any time by giving written notice of such discontinuance to the District and the Trustee and discharging its responsibilities with respect thereto under applicable law. In such event, the 2015 Bonds will be transferable in accordance with the Indenture.

Whenever DTC requests the District and the Trustee to do so, the Trustee and the District shall cooperate with DTC in taking appropriate action after reasonable notice to arrange for another securities depository to maintain custody of the 2015 Bonds then Outstanding. In such event, the 2015 Bonds shall be transferable to such securities depository in accordance with the Indenture and thereafter, all references in the Indenture to DTC or its nominee shall be deemed to refer to such successor securities depository and its nominee, as appropriate.

Transfers and Exchanges

The 2015 Bonds may be exchanged at the Corporate Trust Office of the Trustee for a like aggregate principal amount of 2015 Bonds of other authorized denominations of the same Series, tenor, maturity and interest rate by the person in whose name it is registered, in person or by his duly authorized attorney, upon surrender of such 2015 Bond for cancellation; provided that, unless otherwise provided no exchange may occur during the period established by the Trustee for selection of 2015 Bonds for redemption, or of any 2015 Bond or portion of a 2015 Bond so selected for redemption. The Trustee shall require the Owner requesting such exchange to pay any tax or other governmental charge required to be paid with respect to such exchange. The cost of printing Bonds and any services rendered or expenses incurred by the Trustee in connection with any exchange shall be paid by the District.

Any 2015 Bond may, in accordance with its terms, be transferred, upon the register required to be kept pursuant to the Indenture, by the person in whose name it is registered, in person or by his duly authorized

attorney, upon surrender of such 2015 Bond for cancellation, accompanied by delivery of a written instrument of transfer, duly executed in a form acceptable to the Trustee. Whenever any 2015 Bond or 2015 Bonds shall be surrendered for transfer, the District shall execute and the Trustee shall authenticate and deliver a new 2015 Bond or 2015 Bonds, of the same Series, tenor, maturity and interest rate and for a like aggregate principal amount; provided that no registration or transfer may occur during the period established by the Trustee for selection of 2015 Bonds for redemption, or of any 2015 Bond or portion of a 2015 Bond so selected for redemption. The Trustee shall require the owner of such 2015 Bond requesting such transfer to pay any tax or other governmental charge required to be paid with respect to such transfer. The cost of printing 2015 Bonds and any services rendered or expenses incurred by the Trustee in connection with any transfer shall be paid by the District.

Redemption of the 2015 Bonds

Optional Redemption of 2015 Bonds. The 2015 Bonds maturing on or before July 1, 2025 will not be subject to call or redemption prior to maturity. The 2015 Bonds maturing on or after July 1, 2026 will be subject to redemption prior to their respective stated maturities, at the option of the District, from any source of available funds, as a whole or in part on any date (by such maturities as may be specified by the District and by lot within a maturity), on or after July 1, 2025, at a redemption price equal to the principal amount of the 2015 Bonds called for redemption together with accrued interest thereon to the date of redemption, without premium.

The District shall notify the Trustee at least forty-five (45) days prior to the redemption date for 2015 Bonds pursuant to the Indenture. Notice of redemption shall be given in the form and in accordance with the terms of the Indenture.

Notice of Redemption

When redemption is authorized or required, at least 30, but not more than 60 days prior to the redemption date, the Trustee shall mail by first class mail a notice of redemption to the respective Owners of all 2015 Bonds selected for redemption in whole or in part. The Trustee shall also provide notice to the Municipal Securities Rulemaking Board's "EMMA" portal by facsimile or electronic transmission. Each such notice shall state the date of such notice, the 2015 Bonds to be redeemed, the date of issue of such 2015 Bonds, the redemption date, the redemption price, the place or places of redemption (including the name and appropriate address or addresses of the Trustee), the CUSIP number (if any) of the maturity or maturities of the 2015 Bonds to be redeemed and, if less than all of the 2015 Bonds of any such maturity are to be redeemed, the numbers of the 2015 Bonds of such maturity to be redeemed and, in the case of 2015 Bonds to be redeemed in part only, the respective portions of the principal amount thereof to be redeemed, and shall give notice that further interest on such 2015 Bonds or the portions thereof to be redeemed will not accrue from and after the redemption date, and shall require that such 2015 Bonds be then surrendered at the address or the addresses of the Trustee so designated; provided, that neither the District nor the Trustee shall have any responsibility for any defect in the CUSIP number that appears on any 2015 Bond or in any redemption notice with respect thereto, and any such redemption notice may contain a statement to the effect that CUSIP numbers have been assigned by an independent service for convenience of reference and that neither the District nor the Trustee shall be liable for any inaccuracy in such numbers. If any 2015 Bond so chosen for redemption shall not be redeemable in whole, such notice shall also state that such 2015 Bond is to be redeemed in part only and that upon presentation of such 2015 Bond for redemption there will be issued in lieu of the unredeemed portion of principal thereof a new 2015 Bond or 2015 Bonds of the same maturity date, of authorized denominations equal in aggregate principal amount to such unredeemed portion.

With respect to any notice of optional redemption of 2015 Bonds, unless upon the giving of such notice, such 2015 Bonds shall be deemed to have been paid in accordance with the Indenture, or unless the Trustee has moneys or Government Obligations sufficient to pay the principal, redemption premium, if any, and interest on the 2015 Bonds to be redeemed, such notice may state that such redemption shall be

conditional upon the receipt by the Trustee on or prior to the date fixed for such redemption of moneys sufficient to pay the interest on and principal of and redemption premium, if any, on such 2015 Bonds, and that if such moneys shall not have been so received the notice shall be of no force and effect and the Trustee shall not be required to redeem such 2015 Bonds. In the event that the notice of redemption contains such a condition and such moneys are not so received, the redemption shall not be made and the Trustee shall, within a reasonable time thereafter, give notice, in the manner in which the notice of redemption was given, that such moneys were not so received.

Effect of Redemption

When notice of redemption has been given, substantially as provided in the Indenture, and when the amount necessary for the payment of the Redemption Price is set aside for that purpose, the 2015 Bonds designated for redemption shall become due and payable on the redemption date specified, and upon presentation and surrender of said 2015 Bonds, at the place specified in the notice of redemption, such 2015 Bonds shall be redeemed and paid at said Redemption Price, and no interest shall accrue on such 2015 Bonds called for redemption after the redemption date specified in such notice. The Owners of said 2015 Bonds so called for redemption after such redemption date shall look for the payment of such 2015 Bonds and the premium thereon only to said amounts set aside for such purpose. All 2015 Bonds redeemed shall be cancelled forthwith and shall not be reissued.

All unpaid interest payable at or prior to the redemption date shall continue to be payable to the respective registered Owners of such 2015 Bonds, or their order, but without interest thereon.

DEBT SERVICE PAYMENT SCHEDULE

Set forth below is a schedule of principal of and interest on the 2015 Bonds and obligations outstanding on a parity with the 2015 Bonds (the "Parity Obligations") payable in the Fiscal Years ending June 30 indicated:

<i>2015 Bonds</i>				<i>Outstanding Parity Obligations⁽¹⁾</i>	
<i>June 30</i>	<i>Principal</i>	<i>Interest</i>	<i>Total</i>	<i>Obligations⁽¹⁾</i>	<i>Total</i>
2016	--	\$ 1,073,423	\$ 1,073,423	3,947,660	\$ 5,021,083
2017	--	2,246,700	2,246,700	2,742,654	4,989,354
2018	--	2,246,700	2,246,700	2,746,032	4,992,732
2019	\$ 1,905,000	2,208,600	4,113,600	807,558	4,921,158
2020	2,020,000	2,120,000	4,140,000	777,044	4,917,044
2021	2,125,000	2,016,375	4,141,375	776,551	4,917,926
2022	2,235,000	1,907,375	4,142,375	777,760	4,920,135
2023	2,345,000	1,792,875	4,137,875	779,643	4,917,518
2024	2,465,000	1,672,625	4,137,625	--	4,137,625
2025	2,590,000	1,546,250	4,136,250	--	4,136,250
2026	2,720,000	1,413,500	4,133,500	--	4,133,500
2027	2,865,000	1,273,875	4,138,875	--	4,138,875
2028	3,010,000	1,127,000	4,137,000	--	4,137,000
2029	3,160,000	972,750	4,132,750	--	4,132,750
2030	3,325,000	810,625	4,135,625	--	4,135,625
2031	3,490,000	640,250	4,130,250	--	4,130,250
2032	1,995,000	503,125	2,498,125	--	2,498,125
2033	2,095,000	400,875	2,495,875	--	2,495,875
2034	2,210,000	293,250	2,503,250	--	2,503,250
2035	2,320,000	180,000	2,500,000	--	2,500,000
2036	2,440,000	61,000	2,501,000	--	2,501,000
TOTAL	\$ 45,315,000	\$26,507,173	\$71,822,173	\$13,354,901	\$85,177,074

⁽¹⁾ Represents principal and interest due on the 2012 Installment Purchase Contract and on the 2005 Contract corresponding to the Unrefunded 2005A COPs, as described under the caption "THE VALLECITOS WATER DISTRICT- Outstanding District Obligations- Outstanding Obligations Payable From Net Revenues On A Parity With The 2015 Bonds."

SECURITY FOR THE 2015 BONDS

The Indenture

The 2015 Bonds are being issued pursuant to the Indenture as a Parity Obligation under the provisions of the Master Contract. The Indenture obligates the District to make payments of principal of and interest on the 2015 Bonds solely from Net Revenues of the District's Enterprise (see the caption "-The Master Contract- Net Revenues"). After issuance of the 2015 Bonds, the District will have the following outstanding Parity Obligations: the 2012 Installment Purchase Agreement, and the 2005 Contract corresponding to the Unrefunded 2005A COPs, both of which are payable on a parity with the 2015 Bonds. See the caption "THE DISTRICT-Outstanding District Obligations-Outstanding Obligations Payable From Net Revenues On A Parity With The 2015 Bonds" for a more detailed description of the 2012 Installment Purchase Agreement. The District may incur additional Parity Obligations, which will be payable from Net Revenues on a parity with the 2015 Bonds and the 2012 Installment Purchase Agreement. See the caption "-Master Contract- Additional Parity Obligations." The District may also issue Subordinate Obligations. The District's only Subordinate Obligation is the UBOC Loan, as described under the caption "THE DISTRICT-Outstanding

District Obligations- Other Outstanding Obligations.” See Appendix B—“DEFINITIONS AND SUMMARY OF PRINCIPAL LEGAL DOCUMENTS and see “BOND OWNERS’ RISKS — Issuance of Senior Obligations” for a discussion of the legal ability of the District to designate certain obligations as Maintenance and Operation Costs, and how such designation may reduce the level of coverage otherwise required.

THE 2015 BONDS ARE A LIMITED OBLIGATION OF THE DISTRICT PAYABLE SOLELY FROM THE REVENUES OF ITS WATER SYSTEM AND WASTEWATER SYSTEM LESS MAINTENANCE AND OPERATIONS COSTS THEREOF (AS DEFINED IN THE MASTER INSTALLMENT PURCHASE CONTRACT), ALL AS FURTHER DESCRIBED HEREIN. SAID OBLIGATION DOES NOT CONSTITUTE A DEBT OF THE DISTRICT OR THE STATE OF CALIFORNIA, OR ANY POLITICAL SUBDIVISION THEREOF, IN CONTRAVENTION OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION. NEITHER THE FAITH AND CREDIT NOR THE TAXING POWER OF THE DISTRICT OR THE STATE, OR ANY POLITICAL SUBDIVISION THEREOF, IS PLEDGED TO THE PAYMENT OF PRINCIPAL AND INTEREST ON THE 2015 BONDS.

The Master Contract

General. The Master Contract establishes the terms and conditions upon which certain obligations of the District shall be incurred and secured. Pursuant to the Master Contract, the District irrevocably grants and pledges the Net Revenues first to secure Parity Obligations (including the 2015 Bonds, the 2012 Installment Purchase Contract, the 2005 Contract corresponding to the Unrefunded 2005A COPs, and any Supplemental Contracts and Payment Agreements secured by a lien on Net Revenues on a parity with the 2015 Bonds and the 2012 Installment Purchase Contract) and second, to secure obligations which are subordinate to the payments due with respect to the Parity Obligations (the “Subordinate Obligations” and, together with the Parity Obligations, the “Obligations”). All Parity Obligations will be of equal rank without preference, priority or distinction of any Parity Obligations over any other Parity Obligations.

The Master Contract established the “Vallecitos Water District Revenue Fund,” which may be the District’s General Fund and which is to be held and maintained by the District for so long as any Payments due under the Master Contract shall be Outstanding. The District treats its Water Enterprise Fund and Wastewater Enterprise Fund as the Revenue Fund for the purpose of the Master Contract. The District has agreed and covenanted in the Master Contract to deposit all Revenues received by it into the Revenue Fund when and as received. In addition, the District may from time to time as it deems necessary or appropriate transfer to the Revenue Fund amounts on deposit in the Rate Stabilization Account.

Net Revenues. The term “Revenues” means, for any Fiscal Year or twelve (12) calendar month period, all income and revenue received or receivable by the District during such Fiscal Year or twelve (12) calendar month period from the ownership or operation of the Enterprise, determined in accordance with Generally Accepted Accounting Principles, including all Ad Valorem Taxes, ad valorem assessments, Capacity Facility Fees, standby charges, rates, fees and charges received by the District for the Service, all proceeds of insurance covering business interruption loss relating to the Enterprise, all connection fees and charges payable to the District for the Service made available or provided by the Enterprise, all payments for the lease of property comprising a part of the Enterprise, all other income and revenue howsoever derived by the District from the ownership or operation of the Enterprise or arising from the Enterprise, all Payment Agreement Receipts, and all income from the investment of amounts on deposit in the Revenue Fund and the Parity Obligation Payment Fund, but excluding in all cases: (i) any proceeds of taxes and assessments levied and collected by or on behalf of the District for obligations that are payable solely from such taxes (including Ad Valorem Taxes) or assessments and not from any other Revenues, (ii) any refundable deposits made to establish credit and any advances or contributions in aid of construction, and (iii) any income from the investment of amounts on deposit in the Improvement Fund.

“Net Revenues” means, for any Fiscal Year or twelve (12) calendar month period, the Revenues during such Fiscal Year or twelve (12) calendar month period less the Maintenance and Operation Costs during such Fiscal Year or twelve (12) calendar month period.

“Maintenance and Operation Costs” means, for any Fiscal Year or twelve (12) calendar month period, all reasonable and necessary costs paid or incurred by the District during such Fiscal Year or twelve (12) calendar month period for maintaining and operating the Enterprise, determined in accordance with Generally Accepted Accounting Principles, including all reasonable expenses of management and repair and other expenses necessary to maintain and preserve the Enterprise in good repair and working order, all amounts due under Contract Resource Obligations (but only under the circumstances described below) all administrative costs of the District that are charged directly or apportioned to the operation of the Enterprise, such as salaries and wages of employees, overhead, taxes (if any), insurance premiums and payments into pension funds, and all other reasonable and necessary costs of the District or charges required to be paid by it to comply with the terms hereof or of any resolution authorizing the execution or issuance of any Parity Obligation or of such Parity Obligation, such as compensation, reimbursement and indemnification of the Trustee and fees and expenses of Independent Certified Public Accountants and Independent Engineers, but excluding in all cases depreciation, replacement and obsolescence charges or reserves therefor and amortization of intangibles.

A “Contract Resource Obligation” is an obligation of the District, designated as a Contract Resource Obligation and entered into pursuant to the Master Contract, to make payments to another party for the acquisition of capacity or right of service, supply or use in or from water and wastewater facilities to be used by the District in providing the services of the Enterprise. Pursuant to the Master Contract, the District may at any time enter into one or more Contract Resource Obligations related to existing facilities or facilities to be constructed; and the District may determine that, and may agree under a Contract Resource Obligation to provide that, all payments under that Contract Resource Obligation shall be Maintenance and Operation Costs if the following requirements are met at the time such Contract Resource Obligation is entered into:

(1) No Event of Default, as defined in the Master Contract, has occurred and is continuing;

(2) There shall be on file a certificate of an Independent Engineer stating that (i) the payments to be made by the District in connection with the Contract Resource Obligation are reasonable, (ii) the facilities, services, supply or use for which the Contract Resource Obligation will be incurred are technically and economically feasible and are available or are likely to be available no later than a date set forth in the Independent Engineer’s certification, and (iii) the Adjusted Annual Net Revenues (further adjusted by the Independent Engineer’s estimate of the payments to be made in accordance with the Contract Resource Obligation) for the five Fiscal Years following the year in which the Contract Resource Obligation is incurred, as such Adjusted Annual Net Revenues are estimated by the Independent Engineer in the manner described below under the caption “-Additional Parity Obligations,” will be at least equal to the Coverage Requirement.

The District does not currently have any Contract Resource Obligations outstanding. See “BONDOWNERS’ RISKS — Issuance of Senior Obligations.”

Application of Revenues. In order to carry out and effectuate the obligations of the District contained in the 2015 Bonds, the 2012 Installment Purchase Agreement, and with respect to any other Parity Obligations, the District has agreed and covenanted under the Master Contract and the Indenture that all Revenues received by it shall be deposited when and as received in the Revenue Fund. Additionally, amounts may, from time to time as the District deems necessary or appropriate, be transferred from the Rate Stabilization Account (if any) and deposited in the Revenue Fund.

The District shall withdraw or transfer from the Revenue Fund and pay or deposit such amounts for the following purposes in the following order, the amounts set forth below:

First, the District will pay all Maintenance and Operation Costs (including amounts reasonably required to be set aside in contingency reserves for Maintenance and Operation Costs the payment of which is not then immediately required) from the Revenue Fund as they become due; and

Second, on or before the fifth Business Day immediately preceding each Interest Payment Date and Principal Payment Date, the District shall, from the remaining money then on deposit in the Revenue Fund, deposit in the "Vallecitos Water District Parity Obligation Payment Fund," which fund the District has agreed pursuant to the Master Contract to hold and maintain so long as any Parity Payments shall be Outstanding, the following amounts in the following order of priority: (1) a sum equal to (A) the interest and principal payments becoming due and payable under all Parity Obligations, plus (B) the net payments becoming due and payable on Parity Payment Agreements (except any Termination Payments), plus (C) any other amounts due with respect to Parity Obligations (including any letter of credit and remarketing fees), in each case, during the next succeeding month; plus (2) all amounts due to make up any deficiency in the Reserve Funds for Parity Obligations including any Reserve Fund established with respect to a Series of Bonds in accordance with the provisions of the applicable Supplemental Indenture or other Issuing Document, including all Reserve Fund Credit Facility Costs.

From time to time, moneys on deposit in the Parity Obligation Payment Fund shall be transferred by the District to the Trustee or other third party payee thereof in accordance with the terms of the Parity Obligations to make and satisfy the Parity Payments due on the next applicable Payment Dates on such Parity Obligations. In the event that any Parity Obligation has been paid from amounts made available pursuant to a Credit Support Instrument, moneys on deposit in the Parity Obligation Payment Fund, and any such amounts transferred by the District from the Parity Obligation Payment Fund to the Trustee or other third party payee for such Parity Obligation pursuant to the Maser Contract, shall be paid to the applicable Credit Provider as a Credit Support Reimbursement Obligation for the amounts so paid.

Third, after the payments described in the prior three paragraphs have been made, any amounts thereafter remaining in the Revenue Fund shall be used for the payment of the interest and principal payments becoming due and payable under all Subordinate Obligations and the net payments becoming due and payable on all Subordinate Payment Agreements (except any Termination Payments) and any other amounts becoming due and payable with respect to Subordinate Obligations (including any letter of credit and remarketing fees and any other amounts becoming due and payable to make up any deficiency in the Reserve Funds for Subordinate Obligations, including all Reserve Fund Credit Facility Costs, or any Credit Support Reimbursement Obligations with respect to Subordinate Obligations) and any Termination Payments on Parity Payment Agreements; so long as the following conditions are met: (1) all Maintenance and Operations Costs are being and have been paid and are then current; and (2) all deposits and payments contemplated by the prior three paragraphs have been made in full and no deficiency in any Reserve Fund for Parity Obligations shall exist and no Reserve Fund Credit Facility Costs or Credit Support Reimbursement Obligations with respect to Parity Obligations shall be due and payable, and there shall have been paid, or segregated within the Revenue Fund, the amounts currently payable pursuant to the prior two paragraphs.

Fourth, after deposits contemplated by the prior four paragraphs have been made, any amounts thereafter remaining in the Revenue Fund may be used for any lawful purpose, including, but not limited to (i) the payment of any Termination Payments on Subordinate Payment Agreements or (ii) transfer to the Rate Stabilization Account.

Rate Covenant. Under the Master Contract, the District has covenanted to fix, prescribe and collect rates, fees and charges for the Service of the Enterprise during each Fiscal Year which are reasonably fair and non-discriminatory and which are estimated to yield Adjusted Annual Net Revenues and Net Revenues, for such Fiscal Year in an amount not less than the Coverage Requirement for such Fiscal Year. The District may make adjustments from time to time in such fees and charges and may make such classification thereof as it deems necessary, but has covenanted under the Master Contract not to reduce rates, fees and charges then in

effect, unless the Adjusted Annual Net Revenues from such reduced rates, fees and charges are estimated to be sufficient to meet the requirements of the Rate Covenant.

“Adjusted Annual Net Revenues” means, for any Fiscal Year or twelve (12) calendar month period, the Adjusted Annual Revenues during such Fiscal Year or twelve (12) calendar month period minus the Maintenance and Operation Costs during such Fiscal Year or twelve (12) calendar month period; and “Adjusted Annual Revenues” means, for any Fiscal Year or twelve (12) calendar month period, the Revenues during such Fiscal Year or twelve (12) calendar month period plus the withdrawals from the Rate Stabilization Account in such Fiscal Year or twelve (12) calendar month period minus the deposits into the Rate Stabilization Account in such Fiscal Year or twelve (12) calendar month period, as set forth in a Certificate of the District.

“Coverage Requirement” means, for any Fiscal Year or twelve (12) calendar month period, (i) an amount of Adjusted Annual Net Revenues which equals at least one hundred fifteen percent (115%) of the Adjusted Annual Debt Service for such Fiscal Year or twelve (12) calendar month period, and (ii) an amount of Net Revenues which equals one hundred per cent (100%) of all Payments and all other amounts which are payable from Net Revenues payable in such Fiscal Year or twelve (12) calendar month period; provided, that, for purposes of determining compliance with the Coverage Requirement, it shall be assumed that all Obligations accrue interest at the applicable Assumed Interest Rate. See Appendix B — “DEFINITIONS AND SUMMARY OF PRINCIPAL LEGAL DOCUMENTS and see “BONDOWNERS’ RISKS — Issuance of Senior Obligations” for a discussion of the legal ability of the District to designate certain obligations as Maintenance and Operation Costs, and how such designation may reduce the level of coverage otherwise required.

The opinion of Bond Counsel proposed to be delivered in connection with fixing of the interest rates applicable to the 2015 Bonds (a copy of the proposed form of which is set forth in Appendix C) points out that, “... the imposition of fees and charges by the District relating to the Enterprise may be subject to the provisions of Article XIIC and XIID of the California Constitution.” See “CONSTITUTIONAL LIMITATIONS ON APPROPRIATIONS AND CHARGES — Proposition 218” and “— Effect of Proposition 218 and of Possible General Limitations on Enforcement Remedies.”

Additional Parity Obligations. Under the terms of the Master Contract the District may at any time incur Parity Obligations payable as provided in the Master Contract; provided:

There shall be on file with the District either:

(1) A Certificate of the District demonstrating that, during the last audited Fiscal Year or any consecutive twelve (12) calendar month period during the immediately preceding eighteen (18) calendar month period, the Adjusted Annual Net Revenues were at least equal to 115% of Maximum Annual Debt Service on all Outstanding Parity Obligations plus the Parity Obligations proposed to be issued or executed; provided, that for the purpose of providing such Certificate, the District may adjust the foregoing Adjusted Annual Net Revenues to reflect:

(a) An allowance for Net Revenues that would have resulted from any increase or decrease in the rates, fees and charges fixed and prescribed for Service which, during any part of such Fiscal Year or twelve (12) calendar month period, was not in effect, in an amount equal to the estimated change in Net Revenues that would have resulted from such increase or decrease in rates, fees and charges if it had been in effect for the entire Fiscal Year or twelve (12) calendar month period; and

(b) An allowance for Net Revenues that would have been derived from each new use or user of the Enterprise that, during any part of such Fiscal Year or twelve (12) calendar month period, was not in existence, in an amount equal to the estimated additional Net Revenues that would have

been derived from each such new use or user if it had been in existence for the entire Fiscal Year or twelve (12) calendar month period, or

(2) An Engineer's Report that the estimated Adjusted Annual Net Revenues for each of the five (5) Fiscal Years next following the earlier of (i) the end of the period during which interest on the Parity Obligations proposed to be executed is to be capitalized or, if no interest is capitalized, the Fiscal Year in which the Parity Obligations proposed to be executed is executed, or (ii) the date on which substantially all Projects financed with the Parity Obligations proposed to be executed are expected to commence operations, will be at least equal to 115% of the Maximum Annual Debt Service for such period; provided, that for the purpose of providing this Engineer's Report, the Independent Engineer may adjust the foregoing estimated Adjusted Annual Net Revenues to reflect:

(a) An allowance for Net Revenues that are estimated to result from any increase or decrease in the rates, fees and charges for Service in effect and being charged or from any increase or decrease in the rates, fees and charges for Service that are expected to be charged; and

(b) An allowance for Net Revenues that are estimated to be derived from additional uses or users of the Enterprise anticipated to be served by the additions, betterments or improvements to the Enterprise to be financed by the Parity Obligations proposed to be executed together with any additional Supplemental Contracts expected to be executed and entered into during such five (5)-year period.

See "BONDOWNERS' RISKS — Issuance of Senior Obligations" for a discussion of the ability of the District to incur obligations payable prior to the 2015 Bonds.

Without regard to foregoing, the District may, at any time and from time to time, enter into Credit Support Agreements or otherwise become obligated for Credit Provider Reimbursement Obligations with respect to Parity Obligations.

Notwithstanding the foregoing provisions, there shall be no limitations on the ability of the District to execute any Parity Obligations at any time to refund any outstanding Parity Obligations so long as the Annual Debt Service payable by the District for each Fiscal Year with respect to such refunding Parity Obligations is less than or equal to 105% of the Annual Debt Service for each corresponding Fiscal Year for such Parity Obligations being refunded.

Reserve Fund. No Reserve Fund has been created under the Master Contract or the Indenture for the benefit of the 2015 Bonds.

Rate Stabilization Account. The Master Contract permits the District to establish and maintain an account designated the "Vallecitos Water District Rate Stabilization Account." The District has not currently established a Rate Stabilization Account as contemplated under the Master Contract. The District may, at any time, as determined by the District, deposit in the Rate Stabilization Account any Revenues (subject to provisions described under the caption "-Application of Revenues") and any other money received and available to be used therefor, and the District may at any time withdraw any or all of the money from the Rate Stabilization Account for inclusion in Adjusted Annual Revenues; provided, that any such withdrawal may be made up to and including the date one hundred and eighty (180) days after the end of the Fiscal Year for which the withdrawal will be included as Adjusted Annual Revenues.

ESTIMATED SOURCES AND USES OF FUNDS

The following table sets forth the estimated sources and uses of funds with respect to the prepayment of the 2005 Installment Payments and the Refunded 2005A COPs:

Sources⁽¹⁾:	
Principal Amount of 2015 Bonds	\$45,315,000
Original Issue Premium	7,299,390
District Contribution ⁽²⁾	<u>53,538</u>
Total Sources	<u><u>\$52,667,927</u></u>
Uses⁽¹⁾:	
Transfer to Escrow Agent for Prepayment of 2005 Installment Payments and Refunded 2005A COPs	\$ 52,390,214
Deposit to Costs of Issuance Fund ⁽³⁾	<u>277,713</u>
Total Uses	<u><u>\$ 52,667,927</u></u>

-
- (1) All amounts rounded to the nearest dollar. Totals may not add due to rounding.
 - (2) Reflects interest accrued with respect to the Refunded 2005A COPs from July 1, 2015 through the Issuance Date of the 2015 Bonds.
 - (3) Includes Underwriter’s discount and certain legal fees, financing and printing costs.

THE DISTRICT

General

The District was formed on March 21, 1955, pursuant to the County Water District Law (Division 12, commencing at Section 30000, of the Water Code of the State of California). It was originally named the San Marcos County Water District, but its name was changed to the Vallecitos Water District in 1989.

The District includes an area of approximately 45 square miles in the northwestern part of San Diego County. It is located about ten miles east of the Pacific Ocean, 30 miles north of San Diego and 100 miles south of Los Angeles. It currently provides water, wastewater and water reclamation services to nearly all of the City of San Marcos, portions of the cities of Escondido and Carlsbad, and unincorporated areas of San Diego County north and south of the City of San Marcos including the community of Lake San Marcos. The District’s population is approximately 97,000, and the San Diego Association of Governments Series 13 Regional Growth Forecast projects that the District’s population will grow to over 111,000 by the year 2020. Land uses in the District include commercial, industrial and residential development, as well as agricultural activities.

The District is a member of the San Diego County Water Authority (“SDCWA”), the regional wholesaler of water from which the District purchases substantially all of the water served through its water system. SDCWA is a member of The Metropolitan Water District of Southern California (“MWD”) from which SDCWA currently purchases a substantial portion of the water that SDCWA sells to the District.

Governance and Management

The District is governed by a five member Board of Directors (the “Board”) who are elected by the registered voters in the District to staggered four year terms. The current directors, their occupations and the expiration dates of their terms are set forth below.

<i>Director</i>	<i>Expiration of Term (December)</i>	<i>Occupation</i>
Betty Evans, President	2016	Former Councilmember/Retired Educator
Mike Sannella, Vice President	2016	General Atomics
Jim Hernandez	2018	Architect
Craig Elitharp	2018	Part Time Senior Engineer
Hal Martin	2016	Development Director

Day to day management of the District is delegated to the General Manager. Set forth below are brief resumes of the General Manager and other key management personnel of the District.

General Manager. Mr. Dennis Lamb joined the District in July 1982 as a draftsman and has over 30 years of experience with the District including Engineering Manager, Director of Engineering/Operations and Deputy General Manager. Mr. Lamb has been the General Manager since January 2010. Mr. Lamb has overall responsibility for policy development; water resources planning and distribution; wastewater collection, treatment, disposal, and reclamation; fiscal management; administration, and operation of all District functions, program, and activities. Mr. Lamb is responsible for accomplishing District goals and objectives and for implementing the policies of the Board. Mr. Lamb has served as a Board Member of the San Diego County Water Authority from 2011 to 2012.

Assistant General Manager. Mr. Tom Scaglione has been the Assistant General Manager for the District since March 2012. Mr. Scaglione is responsible for planning and directing the District's financial activities and acts as the General Manager in the General Manager's absence. Prior to joining the District in September 2000, Mr. Scaglione worked in public accounting providing audit, tax, and consulting services. He has been teaching Accounting, mostly at Palomar College, for over 20 years and now teaches Finance for the Water Industry at Cal State University, San Marcos. Mr. Scaglione has a Master's Degree in Business Administration with an emphasis in Government Leadership from Cal State University, San Marcos and is a Certified Public Accountant.

Director of Engineering and Operations. Mr. Ken Gerdes joined the District in March 1998 as the Capital Facilities/Construction Engineer, and became the Director of Engineering and Operations in 1998. Mr. Gerdes provides oversight and direction for the general planning and supervision of engineering, construction, operation and maintenance related to District water, wastewater, and reclamation services and facilities. Mr. Gerdes has over 40 years of experience in civil engineering and public utilities. Prior to joining the District, Mr. Gerdes served as the City Engineer for the City of San Marcos, California, and as an engineering consultant to a number of Midwest municipalities. Mr. Gerdes has a Master's Degree in Business Administration from St. Ambrose University, Davenport, Iowa, and a Bachelor of Science in Civil Engineering from the University of Iowa. He is registered as a Professional Engineer in California, Iowa and Illinois, and is licensed as a Professional Land Surveyor in California.

Administrative Services Manager. Mrs. Rhondi Emmanuel joined the District as its Administrative Services Manager in April 2012. She is responsible for overseeing and managing human resources, risk management, safety, worker's compensation, information technology, public information, water conservation, and District-wide administrative support, as well as developing and implementing policies and procedures. Mrs. Emmanuel has more than 15 years of experience in human resources and general administration. Prior to joining the District, Mrs. Emmanuel served as the Human Resources Services Manager for the County of San Diego. Mrs. Emmanuel holds a Master of Arts Degree in Human Resources Management from National University, San Diego and is an International Public Management Association Certified Professional.

Finance Manager. Mr. John Fusco, MSCIS CPA, joined the District in June 2005 as the Accounting Supervisor and is responsible for overseeing and managing the Accounting; Meter Reading; Purchasing/Warehouse and Customer Service departments as well as the District's investment portfolio. Mr. Fusco holds a BS in Accounting from California State University San Marcos and Master of Science in

Computer Information Systems from University of Phoenix. Mr. Fusco became a Certified Public Accountant in California in 1999 and maintains an active status license. Mr. Fusco also serves as an Adjunct Professor of Accounting at San Diego Mesa College teaching three levels of accounting since 2003.

Operations and Maintenance Manager. Mr. Ed Pedrazzi joined the District in November 1989. Mr. Pedrazzi manages the District's water and wastewater operations and maintenance, wastewater treatment plant, landscape maintenance, mechanical/electrical repairs and maintenance, vehicle maintenance shop, and construction; formulates and implements operating policies and procedures within general administrative guidelines and develops the department's budget.

District Engineer. Mr. James Gumpel became the District Engineer in 2014, and has been with the District since 2005. Mr. Gumpel is a licensed Professional Engineer with nearly 20 years of experience in water and wastewater industry providing engineering, project management, operational support, and planning for wastewater/water projects. In addition to his management and leadership responsibilities, he oversees all aspects of the Capital Facility, Development Services, Inspections, and GIS departments, which is responsible for planning, design, mapping, inspection and construction of the District's infrastructure. Some key projects include the upgrade and redesign of the District's water reclamation facility, successfully doubling the output capacity from 2.25 to 5.0 million gallons per day. Mr. Gumpel was also the project manager for the Twin Oaks Reservoir Tank No.2, a 40-million gallon underground water storage facility, regarded as the largest in the world. Both projects were awarded Project of the Year honors from the WateReuse Association and the American Society of Civil Engineers. Mr. Gumpel has been involved in a variety of professional and industry associations, having served as the both the President of the San Diego Younger Member Forum of Civil Engineers, the Director and board member of ASCE, the president of the Pipeline and Environmental Technical Group of ASCE, and is a member of the APWA American Public Works Association and the Construction Management Association of America. He holds a Bachelor of Science in Civil/Environmental Engineering from San Diego State University.

Powers

Under the County Water District Law, the District has broad general powers over the use of water within its boundaries, including the right of eminent domain and the authority to acquire, control, distribute, store, treat, reclaim and recapture any water for beneficial use, to acquire, construct and operate facilities for the collection, treatment, and disposal of sewage, waste and storm water, and to sell potable or non-potable water.

Employees and Employee Benefits

Employees. The District generally employs 116 persons, of whom approximately 72 work in the operations and engineering departments and approximately 44 work in finance or administration. All of the District's employees are presently members of a single employee association with which the District meets and confers concerning salary, benefits and other employment matters. The District has not experienced any strike or other labor actions and is currently in the second year of a three-year agreement with the employees' association (its seventh consecutive multi-year agreement).

Retirement Plan Description. The District provides retirement benefits to employees through the California Public Employees Retirement System ("PERS"), a cost sharing multi-employer defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. PERS 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 District. Copies of PERS annual financial report may be obtained from their executive office: 400 P Street, Sacramento, CA, 95814.

Plan Member Contributions. The contribution rate for plan members in the PERS 3.0% at 60 Risk Pool Retirement Plan is 8% of their annual covered salary. For employees hired before January 1, 2013, the District pays half of the 8% contributions. For employees that are “new members” of the PERS hired after January 1, 2013, under the California Employee’s Pension Reform Act (“PEPRA”) provisions, the contribution rate for plan members in the PERS 2.0% at 62 Risk Pool Retirement Plan is 6.25% of their annual covered salary. The District is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the PERS Board of Administration.

Employer Contributions. The required employer contribution rate for the PERS 3% at 60 Risk Pool for the fiscal year ending June 30, 2016 is 11.718% plus an employer payment of unfunded liability of \$550,027. The required employer contribution rate for the PERS 3% at 60 Risk Pool for the fiscal year ending June 30, 2016 is 6.237%. The District is required to contribute the actuarially determined remaining amounts necessary to fund the 3.0% at 60 Risk Pool Retirement Plan benefits for its classic members and 2.0% at 62 Risk Pool Retirement Plan for its new members (employees hired after December 31, 2012) under the PEPRA provisions. The contribution requirements are established by State statute and the employer contribution rate is established and may be amended by the PERS.

Annual Pension Costs. For the fiscal year ending June 30, 2015, the District’s annual pension cost and actual contribution was \$1,197,373. The required contribution for the fiscal year ending June 30, 2015 was determined as part of the June, 30 2013 actuarial valuation. The actuarial assumptions included (a) 7.5% investment rate of return (net of administrative expenses); (b) projected salary increases that vary by duration of service ranging from 3.30% to 14.20%, and (c) 3.00% payroll growth. Both (a) and (b) include an inflation component of 2.75%.

Initial unfunded liabilities are amortized over a closed period that depends on the plan’s date of entry into PERS. Subsequent plan amendments are amortized as a level percentage of pay over a closed 20-year period. Gains and losses that occur in the operation of the plan are amortized over a rolling period, which results in an amortization of 6% of unamortized gains and losses each year. If the plan’s accrued liability exceeds the actuarial value of the plan assets, then the amortization payment of the total unfunded liability may be lower than the payment calculated over a 30-year amortization period.

<i>Fiscal Year</i>	<i>APC</i>	<i>Percentage of APC Contributed</i>	<i>Net Pension Obligation</i>
June 30, 2012	\$1,045,353	100%	-
June 30, 2013	1,064,666	100	-
June 30, 2014	1,184,618	100	-

Funding Status. As of June 30, 2004, the District’s miscellaneous plan became part of a PERS Risk Pool for employers with less than 100 active plan members. As part of a cost-sharing multiple-employer defined benefit plan, disclosure of the schedule of funding progress is not required as information is not specific to the District. See APPENDIX A—“VALLECITOS WATER DISTRICT FINANCIAL STATEMENTS.”

AB 340. Contributions for participants hired on or after January 1, 2013 who were not already enrolled in PERS through their previous employers are governed by Assembly Bill 340 (“AB 340”), which is described below.

On September 12, 2012, the State Governor signed AB 340, which implements pension reform in the State. Effective January 1, 2013, AB 340, among other things: (i) requires public retirement systems and their participating employers to share equally with employees the normal cost rate for such retirement systems; (ii) prohibits employers from paying any portion of the required member contributions to such retirement systems for employees hired after January 1, 2013 who are new PERS members (those who were not already enrolled

in a public retirement system through their previous employers or who moved between employers or public retirement systems with a 6 month break in service) (“New Members”); (iii) establishes a compulsory maximum non safety benefit formula of 2.5% at age 67; and (iv) defines final compensation as the highest average annual pensionable compensation earned during a 36 month period.

Due to significant market investment losses of approximately 24% in the PERS trust fund for fiscal year 2009, PERS implemented a 3-year phase-in of the fiscal year 2009 investment loss. This phased in approach will be achieved by temporarily relaxing the constraints on the smoothed value of assets around the actual market value. The corridor will be widened and then contracted as follows:

- Increase the corridor limits from 80% to 120% of market value to 60% to 140% of market value to determine the actuarial value of assets for the June 30, 2009 valuation, which impacts the fiscal year 2012 contribution rate.
- Reduce the corridor limits from 60% to 140% of market value to 70% to 130% of market value to determine the actuarial value of assets for the June 30, 2010 valuation, which impacts the fiscal year 2013 contribution rate.
- Return to the 80% to 120% of market value corridor limits for the actuarial value of assets on June 30, 2011 and thereafter, which impacts contribution rates for fiscal year 2014 and beyond.
- Asset losses outside of the 80% to 120% corridor described above will be amortized pursuant to a fixed 30-year amortization schedule.

In addition, in February 2010, the PERS Board adopted a resolution requiring additional contributions for any plan or pool if the cash flows hamper adequate funding progress by preventing the expected funded status on a market value of assets basis of the plan to either:

- Increase by at least 15% by June 30, 2043; or
- Reach a level of 75% funded by June 30, 2043.

Such contributions have been factored into the District’s contribution rates set by PERS.

On April 17, 2013, the PERS Board of Administration approved a plan: (i) to replace the current 15-year asset-smoothing policy with a 5-year direct-rate smoothing process; and (ii) to replace the current 30-year rolling amortization of unfunded liabilities with a 30-year fixed amortization period. PERS’ Chief Actuary has stated that the revised approach provides a single measure of funded status and unfunded liabilities, less volatility in extreme years, a faster path to full funding and more transparency to employers such as the District about future contribution rates. These changes are expected to accelerate the repayment of unfunded liabilities (including PERS’ Fiscal Year 2008-09 market losses described above) of the District’s plans in the near term; the exact magnitude of the potential contribution rate increases is not known at this time, but may be significant. These changes will be reflected beginning with the June 30, 2014 actuarial valuation affecting contribution rates for Fiscal Year 2016 and thereafter.

For additional information with respect to the District and PERS, see Note 10 of APPENDIX A—“VALLECITOS WATER DISTRICT FINANCIAL STATEMENTS.”

Other Post-Employment Benefits

The District provides post-employment health benefits in accordance with a resolution approved by the District’s Board of Directors, to all employees who retire from the District under the retirement criteria established by PERS, up to age 65. As of June 30, 2014, there were twenty-nine retired employees who met

these eligibility requirements and are therefore receiving the benefits. The Governmental Accounting Standards Board's Statement No. 45 ("GASB 45") requires governmental agencies that fund post-employment benefits on a pay as-you go basis, such as the District, to account for and report the outstanding obligations and commitments related to such post-employment benefits in essentially the same manner as for pensions. The total expense incurred for these benefits for retired employees for the fiscal year ended June 30, 2014 was \$357,639, and for the fiscal year ended June 30, 2013, was \$385,258.

Plan Description. The District administers the Other Post-Employment Benefit Plan ("OPEB"), a multi-employer defined benefit plan. For employees who retired before July 1, 2013, the District's 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. For employees who retire after June 30, 2013, the District's OPEB provides continued medical coverage for an eligible retired employee and spouse or registered domestic partner until they become entitled to Medicare benefits at age 65. Medical premiums paid by the District are established per the most current Memorandum of Understanding ("MOU"). Plan premiums elected by the retiree above those established in the MOU are paid by the retiree.

To become eligible for partial OPEB benefits, non-retired employees hired before July 1, 2013, must be age 50 and have five years of continuous service with the District. OPEB benefits increase with each year of continuous service up to ten years when the employee becomes 100% vested to receive the maximum amount of premium established in the most current MOU at retirement.

OPEB benefit is not offered to employees hired after July 1, 2013.

Eligible retirees may enroll in any of the plans the District offers through the Association of California Water Agencies ("ACWA") Program. The activity and liability from the OPEB plan are included in these financial statements.

Funding Policy. The District's Resolution No. 788, established the authority for the plan and provides that the District will pay 100% of the cost of the OPEB plan to employees who retired prior to July 1, 2013, and a percentage of the basic medical premiums for employees hired prior to July 1, 2013 and who retire after July 1, 2013. Resolution No. 1389 authorized the District to establish and maintain an irrevocable trust to fund OPEB and seek reimbursement from the trust to cover current retiree benefit premiums which are paid by the District on a pay-as-you-go basis. The District began funding the trust in March of 2012.

Annual OPEB Cost. The following table shows the components of the District's annual OPEB cost, the amount actually contributed to the plan, and the changes in the District's net OPEB obligation for the fiscal years ended June 30th, 2014 and June 30th, 2013, as follows:

	<i>2014</i>	<i>2013</i>
Annual required contribution	\$ 387,648	\$ 435,652
Interest on net post employment benefits payable obligation	-	-
Adjustment to annual required contribution	-	-
Annual post employment benefits payable obligation cost (expense)	<u>387,648</u>	<u>435,652</u>
Contributions made:		
Retired employees post employment medical benefits payments	(375,729)	(437,904)
Increase (decrease) in net post employment benefits payable obligation	11,919	(2,252)
Post employment benefits payable, net - beginning of year	<u>18,090</u>	<u>20,342</u>
Post employment benefits payable, net - end of year	<u>\$ 30,009</u>	<u>\$ 18,090</u>

Funding Status. The most recent valuation (dated January 1, 2013) includes an Actuarial Accrued Liability of \$4,707,625 and an Unfunded Actuarial Accrued Liability of \$1,896,023. The covered payroll (annual payroll of active employees covered by the plan) for the year ended June 30, 2014 is \$7,445,301. The ratio of the Unfunded Actuarial Accrued Liability to annual payroll covered is 25.47%. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for the benefits.

<i>Fiscal Year</i>	<i>Annual OPEB Costs</i>	<i>Percentage of Annual OPEB Cost Contributed</i>	<i>Net OPEB Obligation</i>
June 30, 2012	\$595,722	486.98%	\$20,342
June 30, 2013	435,652	100.52	18,090
June 30, 2014	387,648	96.93	30,009

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 6.75% discount rate. The high rate of annual health care cost increases experienced in recent years is assumed to gradually decrease by 16.3% in 2014 and 10.0% in 2015. A level dollar amortization of the Unfunded Actuarial Accrued Liability is used over a closed 30-year period.

For additional information with respect to the District and the OPEB, see Note 11 of APPENDIX A—“VALLECITOS WATER DISTRICT FINANCIAL STATEMENTS.”

Budget Process

The General Manager of the District submits to the Board for its consideration a proposed budget for each Fiscal Year. The proposed budget is reviewed by the applicable committees of the Board which make recommendations to the full Board. The Board is ultimately responsible for the adoption of the budget. The Fiscal Year 2016 Budget is expected to be submitted to the District Board of Directors for consideration and approval in June 2015.

The District's budget is prepared on a modified accrual basis. For budgeting purposes, the District generally sets user charges to cover operating expenses of the particular services, including water purchases

and uses revenue from the Capital Facility Fees to finance capital projects that accommodate growth. See Appendix A — “VALLECITOS WATER DISTRICT FINANCIAL STATEMENTS.”

Insurance

On June 30, 2014 the District participated in the self-insurance program of the Association of California Water Agencies Joint Powers Insurance Authority (the “JPIA”) for insurance coverage as follows:

Property Loss – Insured up to \$100 million per occurrence with \$10,000 deductible per occurrence. Property loss is paid at the replacement cost for property on file, if replaced within two years after the loss, or otherwise paid on an actual cash value basis. The total risk financed self-insurance limits is \$50,000 with additional insurance purchased with coverage limits of \$100 million.

Boiler and Machinery Coverage – Insured for the replacement cost up to \$100 million per occurrence, subject to various deductibles depending on the type of equipment.

Employee Dishonesty – Insured up to \$100,000 per loss, including public employee dishonesty, forgery or alteration and theft, disappearance and destruction coverage.

General and Auto Liability, Public Officials and Employees’ Errors and Omissions – Insured with a total risk financed self-insurance limit of \$2 million and a combined single limit at \$1 million per occurrence. The District purchased additional excess coverage layers in the amount of \$58 million for general, auto and public officials liability, which increases the limits on the insurance coverage noted above.

Workers’ Compensation – Insured up to the statutory limits for all work related injuries/illnesses covered by California law, with total risk financed self-insurance limits of \$2 million.

The District pays the annual premiums for these coverages. They are subject to retrospective adjustments based on claims experience. The nature and amounts of these adjustments cannot be estimated and are charged to expense as invoiced. The District’s insurance expense for the Fiscal Years ended June 30, 2014 and 2015 was \$595,956 and \$476,035 (unaudited), respectively. There were no instances in the past three Fiscal Years where a settlement exceeded the District’s coverage.

Outstanding District Obligations

Outstanding Obligations Payable From Net Revenues On A Parity With The 2015 Bonds. After delivery of the 2015 Bonds, the District will have outstanding obligations payable from Net Revenues on a parity with the 2015 Bonds as described below.

The District is obligated to make the 2005 Installment Payments under the Master Contract, which is currently outstanding in the aggregate principal amount of \$53,775,000. After refunding the Refunded 2005A COPs, the 2005 Contract will be outstanding in the aggregate principal amount of \$3,720,000, which outstanding principal amount represents the 2005A COPs maturing on July 1, 2015 through 2017, inclusive. See the caption “REFUNDING PLAN.” The obligation of the District to make approximately \$3,720,000 aggregate principal amount of payments outstanding under the Master Contract remaining with respect to the 2005A COPs maturing July 1, 2015 through July 1, 2017, inclusive, after the refunding is payable on a parity with the obligation of the District to pay the 2015 Bonds.

In addition, in 2012, the District entered into an Installment Purchase Contract (the “2012 Installment Purchase Contract”) with the Corporation, pursuant to which the District has agreed to make installment payments (the “2012 Installment Payments”) to the Corporation, secured by Net Revenues. The 2012 Installment Purchase Contract is currently outstanding in the aggregate principal amount of \$5,795,000 with a final maturity in Fiscal Year 2023.

Other Outstanding Obligations. In 2008, the District entered into a Loan Agreement with Union Bank of California (the “UBOC Loan Agreement”) in a maximum amount of \$8,000,000, evidenced by a negotiable promissory note (the “UBOC Note”), pursuant to which the District promises to pay to UBOC the amounts owed under the UBOC Loan Agreement. There is currently outstanding on the UBOC Note \$5,400,000. The UBOC Note is payable from Net Revenues subordinate to the 2012 Installment Purchase Contract and the 2015 Bonds.

THE ENTERPRISE

Water System

Water System Facilities. The District has 4 interconnections with the SDCWA’s water system. The District provides water service to its customers through its Water System facilities. The District owns, operates and maintains, 19 reservoirs with a total of 121.5 million gallons of capacity, including the Twin Oaks Reservoirs No. 1 and No 2, with capacities of 33 million gallons and 40 million gallons, respectively. The District also owns, operates and maintains 9 pump stations, and delivers water through 356 miles of pipelines ranging in size from 2” to 48”.

Service Area. The District is the sole provider of water service for residential, commercial, industrial and agricultural users within the District. The District’s current population is estimated to be over 97,000 people. As of June 30, 2015, the Water System is estimated to include a total of approximately 21,358 active metered connections, including approximately 19,332 residential service connections, approximately 154 agricultural service connections, approximately 926 industrial and commercial service connections, and approximately 809 irrigation service connections. The following table illustrates use of the Water System in Fiscal Year 2015.

**Table No. 1
VALLECITOS WATER DISTRICT WATER SYSTEM
WATER USE BY TYPE
(Fiscal Year 2015)⁽¹⁾**

<i>Types of Uses</i>	<i>Percentage of Total</i>
Residential	65.0%
Landscape Irrigation	13.7
Commercial/Industrial	10.1
Agricultural	8.6
Public, Other	<u>2.6</u>
TOTAL	100%

⁽¹⁾ Actual unaudited results through March 31, 2015, and projected results through June 30, 2015.
Source: District

Water Sources and Supply. The District obtains its water supply through and as a member of SDCWA. SDCWA currently obtains its water supply from MWD and, to a limited extent from the Imperial Irrigation District (“IID”). In 2016, SDCWA and the District will begin accepting deliveries of desalinated water from Poseidon Resources Limited pursuant to purchase contracts. The District’s direct connection to the Carlsbad Desalter will supply 3,500 acre feet of desalinated water per year into the District’s distribution system, as described below. Depending upon availability, the District may obtain an additional 583 acre-feet, in the event that additional desalinated water is available. Beginning in Fiscal Year ending 2016, the District will also purchase treated water from the Olivenhain Municipal Water District (“Olivenhain”).

SDCWA was formed in 1944 under the County Water Authority Act for the purpose of transporting Colorado River Water to supplement the local water supply of its members. Its water supply now also

includes water obtained from the State Water Project through MWD as well as water purchased from the IID pursuant to a water transfer agreement between SDCWA and IID. Under the terms of that agreement with IID, 10,000 acre-feet of water was conveyed to SDCWA in 2003, and the amount of the annual transfer ramps up to 200,000 acre-feet in 2022. The agreement has an initial term of 45 years and a renewal term of 30 years.

SDCWA built its first aqueduct in 1947 and completed its second one which runs directly through the District, in 1959. The District has four connections to the SDCWA aqueduct.

MWD is a public corporation organized in 1928 under the authority of the Metropolitan Water District Act. It delivers a blend of local water, Colorado River water and State Water Project water to its members, including SDCWA.

On December 20, 2012, the SDCWA entered into the Carlsbad Seawater Desalination Project Water Purchase Agreement (the “Poseidon WPA”) and the and Design Build Agreement for Product Water Pipeline Improvements Relating to the Carlsbad Seawater Desalination Project with Poseidon Resources (Channelside) LP (the “Poseidon DBA” and collectively the “Poseidon Agreements”). The Poseidon Agreements provide new facilities for production and conveyance of desalinated water to the SDCWA (the “Carlsbad Desalter”). Under the Poseidon WPA, the SDCWA committed to purchase, take delivery of, and pay for 48,000 acre-feet of water, depending upon availability. In June of 2011, the SDCWA adopted guiding principles to make up to 49% of such 48,000 acre-feet commitment available to its member agencies pursuant to uniform contracts providing for firm commitments to individually purchase designated amounts from the SDCWA.

In April of 2015, the District’s Board of Directors authorized entering into the Uniform Contract for Member Agency Purchase of Treated Water from the San Diego County Water Authority – Carlsbad Desalination Project (the “Uniform Contract”). The Uniform Contract is for a term of the lesser of 30 years following commercial operation of the Carlsbad Desalter, or the termination of the Poseidon WPA. Pursuant to the Carlsbad Desalination Project Contract, the District has committed to purchase 3,500 acre feet of water per year under the Uniform Contract, subject to certain adjustments as provided therein. The District may obtain up to 583 additional acre feet depending upon availability.

The per-acre-foot charge for Desalinated Water will be calculated pursuant to the Uniform Contract and the Poseidon WPA. Such charges will be determined in an amount sufficient to pay the District’s proportional share of variable and fixed operating costs, including certain costs relating to financing the Carlsbad Desalter, consumable inputs, such as energy and chemicals, labor at the Carlsbad Desalter, oversight, and transportation costs for treated water. Costs associated with the project, including replacement chemicals and labor, are indexed to inflation.

MWD and SDCWA face various challenges in continuing to supply imported water to their respective member agencies including, but not limited to, an extended drought being experienced throughout the southwestern portion of the country as well as environmental considerations and litigation filed from time to time which, if determined adversely, could disrupt the supply of imported water available through them.

A description of various challenges facing MWD as well a variety of other operating information with respect to MWD is included in certain disclosure documents prepared by MWD; and a description of the challenges facing SDCWA together with operating information with respect to SDCWA is included in certain disclosure documents prepared by SDCWA. MWD and SDCWA have each entered into certain continuing disclosure agreements pursuant to which each of them is contractually obligated for the benefit of owners of certain of its outstanding obligations, to file with certain information repositories annual reports, notices of certain material events as defined under Rule 15c2-12 of the Exchange Act (“Rule 15c2-12”) and annual audited financial statements (the “MWD Information” or the “SDCWA Information,” as applicable). MWD’s and SDCWA’s disclosure documents and annual reports should be reviewed for information pertaining to water supply matters. MWD AND SDCWA HAVE NOT ENTERED INTO ANY CONTRACTUAL COMMITMENT WITH THE DISTRICT, THE TRUSTEE OR THE OWNERS OF THE 2015 BONDS TO

PROVIDE MWD INFORMATION OR SDCWA INFORMATION, AS THE CASE MAY BE, TO THE DISTRICT OR THE OWNERS OF THE 2015 BONDS.

NEITHER MWD NOR SDCWA HAS REVIEWED THIS OFFICIAL STATEMENT OR MADE ANY REPRESENTATIONS OR WARRANTIES WITH RESPECT TO THE ACCURACY OR COMPLETENESS OF THE INFORMATION CONTAINED OR INCORPORATED HEREIN, INCLUDING INFORMATION WITH REGARD TO MWD OR SDCWA. NEITHER OF THEM HAS UNDERTAKEN TO UPDATE SUCH INFORMATION FOR THE BENEFIT OF THE DISTRICT OR THE OWNERS OF THE 2015 BONDS UNDER RULE 15c2-12.

California Drought and Response

Governor's Executive Orders. On April 1, 2015, Governor Jerry Brown (the "Governor") issued Executive Order B-29-15 (the "2015 Executive Order") to address the ongoing drought conditions in California. The 2015 Executive Order, among other things, directed the State Water Resources Control Board ("SWRCB") to impose restrictions to achieve a statewide 25% reduction in potable urban water usage from 2013 levels through February 28, 2016. The 2015 Executive Order further directs the SWRCB to impose restrictions to require that commercial, industrial and institutional properties, such as campuses, golf courses and cemeteries, immediately implement water efficiency measures to reduce potable water usage, and calls upon the SWRCB to direct urban water suppliers to develop rate structures and other pricing mechanisms, including but not limited to surcharges, fees and penalties, to maximize water conservation consistent with statewide water restrictions. The 2015 Executive Order includes several provisions to increase enforcement activity against water waste and to streamline the State and local response to drought-related initiatives.

On May 5, 2015, following a formal rulemaking process and public comment period, the SWRCB adopted an emergency regulation to implement the 2015 Executive Order. The regulation will become effective immediately upon approval by the Office of Administrative Law, which is anticipated on or about May 15, 2015, and will remain in effect for 270 days from such date. Under the regulation, 411 urban water providers in the State are classified into nine tiers and assigned a required conservation standard which is imposed on each tier. The tier classifications are based upon a water supplier's per capita water usage in the three month period July to September 2014. The conservation standard applied to the tiers ranges from a 4% reduction in total potable water production (although no water providers were proposed to be classified in such tier absent the demonstration by a water provider of satisfaction of certain specified criteria) to a 36% reduction in total potable water production from 2013 levels. As adopted, the regulation requires areas with high per capita water usage to achieve proportionately greater reductions in water use than those with low use. The regulation provides that the 2,600 "small water suppliers" in the State that serve fewer than 3,000 customers or deliver less than 3,000 acre-feet of water annually are required to either achieve a 25% conservation standard or restrict outdoor irrigation to no more than two days per week. Commercial, industrial and institutional properties that are not served by a water supplier (or are self-supplied) are similarly required to either achieve a 25% conservation standard or restrict outdoor irrigation to no more than two days per week. Under the regulation, compliance by the 411 urban water suppliers will be assessed for the period of June 2015 through February 2016 as compared to water usage in the corresponding prior timespan of June 2013 through February 2014. In addition to the total monthly water production and specific reporting on residential use and enforcement action previously adopted by the SWRCB, the regulation adopted May 5, 2015 also includes new reporting requirements for urban water suppliers to include information on water use in the commercial, industrial and institutional sectors. In order to enforce compliance by water suppliers, the regulation authorizes the SWRCB to issue informational orders, conservation orders or cease and desist orders requiring additional specific actions by a water supplier that is not meeting its conservation standard. Failure to provide information requested pursuant to an informational order within the required timeframe would be subject to civil liability of up to \$500 per day for each day out of compliance. Water agencies that violate cease and desist orders may be subject to a civil liability of up to \$10,000 a day.

Under the adopted regulation, the District is classified in Tier 6 (July - September 2014 residential per capita water use of 116 gallons or more per day) and is subject to the 24% conservation standard proposed for that tier. (See the caption “-District Drought Response Actions and Impact” for actions taken by the District in response to the drought and the 2015 Executive Order.)

On April 28, 2015, concurrent with the SWRCB’s release of the Notice of Proposed Emergency Regulations for the subsequently adopted regulation, Governor Jerry Brown also announced that he would propose new legislation to provide expanded enforcement powers to local agencies, including the ability to deputize staff to issue water conservation-related warnings and citations and to impose fines up to \$10,000 per day for infractions of locally imposed water restrictions.

While reductions in water usage resulting from implementation of the 2015 Executive Order may adversely affect the District’s projected operating results set forth under the caption “FINANCIAL INFORMATION OF THE DISTRICT—Projected Operating Results and Debt Service Coverage,” the effect of any such reduction would likely be minimized by the District’s current rate structure. The District does not currently believe that such reductions, if achieved, will have a material adverse effect on the District’s ability to pay the principal of and interest on the 2015 Bonds as a result of previously approved drought rates described under the caption “-Rates and Charges.” The District is obligated under the Indenture to set rates and charges sufficient to provide Net Revenues equal to 115% of Debt Service due in each fiscal year as more particularly described under the caption “SECURITY FOR THE 2015 BONDS—Rate Covenant.” The ability of the District to modify its current rate structure could, however, be limited by certain California Constitutional provisions, including but not limited to Proposition 218. See the caption “CONSTITUTIONAL LIMITATIONS ON APPROPRIATIONS AND CHARGES.”

District Drought Response Actions and Impact.

On May 6, 2009, the District adopted Ordinance No. 162 (the “Ordinance”) implementing certain regulations, restrictions, and measures aimed to manage water supply shortages. The Ordinance implements four Drought Response Levels, each carrying specific voluntary or mandatory conservation measures with respect to water usage. The rates corresponding to the water supply shortage levels were approved pursuant to the provisions of Proposition 218 on October 2, 2013. See “The Water System-Rates and Charges”. The District is also authorized to provide variances to mandatory conservation practices to certain customers, upon application and demonstration of undue hardship resulting from implementing such measures. The District declared a Drought Response Level 2 in August of 2014, and has not modified that declaration as a result of the 2015 Executive Order.

Drought Response Level 1 - Voluntary Conservation Practices. Level 1 occurs upon notification by SDCWA that, due to drought or other supply reductions, there is a reasonable probability there will be supply shortages and that a voluntary consumer demand reduction of up to 10% is required in order to meet anticipated demands. The District’s General Manager is authorized to declare the existence of a Drought Response Level 1, and can implement certain voluntary conservation practices. For example, consumers are encouraged to irrigate landscape efficiently, to use a hose with a shut-off nozzle for washing cars, and to restrict commercial and residential landscape irrigation to the hours before 10 a.m. and after 6 p.m. daily. Recycled or non-potable water is to be used for construction purposes when permitted, and food establishments are only to serve and refill water upon request.

Drought Response Level 2-Drought Alert. Level 2 occurs upon notification by SDCWA that, due to cutbacks caused by drought or other reduction in supplies, a consumer demand reduction of up to 20% is necessary to have sufficient supplies to meet anticipated demand. If the required reduction is 10% or less, the General Manager is authorized to determine the administration of the conservation practices. In addition to complying with voluntary conservation practices with respect to Level 1, consumers are required to limit residential and commercial landscape irrigation to 3 assigned days per week, and to use sprinklers for irrigation no more than 10 minutes per watering station per assigned day. Water leaks must be repaired within 72 hours

of notification by the District (unless otherwise provided for by the General Manager), and operation of ornamental fountains or similar decorative water features is prohibited unless re-circulated water is used.

Drought Response Level 3 – Drought Critical. Level 3 occurs upon notification by SDCWA that, due to increasing cutbacks caused by the drought or other reduction of supplies, a consumer demand reduction of up to 40% is required in order to have sufficient supplies available to meet anticipated demands. The Board of Directors shall declare that Level 3 conditions exist, the allocation reduction, and implement Level 3 conservation practices. In addition to complying with Level 1 and Level 2 conservation practices, customers are required to limit residential and commercial landscape irrigation to 2 assigned days per week, and to use sprinklers for irrigation no more than 8 minutes per watering station per assigned day. Water leaks must be repaired within 48 hours of notification by the District (unless otherwise provided for by the General Manager), and customers are prohibited from filling or refilling pools, spas, ornamental lakes or ponds (except to the extent necessary to sustain aquatic life of significant value that had been actively managed prior to declaration of Level 3 conditions). Customers are further prohibited from washing vehicles, except at commercial carwashes that re-circulate water by high pressure/low volume wash systems.

In addition, upon declaration of Level 3 conditions, no new potable water service shall be provided, no new temporary meters or permanent meters shall be provided or installed, and no statements of immediate ability to serve or provide potable water shall be issued, except under limited circumstances. The District must also suspend consideration of water service annexations to its service area, and may establish water allocation for property served by the District using a method that does not penalize persons for implementing conservation methods or installing water saving devices. The water allocation may also provide for penalties in an amount adopted by the Board of Directors for use in excess of allocation.

Drought Response Level 4 – Drought Emergency Condition. Level 4 occurs when the SDCWA declares a water shortage emergency pursuant to California Water Code Section 350, and notifies the District that a mandatory demand reduction of over 40% is required in order for the District to have adequate supplies available to meet anticipated demands. In addition to complying with Level 1, Level 2, and Level 3 conservation practices, residential and commercial customers are prohibited from all landscape irrigation and other outdoor watering (with the exception of commercial growers and nurseries), except the minimum required for maintenance of landscaping necessary for fire protection and erosion control, maintenance of rare plants or plants necessary for rare animals, maintenance of landscaping within certain public facilities including parks and cemeteries two times a week, watering of livestock, and public works projects. Water leaks must be repaired within 24 hours.

The District may also establish water allocation for property served by the District using a method that does not penalize persons for implementing conservation methods or installing water saving devices. The water allocation may also provide for penalties in an amount adopted by the Board of Directors for use in excess of allocation.

Water Quality Compliance. Water quality requirements for potable water are developed by the United States Environmental Protection Agency and the California Department of Health Services pursuant to mandates contained in the federal Safe Drinking Water Act. Since all of the potable water that the District currently delivers to its customers (both water purchased from MWD and water purchased from IID) is water that has been treated by MWD, MWD is the agency that is initially responsible for complying with all applicable water quality requirements. On the basis of data supplied by MWD, the District believes that the potable water it delivers to its customers satisfies currently applicable requirements. Any action at the federal or state level the effect of which would be to set stricter water quality standards would likely increase MWD's treatment costs, and any such increased costs would likely be reflected in the rates MWD charges SDCWA and the rates SDCWA charges the District.

Rates and Charges. In accordance with California law, the District may, from time to time, fix, alter or change fixed monthly system access (ready-to-serve) fees, commodity charges and other fees related to the

Water System and the charges related to its Wastewater System. Consequently, the District periodically reviews its rates. In accordance with California law, the District reviews such charges and fees to determine if they are sufficient to cover operation and maintenance costs, capital improvement expenditures and debt service requirements. Such charges and fees are set by the District for the services provided by the Enterprise after a noticed public hearing is held, generally at the time of adoption of the annual budget.

Neither the District nor the Enterprise is subject to the jurisdiction of, or regulation by, the California Public Utilities Commission or any other regulatory body in connection with the establishment of charges and fees related to the Enterprise. However, increases in the District’s rates and charges for a property related services within the meaning of Article XIII D of the California Constitution are subject to the provisions thereof. See “CONSTITUTIONAL LIMITATIONS ON APPROPRIATIONS AND CHARGES — Proposition 218” and “— Effect of Proposition 218 and of Possible General Limitations on Enforcement Remedies.”

The District charges for water based on a tiered structure charge per unit (a unit consists of 748 gallons) (see the caption “CONSTITUTIONAL LIMITATIONS ON APPROPRIATIONS AND CHARGES-Proposition 218” for a discussion on tiered rates). The current tier limits and per-unit rates are noted in the table below. The agricultural rate reflects a 73¢ credit per unit and are not subject to higher tier rates. Currently, 2,813 customers located in high elevations pay an additional 1¢ to 51¢ per unit to recover the power costs associated with pumping. The District also charges a monthly ready-to-serve (“RTS”) charge to recover the costs of maintenance on meters, water lines and storage facilities, customer service, meter reading, billing, engineering, administration, and other costs to assure that water is available upon demand. Current RTS charges are identified in Table No. 3 following the tiered rate table. The District anticipates wholesale rate increases each year from MWD and SDCWA, and passes them on to its customers through the commodity and RTS rates automatically per District ordinance. Retail increases may be recommended during or after preparation of the annual operating budget considering expense projections, rate covenants and reserve floors.

Table No. 2
VALLECITOS WATER DISTRICT WATER SYSTEM
SCHEDULE OF WATER UNITS AND RATES
(As of January 1, 2015)

	<i>Tier 1</i> <i>(\$2.62/unit)</i>	<i>Tier 2</i> <i>(\$3.66/unit)</i>	<i>Tier 3</i> <i>(\$4.87/unit)</i>	<i>Tier 4</i> <i>(\$6.95/unit)</i>
Multi-family ⁽¹⁾	1-5	6 units per living unit	11 units per living unit	12 units and up per living unit
5/8” and 3/4” meters	1-5	6-17	18-36	37 and up
1” meter	1-5	6-60	61-214	215 and up
1 1/2” meters	1-5	6-157	158-627	628 and up
2” meters	1-5	6-242	243-806	807 and up
3” and larger meters	1-5	6-1,133	1,134-3,970	3,971 and up
Certified Agricultural	1-5	6 and up	--	--
Temporary construction meters	--	--	--	1 and up

(1) Multi-family with 3 living units or less are billed by the meter size. Multi-family of more than 3 living units are billed at the Tier 1 rate for the first 5 units per account and by the Tier limit times the number of living units for Tier 2 and higher
Source: District

Table No. 3
VALLECITOS WATER DISTRICT
MONTHLY METER RTS CHARGES
(Effective July 1, 2015)

<i>Meter Size</i>	<i>Charge</i>
5/8"	\$31.42
3/4"	36.52
1"	55.29
1 1/2"	110.59
2"	178.11
3"	356.22
4"	552.94
6"	1,105.88
10"	2,549.36
Additional living unit	18.26
Temporary construction	204.48
Fire service per diameter	5.87

Source: District

Drought rates become effective when a level of conservation is mandated. Tiers 2 through 4 of the non-drought rates are split and the following multipliers are applied to the Tier 2 rate based on the percentage of cutback. Rate multipliers are adjusted for actual levels of mandated conservation.

Table No. 4
VALLECITOS WATER DISTRICT
DROUGHT RATE MULTIPLIERS
(Effective July 1, 2015)

	<i>Level 2</i> <i>20% Cutback</i>	<i>Level 3</i> <i>40% Cutback</i>
	Wholesale Rate	Wholesale Rate
Tier 1		
Tier 2	1.00	1.00
Tier 3	1.20	1.40
Tier 4	1.40	2.30
Tier 5	2.30	3.00
Tier 6	3.00	4.60
Tier 7	4.60	6.20

Source: District

Collection Procedures. The District is on a monthly billing cycle and sends bills out by the third day following the end of a billing cycle. Customers who receive both water and wastewater services receive a single bill. Payment is due within 20 days following the mailing of the original bill. If payment is not received by the 35th day following the mailing of the original bill, accounts are charged a delinquency charge equal to 10% of the unpaid balance. At least 15 days prior to discontinuance of service due to non-payment of water bills, the District mails delinquent notices to customers with past due bills. At least 48 hours prior to discontinuance of service due to non-payment, the District posts a shut off notice in a conspicuous location on the property. If the notice cannot be posted on the property, it is mailed. A final attempt to contact the customer by telephone is made at least 12 hours prior to actual discontinuance of service. Service will not be discontinued if there are any known life threatening consequences, or during payment negotiations by customer request. Also, the District will not terminate service to a customer making payments under an

amortization agreement, as long as payments under the agreement and subsequent charges for water use are both kept current. However, if payments under a payment agreement are not received timely, the District may discontinue water service. Once service has been discontinued, service is reinstated only after the customer pays the past due balance plus a service charge. For closed accounts, the District sends a closing bill as part of the current billing cycle. A second notice is sent after the closing bill becomes delinquent. Accounts which remain unpaid after 90 days are submitted to the District's collection agency. At March 31, 2015, delinquencies represented less than 1% of billings.

Water Meter Connections. The following table presents a summary of meter connections to the Water System for the most recent five Fiscal Years:

**Table No. 5
VALLECITOS WATER DISTRICT
HISTORIC METER CONNECTIONS**

<i>Year Ended June 30</i>	<i>Meter Connections</i>	<i>Percent Increase</i>
2015 ⁽¹⁾	21,358	0.3%
2014	21,295	1.1
2013	21,060	1.1
2012	20,826	1.0
2011	20,623	0.5

⁽¹⁾ Reflects actual unaudited results as of March 31, 2015, and projected results through June 30, 2015.
Source: District

The following table presents the District's projection of meter connections for the current and next four Fiscal Years:

**Table No. 6
VALLECITOS WATER DISTRICT
PROJECTED METER CONNECTIONS**

<i>Year Ending June 30</i>	<i>Meter Connections</i>	<i>Percent Increase</i>
2016	21,550	0.8%
2017	21,730	0.8
2018	21,910	0.8
2019	22,090	0.8
2020	22,270	0.8

⁽¹⁾ Fiscal Year 2016 reflects District's budgeted amount. Projected to increase at a rate of approximately 0.8% per annum thereafter.
Source: District

Water Purchases and Demand. Historical water purchases by the District from SDCWA over the 10-year period ended in Fiscal Year 2015 show that the District has reduced water purchases from a high of 21,836 acre-feet in Fiscal Year 2007 to 17,900 acre-feet in Fiscal Year 2015, primarily as a result of conservation. The District estimates that approximately six percent (6%) of water purchases is unbilled due to tie-ins, unmetered operational use, fire hydrant damage and use, meter malfunctions and leaks in the system. The actual amount of water sold is estimated to be correspondingly lower than the water purchased by a similar six percent (6%) factor. The District records the volume of water delivered by the Water System.

The following table summarizes water purchases and deliveries for the most recent ten Fiscal Years.

**Table No. 7
VALLECITOS WATER DISTRICT
WATER PURCHASES AND DELIVERIES**

<i>Year Ended June 30</i>	<i>Acre-Feet Purchased</i>	<i>Acre-Feet Delivered</i>	<i>Percent of Ten Year Average</i>	<i>Percent Change of Deliveries</i>
2015 ⁽¹⁾	16,300	15,900	93.4%	(4.10)%
2014	17,900	16,581	96.7	3.72
2013	17,430	15,987	92.3	11.88
2012	16,210	14,290	82.2	-2.00
2011	15,433	14,581	83.0	-4.99
2010	16,108	15,346	87.2	-16.20
2009	19,107	18,313	104.1	-7.40
2008	20,566	19,776	115.8	-3.66
2007	21,836	20,528	126.1	8.71
2006	19,575	18,883	121.4	10.03

⁽¹⁾ Reflects actual unaudited results as of March 31, 2015, and projected results through June 30, 2015.
Source: District

Beginning in Fiscal Year ending 2016, the District will also purchase treated water from the Olivenhain Municipal Water District (“Olivenhain”), which Olivenhain in turn purchases from SDCWA. The following tables show the water purchases and deliveries projected by the District for the current and next four Fiscal Years from SDCWA and Olivenhain, as well as supply of desalinated water from the Carlsbad Desalter. Increases in water purchases and deliveries are projected to occur primarily as a result of new connections to the Water System and to a lesser extent because of increased water consumption by existing consumers. Actual water deliveries may vary materially from those estimated below.

**Table No. 8
VALLECITOS WATER DISTRICT
WATER PURCHASES AND DELIVERIES FROM SDCWA AND OLIVENHAIN
FIVE YEAR PROJECTION
(Acre-Feet)**

<i>Year Ending June 30</i>	<i>Acre-Feet Purchased</i>	<i>Acre-Feet Delivered</i>	<i>Percent Change of Deliveries</i>
2016	10,338	9,873	--
2017	9,439	9,014	(8.7)%
2018	10,296	9,832	9.1
2019	11,209	10,704	8.9
2020	12,185	11,636	8.7

Source: District

Table No. 9
VALLECITOS WATER DISTRICT
WATER SUPPLY FROM CARLSBAD DESALTER
FIVE YEAR PROJECTION
(Acre-Feet)

<i>Year Ending June 30</i>	<i>Acre-Feet Purchased</i>	<i>Acre-Feet Delivered</i>	<i>Percent Change of Deliveries</i>
2016	2,040	1,948	--
2017	4,083	3,899	100%
2018	4,083	3,899	0
2019	4,083	3,899	0
2020	4,083	3,899	0

Source: District

Largest Water Customers. The following table presents certain information relating to the ten largest customers of the Water System based on estimated usage for the Fiscal Year ended June 30, 2015:

Table No. 10
VALLECITOS WATER DISTRICT
TEN LARGEST CUSTOMERS
(As of March 31, 2015)

<i>Customer</i>	<i>Land Use(s)</i>	<i>Acre-feet of Water</i>	<i>Water as a % of Total Fiscal Year 2015 Sales</i>
City of San Marcos	Offices/Irrigation	688.1	4.33%
San Marcos Unified School District	Schools/Offices	250.5	1.58
San Elijo Hills Community Association	Irrigation	178.1	1.12
Escondido Highlands HOA	Irrigation	162.4	1.02
Bonsall Farms	Agriculture	157.1	0.99
Palomar Estates East/West	Mobile Home Parks	139.0	0.87
D.R. Horton	Agriculture	118.4	0.74
Golden Door Properties, LLC	Commercial	115.2	0.72
Palomar College	Schools/Offices	105.7	0.66
Meadowridge HOA	Irrigation	103.5	0.65

Source: District

The ten largest customers of the Water System accounted for approximately 12.68% of water delivered in Fiscal Year 2015.

Water System Revenues. The following table shows the District’s annual revenues from water sales (exclusive of pumping charges and RTS charges) for the five most recent Fiscal Years.

**Table No. 11
VALLECITOS WATER DISTRICT
HISTORIC WATER SALES REVENUES**

<i>Year Ended June 30</i>	<i>Water Sales Revenues</i>	<i>Percent Change</i>
2015 ⁽¹⁾	\$24,998,000	(3.97)%
2014	26,031,460	11.41
2013	23,364,573	21.92
2012	19,164,527	10.79
2011	17,298,173	--

⁽¹⁾ Reflects actual unaudited results as of March 31, 2015, and projected results through June 30, 2015.
Source: District

The following table projects annual water sales revenues of the Water System (excluding pumping charges and RTS charges) for the current and next four Fiscal Years. The projection of water sales revenues set forth below is based on the assumptions and increases in projected water deliveries described under “Combined Water and Wastewater Systems — Projected Enterprise Operating Results” below and may vary from actual water sales revenues for the reasons described thereunder. In the event that the District increases or decreases rates and charges, actual sales revenues will vary from those projected below.

**Table No. 12
VALLECITOS WATER DISTRICT
PROJECTED WATER SALES REVENUES**

<i>Year Ending June 30</i>	<i>Water Sales Revenues⁽¹⁾</i>	<i>Percent Change</i>
2016	\$20,229,000	(14.8)%
2017	23,065,000	14.0
2018	26,551,000	15.1
2019	30,140,000	13.5
2020	34,287,000	13.8

⁽¹⁾ Assumes pass through of any increased costs from MWD and SDCWA. Fiscal Year 2016 reflects projected implementation of mandatory water sales reduction in accordance with a Governor’s Executive Order, dated April 1, 2015. See “-California Drought and Response-Governor’s Executive Orders.”
Source: District

Wastewater System

Wastewater System Facilities. The District provides wastewater collection and treatment services to customers within its service area. The District collects and transports wastewater through 4 lift stations and 273 miles of pipeline, ranging in size from 4” to 42”. Upon collection, the District delivers on average approximately 3.5 million gallons per day to the Encina Wastewater Authority, and on average approximately 3.5 million gallons per day to the Meadowlark Water Reclamation Facility. The District owns, operates, and maintains the Meadowlark Reclamation Facility, and delivers wastewater to the Encina Wastewater Authority pursuant to a series of agreements (see the caption “—Encina Wastewater Authority” for more information).

In addition, the District expanded the Meadowlark Water Reclamation Facility in 1982 to include wastewater treatment and recycled water services. The Meadowlark Water Reclamation Facility recycles up to 74% of the wastewater generated within the District, and distributes the reclaimed water for irrigation purposes outside of the District. The District holds up to 54 million gallons of reclaimed water in the Mahr Reclaimed Water Reservoir, which is owned operated, and maintained by the District.

Encina Wastewater Authority. The District is a member of the Encina Wastewater Authority (“EWA”). The EWA is a joint powers agency among the District, the Cities of Vista, Carlsbad, Encinitas, the Buena Sanitation District, and the Leucadia Wastewater District.

The EWA was created in 1988 pursuant to a joint powers agreement (the “Joint Powers Agreement”), and currently operates certain wastewater treatment facilities including the Encina Water Pollution Control Facility (“EWPCF”). The District receives wastewater treatment services from the EWPCF pursuant to a series of agreements. The District pays both operating and capital costs related to the EWPCF. The operating costs paid by the District to EWA are treated as Maintenance and Operation Costs. Capital cash paid by the District to EWA are not included in Maintenance and Operation Costs.

For further information about EWA, contact Michael Steinlicht, Assistant General Manager, at (760) 268-8847.

Service Area. As of March 31, 2015, the Wastewater System included a total of approximately 20,470 connections, including approximately 19,601 residential service connections, approximately 756 industrial and commercial service connections, and approximately 113 public and miscellaneous service connections. The following table illustrates use of the Wastewater System in calendar year 2014.

**Table No. 13
VALLECITOS WATER DISTRICT
WASTEWATER SYSTEM DISCHARGE BY TYPE
(Calendar Year 2014)⁽¹⁾**

<i>Types of Dischargers</i>	<i>Percentage of Total*</i>
Residential	83%
Commercial/Industrial	14
Public, Other	<u>3</u>
Total	100%

⁽¹⁾ Unaudited.

* The Wastewater System is not metered, so percentages of Wastewater System usage are estimated to be approximately the same as the percentages of total wastewater revenue.

Source: District

Wastewater Rates and Charges. The following table sets forth the District’s monthly charges for its Wastewater System, effective July 1, 2015.

Table No. 14
VALLECITOS WATER DISTRICT WATER SYSTEM
MONTHLY WASTEWATER SERVICE CHARGES
(effective July 1, 2015)

<i>Type of Discharger</i>	<i>Monthly Charge</i>
Single Family Residential	\$38.99
Residential Multiple unit	35.09
Mobile Home	31.19
Nonresidential flow (per 100 cu ft)	4.96
Commercial/Industrial (per employee)	3.51
Restaurant (per seat)	2.34
Hotel/motel/conv (per living unit)	19.50
Laundromat (per machine)	32.44
Schools (per student)	0.78
Church/theater (per seat)	0.31
Minimum commercial charge	24.56

Source: District

Collection Procedures. Wastewater System customers who are also customers of the Water System receive a single monthly bill for both services. See “THE ENTERPRISE — Water System - Collection Procedures” for a discussion of the process for the distribution and collection of those bills. Wastewater System customers who are not customers of the Water System are billed on the *ad valorem* property tax bills prepared and distributed by the County of San Diego. Property taxes are payable to the County semiannually. Wastewater System charges that are collected by the County are remitted to the District along with the District’s allocation of property taxes.

Wastewater Connections. The following tables present a summary of connections to the District’s Wastewater System for the most recent five Fiscal Years and the District’s projection of such connections for the current and next four Fiscal Years:

Table No. 15
VALLECITOS WATER DISTRICT
HISTORIC WASTEWATER CONNECTIONS

<i>Year Ended June 30</i>	<i>Wastewater Connections</i>	<i>Percent Increase</i>
2015 ⁽¹⁾	20,515	0.2%
2014	20,468	0.2
2013	20,280	0.4
2012	20,191	1.4
2011	19,907	1.2

⁽¹⁾ Reflects actual unaudited results as of March 31, 2015, and projected results through June 30, 2015.

Source: District

Wastewater connections declined in Fiscal Year 2014 as a result of removal of duplicate wastewater accounts from total wastewater connections.

Table No. 16
VALLECITOS WATER DISTRICT
PROJECTED WASTEWATER CONNECTIONS⁽¹⁾

<i>Year Ending June 30</i>	<i>Wastewater Connections</i>	<i>Percent Increase</i>
2016	20,695	0.9%
2017	20,875	0.8
2018	21,043	0.8
2019	21,211	0.8
2020	21,379	0.8

⁽¹⁾ Fiscal Year 2016 reflects District's budgeted amount. Projected to increase at a rate of approximately 0.8% per annum thereafter.

Source: District

Largest Wastewater Dischargers. The Wastewater System is not metered, so the District does not track the largest wastewater dischargers as it does in the case of the water users.

Wastewater System Revenues. The following table shows the District's annual revenues from its Wastewater System for the five most recent Fiscal Years.

Table No. 17
VALLECITOS WATER DISTRICT
HISTORIC WASTEWATER REVENUES

<i>Year Ended June 30</i>	<i>Wastewater Revenues</i>	<i>Percent Increase</i>
2015 ⁽¹⁾	\$16,638,000	9.98%
2014	15,128,763	1.39
2013	14,921,894	8.29
2012	13,780,015	7.19
2011	12,855,742	--

⁽¹⁾ Reflects actual unaudited results as of March 31, 2015, and projected results through June 30, 2015.

Source: District

The following table projects annual revenues of the Wastewater System for the current and next four Fiscal Years. The projection of such revenues set forth below is based on the assumptions and increases in projected wastewater connections described under “Combined Water and Wastewater Systems — Projected Enterprise Operating Results” below and may vary from actual revenues for the reasons described thereunder.

Table No. 18
VALLECITOS WATER DISTRICT
PROJECTED WASTEWATER REVENUES

<i>Year Ending June 30</i>	<i>Wastewater Revenues</i>	<i>Percent Increase</i>
2016	\$17,296,000	3.96%
2017	17,846,000	3.17
2018	18,412,000	3.17
2019	18,996,000	3.17
2020	19,599,000	3.17

⁽¹⁾ Fiscal Year 2016 reflects District’s budgeted amount. Projected to increase at a rate of approximately 3.17% per annum thereafter.
Source: District

Combined Water and Wastewater Systems

Rates and Charges. The table below sets forth a comparison of a monthly bill for water and wastewater service for a single family residential unit in the District to those of surrounding neighboring communities (assuming that 17 units of 748 gallons each are taken during the month in the case of the water bill and, for agencies that base their wastewater charges on low-month water usage, that 12 such units are taken in the case of the wastewater bill):

Table No. 19
VALLECITOS WATER DISTRICT
MONTHLY BILL COMPARISON
(As of June 30, 2015)

<i>Agency</i>	<i>Monthly Average for Single Family Residence</i>		
	<i>Water</i>	<i>Wastewater</i>	<i>Total</i>
Valley Center MWD-Woods Vly	\$ 91.87	\$98.60	\$190.47
Del Mar, City of	90.11	90.93	181.04
Valley Center MWD-Moosa/press	91.87	51.20	143.07
Rainbow MWD	109.25	56.20	165.45
Santa Fe ID-RSF-Dudek & Assoc	67.04	66.67	133.71
San Diego, City of	83.27	47.71	130.98
Fallbrook PUD	94.65	90.50	185.15
San Dieguito WD-Cardiff	70.35	45.86	116.21
Vista Irrigation District-Buena	88.05	59.25	147.30
OlivenhainMWD-Rancho Ciel	79.66	63.92	143.58
San Dieguito WD-Encinitas	70.35	45.26	115.61
Escondido, City of	92.54	55.08	147.62
Helix Water District - La Mesa	71.34	56.13	127.47
Sweetwater Authority / CV	79.46	33.99	113.45
Padre Dam MWD West - EC	114.74	53.49	168.23
Ramona MWD-San Vicente	109.17	51.98	161.15
Ramona MWD-Santa Maria	109.17	56.31	165.48
Valley Center MWD-Moosa/grav	91.87	93.45	185.32
Vista Irrigation District-City	88.05	53.25	141.30
Poway, City of	75.70	39.88	115.58
Sweetwater Authority / NC	79.46	32.08	111.54
Olivenhain MWD - Ranch	79.66	39.92	119.58
Valley Center MWD-Skyline	91.87	--	91.87
Santa Fe ID-Solana Beach	67.04	50.26	117.30
Rincon Del Diablo MWD	77.73	55.08	132.81
Helix Water District / El Cajon	71.34	53.49	124.83
Oceanside, City of	73.14	51.56	124.70
Vallecitos Water District	75.33	37.45	112.78
Otay Water District	81.67	45.16	126.83
San Dieguito WD / Leucadia	70.35	23.67	94.02
Carlsbad MWD	79.86	26.03	105.89
Average	\$ 84.39	\$54.14	\$136.78

Monthly averages were computed using 18 HCF units per month, and for sewer rates, the two lowest winter months equaling 11 and 13 HCF units.

Source: <http://www.utsandiego.com>

Capital Facility Fees. Capital Facility Fees are charged to recover the cost of the facilities needed to meet the capacity requirements for growth. Such fees are intended to recover an equitable share of the value of capacity in the facilities that are (or will be) available to serve growth. After a public hearing, the District can approve additional increases in Capital Facility Fees for Water System and Wastewater System hook-up permits as long as the increase does not exceed the reasonable cost of providing capital improvements.

The table below sets forth a comparison of Capital Facility Fees for a single family residential unit to the water system and wastewater system connection fees in surrounding communities:

Table No. 20
VALLECITOS WATER DISTRICT
CAPITAL FACILITY FEE COMPARISON
(As of January 1, 2015)

<i>Agency</i>	<i>Connection Fees</i>		
	<i>Water</i>	<i>Sewer</i>	<i>Total</i>
Rainbow MWD	\$ 13,097.00	\$ 17,090.00	\$ 30,187.00
Padre Dam MWD	15,393.67	7,163.00	22,556.67
Ramona MWD	7,000.00	13,280.00	20,280.00
Fallbrook PUD	5,340.00	6,575.00	11,915.00
Escondido, City of	4,690.00	7,500.00	12,190.00
Santa Fe ID	7,057.00	4,500.00	11,557.00
Rincon del Diablo MWD	5,992.00	7,500.00	13,492.00
Otay WD	8,180.35	5,375.01	13,555.36
Poway, City of	5,448.00	6,153.00	11,601.00
Vallecitos WD	7,036.00	9,039.00	16,075.00
Oceanside, City of	4,597.00	6,313.00	10,910.00
Olivenhain MWD	8,466.60	1,300.00	9,766.60
Vista Irrigation District	4,956.00	4,262.00	9,218.00
San Diego, City of	3,047.00	4,124.00	7,171.00
Sweetwater Authority	2,300.00	3,450.00	5,750.00
San Dieguito WD	4,000.00	3,367.67	7,367.67
Helix WD	6,842.00	6,226.50	13,068.50
Carlsbad MWD	3,931.00	2,344.00	6,275.00
Valley Center MWD	4,644.00	8,935.00	13,579.00
Del Mar, City of	3,493.00	6,443.54	9,936.54
Yuima MWD	2,674.00	--	2,674.00

Source: District.

Future Enterprise Improvements. The District's current Capital Facilities Master Plan was updated in 2008. The District believes that the capital projects contemplated in the 2016 Budget will satisfy planned future demand within the District boundaries, absent a significant change to projected demand in the new Master Plan.

As further growth in the District requires, the District anticipates expanding the Water System and the Wastewater System to add new water lines and storage facilities as contemplated by the District's Master Plan. The District anticipates that most of the new lines and storage facilities will be constructed for the District by property owners in connection with the development of their properties and that revenues derived from the Capital Facility Fees will be sufficient to pay the costs of any such future improvements not constructed by property owners.

1% Property Tax Revenues. The District receives a portion of the County 1% property tax levied on behalf of all taxing agencies in the County. The District also receives moneys from successor agencies to certain redevelopment agencies with which the District has pass-through and other tax-sharing agreements. All moneys received by the District as distributions of the 1% property tax and from such successor agencies are included in the Revenues of the District.

The taxes collected by the County are allocated to taxing agencies within the County, including the District, on the basis of a formula established by State law enacted in 1979. Under this formula, the County and all other taxing entities receive a base year allocation plus an allocation on the basis of "situs" growth in assessed value (new construction, change of ownership and inflation) prorated among the jurisdictions, which serve the tax rate areas within which the growth occurs. Tax rate areas are specifically defined geographic areas, which were developed to permit the levying of taxes for less than countywide or less than citywide special districts.

From time to time legislation has been considered as part of the State budget to shift Property Tax Revenues from special districts to school districts or other governmental entities. While legislation enacted in connection with the 1992-93 State budget shifted approximately 35% of many special districts' shares of the countywide one percent ad valorem tax, the share of the countywide one percent ad valorem tax allowable to multi-county special districts, such as the District, was exempted. The 2004-05 State budget reallocated additional portions of the special districts' shares of the countywide one percent ad valorem tax, shifting a portion of the property tax revenues collected by the County from special districts to school districts. As a result of the 2004-05 State budget, the District lost approximately \$2,030,000 of revenue from property tax, cumulatively, over Fiscal Years 2005 and 2006. Pursuant to the 2004-05 State budget, such property tax revenues reverted to the District in Fiscal Year 2007.

On November 2, 2004, State voters approved Proposition 1A, which amends the State Constitution to significantly reduce the State's authority over major local government revenue sources. Under Proposition 1A, the State may not, among other things: (i) shift property taxes from local governments to schools or community colleges; or (ii) change how one percent ad valorem property tax revenues are shared among local governments without two-thirds approval of both houses of the State Legislature. Beginning in State fiscal year 2009-10, the State may shift to schools and community colleges a limited amount of local government property tax revenues if certain conditions are met, including: (a) a proclamation by the Governor that the shift is needed due to a severe financial hardship of the State; and (b) approval of the shift by the State Legislature with a two-thirds vote of both houses. Under such a shift, the State must repay local governments for their property tax losses, with interest, within three years and no additional shifts may occur until the State repays the shifted revenues. Proposition 1A does allow the State to approve voluntary exchanges of local sales tax and property tax revenues among local governments within a county.

On July 27, 2009, the Governor of the State signed a revised fiscal year 2009-10 State budget which included a shift of approximately 8% of the one percent *ad valorem* property tax revenues from certain local agencies, including the District, to school districts and other governmental agencies. The District participated in the State of California Proposition 1A Receivables Program to securitize its receivable from the State, and as a result received the funds shifted in the amount of \$138,756, without interest, in 2 installment payments in 2010 from the California Statewide Communities Development Authority.

There can be no assurance that the property tax revenues that the District currently expects to receive will not be temporarily shifted from the District pursuant to Proposition 1A in future years, or reduced pursuant to State legislation enacted in the future. If the property tax formula is changed in a State fiscal year or permanently changed in the future, it could have a material adverse effect on the receipt of property tax revenues by the District.

The District expects that moneys received from successor agencies to certain redevelopment agencies described above will decline over time. The timing of such decline, however, is difficult for the District to predict. See the caption “-Projected Enterprise Operating Results.”

Assessed Valuations, Tax Collections and Tax Delinquencies

The following tables show the secured assessed valuation within the District and the amount received by the District of the 1% property tax during the five most recent Fiscal Years, and payments from redevelopment agencies and successor agencies pursuant to pass-through and other tax-sharing agreements.

Table 21
SAN DIEGO COUNTY
SECURED ASSESSED VALUATION AND DISTRICT ALLOCATION
(County Fiscal Years Ending June 30, 2010 Through June 30, 2014)

<i>Fiscal Year</i>	<i>Total Secured Assessed Valuation</i>	<i>District Allocation in Corresponding Fiscal Year</i>
2010	\$10,668,875,155	\$1,571,592
2011	10,600,146,556	1,562,158
2012	10,755,217,186	1,564,122
2013	10,749,957,402	1,616,799
2014	11,220,883,652	1,697,736

Source: San Diego County Auditor-Controller for Total Secured Assessed Valuation; Vallecitos Water District for District of 1% property tax allocations.

Table 22
VALLECITOS WATER DISTRICT
PAYMENTS FROM REDEVELOPMENT AGENCIES AND SUCCESSOR AGENCIES
(Fiscal Years Ended June 30)

<i>Fiscal Year</i>	<i>Amount</i>
2010	\$ 866,579
2011	683,046
2012	1,832,882
2013	1,902,282
2014	1,380,230

Source: District

Historic Enterprise Operating Results. The following table is a summary of the operating results of the Enterprise for the last five Fiscal Years for which audited financial results are available. These results have been derived from the District's financial statements but exclude certain non-cash items such as depreciation and include certain other adjustments. This table has not been reviewed by the District's auditor.

Table No. 23
VALLECITOS WATER DISTRICT
HISTORIC ENTERPRISE OPERATING RESULTS
(Fiscal Year Ended June 30)

	2010	2011	2012	2013	2014
Revenues					
Water sales	\$16,798,224	\$ 17,298,173	\$19,164,527	\$ 23,364,573	\$ 26,031,460
Wastewater service charge	12,013,152	12,855,742	13,780,015	14,921,894	15,128,763
Ready-to-serve	7,833,940	9,080,597	9,945,683	10,638,282	11,484,584
Reclaimed water sales	2,151,145	1,604,276	1,710,914	1,718,013	1,533,203
Pumping charge	194,907	171,875	157,887	171,107	192,427
Other services & abatements	1,006,167	562,212	576,906	590,667	912,212
1% Property Tax Revenue ⁽¹⁾	2,438,173	2,245,553	3,397,004	3,519,081	3,077,966
Investment income ⁽²⁾	251,610	226,829	191,262 ⁽³⁾	331,989	226,160
Capital facilities fees ⁽⁴⁾	2,586,209	2,321,509	4,912,864	7,549,785	2,573,944
Other Revenues ⁽⁵⁾	271,455	84,623	31,835	74,440	331,705
Total Revenues	\$45,544,982	\$46,451,389	\$53,677,635	\$62,879,831	\$61,492,424
Maintenance and Operation Costs					
Water purchases	\$15,603,958	\$16,468,792	\$19,107,271	\$21,982,845	\$ 24,145,579
General and administrative	5,216,874	5,224,802	4,842,082	4,879,580	5,173,986
Meadowlark wastewater treatment plant	3,456,133	3,116,849	2,653,869	2,777,837	2,993,578
Encina Wastewater Authority ⁽⁶⁾	2,162,753	2,097,610	2,078,337	2,709,307	2,450,330
Collection and conveyance	1,664,388	1,737,012	1,737,981	1,703,359	1,632,347
Engineering	2,006,925	2,078,053	1,784,054	1,633,839	1,698,699
Transmission and distribution	1,079,479	1,122,921	1,022,862	1,068,907	1,154,882
Other expenses ⁽⁷⁾	5,400,353	5,031,780	5,021,239	5,200,851	5,340,399
Total Maintenance and Operation Costs	\$36,590,863	\$36,877,819	\$38,247,695	\$41,956,525	\$44,589,800
Net Revenues	\$8,954,119	\$9,573,570	\$15,621,202	\$20,923,306	\$16,902,624
Transfers to Rate Stabilization Fund	--	--	--	--	--
Transfers from Rate Stabilization Fund	--	--	--	--	--
Adjusted Annual Net Revenues	\$8,954,119	\$9,573,570	\$15,621,202	\$20,923,306	\$16,902,624
Annual Debt Service					
2005A Installment Purchase Agreement ⁽⁸⁾	\$4,369,588	\$4,399,388	\$4,401,588	\$4,406,238	\$4,411,988
2012 Installment Purchase Agreement ⁽⁸⁾	--	--	--	39,050	779,195
Total Annual Debt Service	\$4,396,588	\$4,399,388	\$4,401,588	\$4,445,288	\$5,191,183
Debt Service Coverage – Net Revenues	2.04	2.18	3.55	4.71	3.26
Debt Service Coverage – Adjusted Annual Net Revenues	2.04	2.18	3.55	4.71	3.26
Adjusted Annual Net Revenue remaining after payment of Annual Debt Service	\$4,557,531	\$5,174,182	\$11,219,614	\$16,478,018	\$11,711,441

Subordinate Payments					
2008 Loan ⁽⁸⁾	\$503,949	\$476,901	\$465,475	\$489,058	\$462,856
Total Subordinate Payments	\$503,949	\$476,901	\$465,475	\$489,058	\$462,856
Total Debt Service Coverage – Adjusted Annual Net Revenues⁽⁹⁾	1.83	1.96	3.21	4.24	2.99
Total Debt Service Coverage – Net Revenues⁽¹⁰⁾	1.83	1.96	3.21	4.24	2.99
Adjusted Annual Net Revenue available after Subordinate Payments	\$4,053,582	\$4,697,281	\$10,754,139	\$15,988,960	\$11,248,585

Source: The District.

- (1) Property taxes as set forth in the audited financial statements. Includes 1% property tax revenue received by the District in addition to pass-through payments pursuant to certain pass-through agreements with dissolved redevelopment agencies.
- (2) Excludes unrealized appreciation or depreciation of investments.
- (3) Investment income was restated in the Fiscal Year 2013 audited financial statements.
- (4) Included as a portion of Capital Contributions in audited financial statements.
- (5) Includes miscellaneous revenues, annexation fees and certain other revenues.
- (6) Excludes capital charges payable by the District to the Encina Wastewater Authority pursuant to the Joint Powers Agreement.
- (7) Includes Maintenance and Operation Costs relating to customer accounts, information technology, buildings and grounds, meter reading and repairs, tanks and reservoirs, equipment and vehicles, pumping, water quality and treatment, and other water and wastewater Maintenance and Operation Costs, and certain expenses consisting of refunds from prior years and miscellaneous reimbursements.
- (8) Reflects debt service paid in each Fiscal Year, as required under the Master Contract, as opposed to debt service accrued in each fiscal year as reflected in the audited financial statements for the respective fiscal year.
- (9) Debt service coverage ratio calculated using Adjusted Annual Net Revenues divided by Total Annual Debt Service and Total Subordinate Payments.
- (10) Debt service coverage calculated using Net Revenues divided by Total Annual Debt Service and Total Subordinate Payments.

Projected Enterprise Operating Results. The District's projected operating results for the Enterprise for the current and next four Fiscal Years are set forth below. These projections are based on the District's judgment as to the most probable occurrence of certain future events. The assumptions set forth in the footnotes to the chart and beneath it are material to the projections, and variations in the assumptions could produce substantially different financial results. Actual revenues and expenses may vary materially from these projections.

Table No. 24
VALLECITOS WATER DISTRICT
PROJECTED OPERATING RESULTS AND
DEBT SERVICE COVERAGE
(Fiscal Year Ending June 30)

	2015 ⁽¹⁾	2016 ⁽²⁾	2017	2018	2019
Revenues					
Water sales ⁽³⁾	\$ 24,998,000	\$ 20,229,000	\$ 23,065,000	\$ 26,551,000	\$ 30,140,000
Wastewater service charge ⁽⁴⁾	16,638,000	17,296,000	17,846,000	18,412,000	18,996,000
Ready-to-serve ⁽⁵⁾	12,724,000	13,502,000	13,839,000	14,372,000	15,031,000
Reclaimed water sales ⁽⁶⁾	1,558,000	1,724,000	1,730,000	1,779,000	1,805,000
Pumping charge ⁽⁷⁾	181,000	198,000	201,000	229,000	236,000
Other services & abatements ⁽⁸⁾	634,000	656,000	669,000	682,000	695,000
1% Property Tax Revenue ⁽⁹⁾	2,382,000	3,060,000	3,086,000	3,012,000	3,040,000
Investment income ⁽¹⁰⁾	420,000	296,000	276,000	265,000	273,000
Capital facilities fees ⁽¹¹⁾	3,259,000	4,448,000	4,559,000	4,673,000	3,909,000
Other Revenues ⁽¹²⁾	126,000	148,000	148,000	148,000	-
Total Revenues	\$ 62,920,000	\$ 61,557,000	\$ 65,419,000	\$ 70,123,000	\$ 74,125,000
Maintenance and Operation Costs					
Water purchases ⁽¹³⁾	\$23,790,000	\$16,731,000	\$17,502,000	\$20,166,000	\$22,401,000
Desalter payments ⁽¹⁴⁾	--	3,937,000	8,003,000	8,263,000	8,533,000
General and administrative ⁽¹⁵⁾	4,098,000	4,387,000	4,613,000	4,855,000	4,870,000
Meadowlark wastewater treatment plant ⁽¹⁶⁾	2,778,000	3,585,000	3,356,000	3,474,000	3,598,000
Encina Wastewater Authority ⁽¹⁷⁾	2,498,000	2,617,000	2,696,000	2,777,000	2,860,000
Collection and conveyance ⁽¹⁸⁾	1,809,000	2,188,000	2,295,000	2,409,000	2,738,000
Engineering ⁽¹⁹⁾	1,802,000	1,941,000	2,052,000	2,185,000	2,154,000
Transmission and distribution ⁽²⁰⁾	1,110,000	1,460,000	1,534,000	1,610,000	1,747,000
Other expenses ⁽²¹⁾	5,333,000	6,931,000	7,243,000	7,552,000	7,987,000
Total Maintenance and Operation Costs	\$43,218,000	\$43,777,000	\$49,294,000	\$53,291,000	\$56,888,000
Net Revenues	\$19,702,000	\$17,780,000	\$16,125,000	\$16,832,000	\$17,237,000
Transfers to Rate Stabilization Fund ⁽²²⁾	--	--	--	--	--
Transfers from Rate Stabilization Fund ⁽²³⁾	--	--	--	--	--
Adjusted Annual Net Revenues	\$19,702,000	\$17,780,000	\$16,125,000	\$16,832,000	\$17,237,000
Annual Debt Service					
2005A Installment Purchase Agreement ⁽²⁴⁾⁽²⁵⁾	\$4,371,038	\$3,166,581	\$1,960,050	\$1,960,138	\$0
2012 Installment Purchase Agreement ⁽²⁴⁾	781,275	781,078	782,604	785,894	807,558
2015 Bonds ⁽²⁴⁾	0	1,073,423	2,246,700	2,246,700	4,113,600
Total Annual Debt Service	\$5,152,313	\$5,021,083	\$4,989,354	\$4,992,732	\$4,921,158
Debt Service Coverage – Net Revenues	3.82	3.54	3.23	3.37	3.50
Debt Service Coverage – Adjusted Annual Net Revenues	3.82	3.54	3.23	3.37	3.50
Adjusted Annual Net Revenue remaining after payment of Annual Debt Service	\$14,549,688	\$12,758,917	\$11,135,646	\$11,839,269	\$12,315,842

Subordinate Payments					
2008 Loan ⁽²⁴⁾	\$ 443,048	\$ 456,475	\$ 455,391	\$ 453,966	\$ 452,162
Total Subordinate Payments	\$ 443,048	\$ 456,475	\$ 455,391	\$ 453,966	\$ 452,162
Total Debt Service Coverage – Adjusted Annual Net Revenues⁽²⁶⁾	3.52	3.25	2.96	3.09	3.21
Total Debt Service Coverage – Net Revenues⁽²⁷⁾	\$14,106,640	\$12,302,442	\$10,680,255	\$11,385,303	\$11,863,680
Adjusted Annual Net Revenue available after Subordinate Payments	\$14,106,640	\$12,302,442	\$10,680,255	\$11,385,303	\$11,863,680

Source: District

- (1) Based on preliminary actual unaudited financial results through March 31, 2015, and projected results through June 30, 2015.
- (2) Fiscal Year 2016 reflects budgeted amount.
- (3) Figure for Fiscal Year 2016 reflects projected reductions in use of water in accordance with the Governor’s Executive Order. See the caption “THE ENTERPRISE- California Drought and Response” for more information on the Governor’s Executive Order and the District’s response. Revenues are projected to increase approximately 14.0% in Fiscal Year 2017, approximately 15.1% in Fiscal Year 2018, and approximately 13.5% in Fiscal year 2019 to reflect projected expiration of such order, as well as projected rate increases. See the captions “THE ENTERPRISE-The Water System-Rates and Charges” and “THE ENTERPRISE-The Water System-Water System Revenues.”
- (4) Projected to increase approximately 3.2% per annum from Fiscal Year 2017 figure. See the caption “THE ENTERPRISE-The Wastewater System-Rates and Charges” and “THE ENTERPRISE-The Wastewater System-Wastewater System Revenues.”
- (5) Projections for Fiscal years 2017 through 2019 are based on average of prior pass-through charges from SDCWA.
- (6) Projections are a recovery of certain budgeted treatment costs pursuant to contracts with the Olivenhain Municipal Water District and the Carlsbad Municipal Water District. See the caption “THE ENTERPRISE-Water System-Water Sources and Supply” for further information. Projected to increase approximately .35% in Fiscal Year 2017, approximately 2.9% in Fiscal Year 2018, and approximately 1.5% in Fiscal Year 2019.
- (7) Projections for Fiscal Year 2017 through 2019 reflect cost allocated to each pump zone, and incorporate overpayments in prior years. Projected to increase approximately 1.5% per annum for Fiscal Year 2017 and 2018, and approximately 3% in Fiscal Year 2019.
- (8) Projected based on 5 year average from Fiscal Year 2009-2014, and includes projected improvement in economic conditions.
- (9) Includes 1% property tax revenue received by the District and pass-through payments pursuant to certain pass-through agreements with dissolved redevelopment agencies. The 1% property tax is projected to increase approximately 1.25% per annum from Fiscal Year 2017. Pass-through and other payments projected at \$1,200,000 per annum.
- (10) Excludes unrealized appreciation or depreciation of investments Projected to decrease approximately 6.8% in Fiscal Year 2017, approximately 4.0% in Fiscal Year 2018 due to projected decreases to District reserves reflecting projected capital expenditures.
- (11) Projected to increase approximately 2% per annum for Fiscal years 2017 and 2018, and to decrease 16.35% in Fiscal Year 2019 reflecting fewer projected capital projects.
- (12) Includes lease payments from the City of San Marcos at \$148,000 per year. The final lease payment from the City of San Marcos is scheduled in Fiscal Year 2018.
- (13) Projected to increase approximately 4.6% in Fiscal Year 2017, 15.2% in Fiscal Year 2018, and 11.1% in Fiscal Year 2019, due to projected increases in rates charged by Olivenhain, MWD and SDCWA, and decreased demand by retail customers due to drought conditions. See the caption “THE ENTERPRISE-The Water System- Water Purchases and Demand.”
- (14) Reflects projected payments under the Uniform Contract, as provided by the operator thereof. For more information on the Uniform Contract, see the caption “THE ENTERPRISE-Water Sources and Supply.”
- (15) Projected to increase approximately 5.2% per annum in Fiscal Year 2017 and Fiscal Year 2018, and .3% in Fiscal Year 2019.
- (16) Includes Maintenance and Operation Costs for the Meadowlark Plant, the Mahr Reservoir, and the Meadowlark Lift Station. Projections include projected expenditures for equipment replacement and upgrades. Projected to decrease by 6.4% in Fiscal Year 2017, and to increase approximately 3.5% in Fiscal Year 2018 and 2019.
- (17) Excludes capital charges payable by the District to the Encina Wastewater Authority pursuant to the Joint Powers Agreement. Projected to increase 3% per annum from Fiscal Year 2017 figure.
- (18) Projected to increase 4.9% per annum from Fiscal Year 2017 through Fiscal Year 2018, and 13.1% in Fiscal Year 2019.

(Footnotes Continued on Following Page)

(Footnotes Continued from Following Page)

- (19) Projected to increase 5.7% in Fiscal Year 2017 and 6.5% in Fiscal Year 2018, and to decrease 1.4% in Fiscal Year 2019.
- (20) Projected to increase approximately 5% in Fiscal Years 2017 and 2018, and 8.5% in Fiscal Year 2019.
- (21) Includes Maintenance and Operation Costs relating to customer accounts, information technology, buildings and grounds, meter reading and repairs, tanks and reservoirs, equipment and vehicles, pumping, water quality and treatment, and other water and wastewater Maintenance and Operation Costs. Projected to increase 4.2% per annum for Fiscal Year 2017 and 2018, and 5.8% for Fiscal Year 2019.
- (22) The District does not project any transfers to the Rate Stabilization Fund.
- (23) The District does not project any transfers from the Rate Stabilization Fund.
- (24) Reflects debt service to be paid in each Fiscal Year, as required under the Master Contract, as opposed to debt service to be accrued in each fiscal year.
- (25) Reflects principal and interest with respect to the 2005A COPs through July 1, 2015, and the principal and interest with respect to the Unrefunded 2005A COPs from July 2, 2015 through July 1, 2017.
- (26) Debt service coverage ratio calculated using Adjusted Annual Net Revenues divided by Total Annual Debt Service and Total Subordinate Payments.
- (27) Debt service coverage calculated using Net Revenues divided by Total Annual Debt Service and Total Subordinate Payments.

Enterprise Financial Information

A copy of the most recent audited financial statements of the District prepared by White Nelson Diehl Evans LLP, Carlsbad, California (the “Auditor”) are included as Appendix A hereto (the “Financial Statements”). The Auditor’s letter concludes that the basic financial statements present fairly, in all material respects, the financial position of the District as of June 30, 2014, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America, as well as accounting systems prescribed by the State Controller’s Office and State Regulations governing special district. The Financial Statements should be read in their entirety. The Auditor did not consent to inclusion, nor did it participate in preparation of the Official Statement.

The summary operating results contained under the caption “Historic Enterprises Operating Results” are derived from these financial statements (excluding certain non-cash items and after certain other adjustments) and are qualified in their entirety by reference to such statements, including the notes thereto.

The basic financial statements of the District accounts have been prepared in conformity with accounting principles generally accepted in the United States of America. The Governmental Accounting Standards Board (“GASB”) is the accepted standard setting body for governmental accounting financial reporting purposes. In certain cases GAAP requires or permits moneys collected in one Fiscal Year to be recognized as revenue in a subsequent Fiscal Year and requires or permits expenses paid or incurred in one Fiscal Year to be recognized in a subsequent Fiscal Year. See APPENDIX A— VALLECITOS WATER DISTRICT FINANCIAL STATEMENTS.” Except as otherwise expressly noted herein, all financial information derived from the District’s audited financial statement reflect the application of GAAP.

District Reserves

The District has established unrestricted funds to use current Revenues to satisfy future spending plans. Pursuant to its Reserve Policy, set forth in Resolution No. 1433 adopted on November 6, 2013, the District is required to maintain: (i) two operating reserves (one for the Water System and one for the Wastewater System); (ii) an OPEB reserve; (iii) two replacement reserves (one for the Water System and one for the Wastewater System), and (iv) two rate stabilization funds (one for the Water System and one for the Wastewater System), which together constitute the Rate Stabilization Fund.

As of March 31, 2015, these unrestricted reserves were funded as follows: (i) the Water System operating reserve was funded at \$4,968,000; (ii) the Wastewater System operating reserve was funded at \$5,857,200; (iii) the OPEB reserve was funded at \$0 (OPEB monies are currently in an irrevocable trust); (iv) the Water System replacement reserve was funded at \$20,264,825, of which \$5,818,951 was restricted; (v) the

Wastewater System replacement reserve was funded at \$23,620,600, of which \$3,870,662 was restricted; (vi) the Rate Stabilization Fund for the Water System was funded at \$0; and (vii) the Rate Stabilization Fund for the Wastewater System was funded at \$0.

Each of these reserves is funded in an amount equal to or greater than the respective targeted level under the current District reserve policy.

BONDOWNERS' RISKS

Some of the events which could prevent the District from paying the principal and interest on the 2015 Bonds as they become due are summarized below. The following discussion of risks is not meant to be an exhaustive list of the risks associated with the purchase of the 2015 Bond and does not necessarily reflect the relative importance of the various risks. *In addition to the risks discussed herein, see "CONSTITUTIONAL LIMITATIONS ON APPROPRIATIONS AND CHARGES."*

Limited Recourse on Default

The District's obligations under the Indenture are not subject to acceleration following an event of default. Therefore, if the District defaults on its obligation to make payment of principal and interest on the 2015 Bonds, the 2015 Bonds may not be accelerated.

Remedies available to the owners of the 2015 Bonds in the event of a default by the District are dependent upon judicial actions, which are often subject to discretion and delay and could prove both expensive and time consuming to obtain. In addition to the specific limitations on remedies contained in the applicable documents themselves, the rights and obligations with respect to the 2015 Bonds and the Indenture are subject to bankruptcy, insolvency, reorganization, moratorium, fraudulent conveyance and other similar laws affecting creditors' rights, to the application of equitable principles if equitable remedies are sought, and to the exercise of judicial discretion in appropriate cases and to limitations on legal remedies against public agencies in the State of California. The various opinions of counsel delivered and to be delivered with respect to such documents, including the opinion of Bond Counsel (the proposed form of which is attached as Appendix C), were and are similarly qualified.

Statutory and Regulatory Impact

Laws and regulations governing treatment and delivery of water and the treatment and disposal of wastewater are enacted and promulgated by government agencies on the federal, state and local levels. Compliance with these laws and regulations may be costly, and, as more stringent standards are developed to protect both the health of consumers and the environment, these costs will likely increase. Claims against the District with respect to the Enterprise could be significant. Such claims are payable from assets of the District (including the Revenues) and from any other legally available sources.

Although the District has covenanted in the Indenture to fix, prescribe and collect rates, fees and charges for the Enterprise during each Fiscal Year which are reasonably fair and nondiscriminatory and which are estimated to yield Adjusted Annual Net Revenues for such Fiscal Year equal to at least the Coverage Requirement for such Fiscal Year, no assurance can be given that the cost of compliance with such laws and regulations will not materially adversely affect the ability of the District to generate Net Revenues in the amounts required by the Indenture and to pay principal and interest on the 2015 Bonds.

Property Tax Collections

In the Fiscal Year ended June 30, 2014, the District received approximately 2.9% of its revenues from ad valorem taxes. As a result of the approval by the voters of the State of Proposition 1A at the November 2004 statewide general election, Article XIII of the California Constitution now limits the authority of the

State to reduce the aggregate amount of ad valorem property taxes that are to be allocated to the local governmental agencies in a county. However, the State is still authorized to change the formula pursuant to which such taxes are allocated among such local governmental agencies. Thus, there can be no assurance that the District will continue to receive ad valorem property taxes in the future.

Shortage of Imported Water

The ability of the District to service its water customers is dependent upon its receipt of imported water from MWD and IID. See “THE ENTERPRISE — Water System – Water Sources and Supply” for a summary description of the various challenges MWD and IID face in continuing to supply imported water to its respective member agencies.

Seismic Considerations

The geographic area constituting the District, like all California communities, may be subject to unpredictable seismic activity. There is significant potential for destructive ground shaking during the occurrence of a major seismic event. In addition, land susceptible to seismic activity may be subject to liquefaction during the occurrence of such an event. In the event of a severe earthquake, there may be significant damage to both property and infrastructure in the District, including the Enterprise. Such an event could result in disruptions in services, a loss or contamination of groundwater supplies and significant reductions in Net Revenues of the District.

Issuance of Senior Obligations

As discussed above under the caption “SECURITY FOR THE 2015 BONDS-Additional Indebtedness-Contract Resource Obligations,” the District has reserved to itself the right to determine that its obligations under Contract Resource Obligations will be treated as “Maintenance and Operation Costs,” provided that certain conditions are satisfied. Maintenance and Operation Costs are payable from Revenues prior to the payments due with respect to the 2015 Bonds and Parity Obligations. Thus, this provision permits the District (subject to the satisfaction of the aforesaid conditions) to enter into installment purchase agreements and similar arrangements with respect to existing and/or future facilities that will be payable prior to the 2015 Bonds. Moreover, by electing to treat its obligations under a Contract Resource Obligation as Maintenance and Operation Costs, the District will be obligated under its rate covenant only to provide coverage equal to 100% the amount so designated, rather than 115% thereof, as it would have to do if the Contract Resource Obligation were treated as a Parity Obligation. Thus, the protection that would have otherwise been provided to the Owners of the 2015 Bonds from the required extra coverage will not be available. See “SECURITY FOR THE 2015 BONDS — Additional Indebtedness– Contract Resource Obligations” for a discussion of the conditions which must be satisfied in connection with the District’s determination that obligations payable under a Contract Resource Obligation will be treated as Maintenance and Operation Costs and see “SECURITY FOR THE 2015 BONDS—Rate Covenant” for a description of the District’s covenant to fix, prescribe and collect rates, fees and charges for the Enterprise.

CONSTITUTIONAL LIMITATIONS ON APPROPRIATIONS AND CHARGES

Article XIII B

The State Constitution limits the annual appropriations of the State and of any city, county, school district, authority or other political subdivision of the State to the level of appropriations of the particular governmental entity for the prior fiscal year, as adjusted for changes in the cost of living and population. The “base year” for establishing such appropriation limit is the 1978-79 fiscal year and the limit is to be adjusted annually to reflect changes in population and consumer prices. Adjustments in the appropriations limit of an entity may also be made if: (i) the financial responsibility for a service is transferred to another public entity or to a private entity; (ii) the financial source for the provision of services is transferred from taxes to other

revenues; or (iii) the voters of the entity approve a change in the limit for a period of time not to exceed four years.

Appropriations subject to Article XIII B generally include the proceeds of taxes levied by the State or other entity of local government, exclusive of certain State subventions and refunds of taxes. "Proceeds of taxes" include, but are not limited to, all tax revenues and the proceeds to an entity of government from: (a) regulatory licenses, user charges, and user fees (but only to the extent such proceeds exceed the cost of providing the service or regulation); and (b) the investment of tax revenues. Article XIII B includes a requirement that if an entity's revenues in any year exceed the amounts permitted to be spent, the excess would have to be returned by revising tax rates or fee schedules over the subsequent two years.

Certain expenditures are excluded from the appropriations limit including payments of indebtedness existing or legally authorized as of January 1, 1979, or of bonded indebtedness thereafter approved by the voters and payments required to comply with court or federal mandates which without discretion require an expenditure for additional services or which unavoidably make the providing of existing services more costly.

The District is of the opinion that the rates imposed by the District do not exceed the costs that the District reasonably bears in providing water service. The District will covenant in the Indenture that, to the fullest extent permitted by law, it will prescribe rates and charges that it reasonably expects to be sufficient to provide Net Revenues for payments under the 2015 Installment Purchase Agreement in each year.

Proposition 218

General. An initiative measure entitled the "Right to Vote on Taxes Act" (the "Initiative") was approved by the voters of the State of California in 1996. The Initiative added Article XIII C and Article XIII D to the California Constitution. According to the "Title and Summary" of the Initiative prepared by the California Attorney General, the Initiative limits "the authority of local governments to impose taxes and property-related assessments, fees and charges."

Article XIII D. Article XIII D defines the terms "fee" and "charge" to mean "any levy other than an ad valorem tax, a special tax or an assessment, imposed by an agency upon a parcel or upon a person as an incident of property ownership, including user fees or charges for a property-related service." A "property-related service" is defined as "a public service having a direct relationship to property ownership." Article XIII D further provides that reliance by an agency on any parcel map (including an assessor's parcel map) may be considered a significant factor in determining whether a fee or charge is imposed as an incident of property ownership.

Article XIII D requires that any agency imposing or increasing any property-related fee or charge must provide written notice thereof to the record owner of each identified parcel upon which such fee or charge is to be imposed and must conduct a public hearing with respect thereto. The proposed fee or charge may not be imposed or increased if a majority of owners of the identified parcels file written protests against it. As a result, if and to the extent that a fee or charge imposed by a local government for water service is ultimately determined to be a "fee" or "charge" as defined in Article XIII D, the local government's ability to increase such fee or charge may be limited by a majority protest.

In addition, Article XIII D includes a number of limitations applicable to existing fees and charges including provisions to the effect that: (i) revenues derived from the fee or charge shall not exceed the funds required to provide the property-related service; (ii) such revenues shall not be used for any purpose other than that for which the fee or charge was imposed; (iii) the amount of a fee or charge imposed upon any parcel or person as an incident of property ownership shall not exceed the proportional cost of the service attributable to the parcel; and (iv) no such fee or charge may be imposed for a service unless that service is actually used by, or immediately available to, the owner of the property in question. Property-related fees or charges based on potential or future use of a service are not permitted.

Based upon the California Court of Appeal decision in *Howard Jarvis Taxpayers Association v. City of Los Angeles*, 85 Cal. App. 4th 79 (2000), which was denied review by the State Supreme Court, it was generally believed that Article XIIIID did not apply to charges for water services that are “primarily based on the amount consumed” (i.e., metered water rates), which had been held to be commodity charges related to consumption of the service, not property ownership. The State Supreme Court ruled in *Bighorn-Desert View Water Agency v. Verjil*, 39 Cal.4th 205 (2006) (the “*Bighorn Case*”), however, that fees for ongoing water service through an existing connection were properly-related fees and charges. The State Supreme Court specifically disapproved the holding in *Howard Jarvis Taxpayers Association v. City of Los Angeles* that metered water rates are not subject to Proposition 218.

The District has complied with the notice, hearing and protest procedures in Article XIIIID with respect to its Water System rates, including those approved in October, 2013. See the caption “WATER SYSTEM—Water System Rates and Charges.”

On April 20, 2015, the California Court of Appeal, Fourth District, issued an opinion in *Capistrano Taxpayers Association, Inc. v. City of San Juan Capistrano* upholding tiered water rates under Proposition 218 provided that the tiers correspond to the actual cost of furnishing service at a given level of usage. The opinion was specific to the facts of the case, including a finding that the City of San Juan Capistrano did not attempt to calculate the actual costs of providing water at various tier levels. The District’s wastewater rates are described under the caption “THE ENTERPRISE—Wastewater System.” The District does not currently expect the decision to affect its wastewater rate structure. The District believes that its current wastewater rates comply with the requirements of Proposition 218 and expects that any future wastewater rates will comply with Proposition 218’s procedural and substantive requirements to the extent applicable thereto.

Article XIIIIC. Article XIIIIC provides that the initiative power shall not be prohibited or otherwise limited in matters of reducing or repealing any local tax, assessment, fee or charge and that the power of initiative to affect local taxes, assessments, fees and charges shall be applicable to all local governments. Article XIIIIC does not define the terms “local tax,” “assessment,” “fee” or “charge,” so it was unclear whether the definitions set forth in Article XIIIID referred to above are applicable to Article XIIIIC. Moreover, the provisions of Article XIIIIC are not expressly limited to local taxes, assessments, fees and charges imposed after November 6, 1996. On July 24, 2006, the Supreme Court held in the *Bighorn Case* that the provisions of Article XIIIIC included rates and fees charged for domestic water use. In the decision, the Court noted that the decision did not address whether an initiative to reduce fees and charges could override statutory rate setting obligations. The District does not believe that Article XIIIIC grants to the voters within the District the power to repeal or reduce the water charges in a manner which would be inconsistent with the contractual obligations of the District. However, there can be no assurance of the availability of particular remedies adequate to protect the beneficial owners of the 2015 Bonds. Remedies available to beneficial owners of the 2015 Bonds in the event of a default by the District are dependent upon judicial actions which are often subject to discretion and delay and could prove both expensive and time-consuming to obtain.

In addition to the specific limitations on remedies contained in the applicable documents themselves, the rights and obligations with respect to the 2015 Bonds and the Indenture are subject to bankruptcy, insolvency, reorganization, moratorium, fraudulent conveyance and other similar laws affecting creditors’ rights, to the application of equitable principles if equitable remedies are sought, and to the exercise of judicial discretion in appropriate cases and to limitations on legal remedies against public agencies in the State. The various opinions of counsel to be delivered with respect to such documents, including the opinion of Bond Counsel (the form of which is attached as Appendix C), will be similarly qualified.

The District believes that its current water rates and other property-related charges comply with the requirements of Proposition 218 and expects that any increases in current rates and charges or the adoption of any new future water rates and other property-related charges will be subject to compliance with Proposition 218’s procedural and substantive requirements to the extent applicable thereto.

Proposition 26

On November 2, 2010, voters in the State approved Proposition 26. Proposition 26 amends Article XIII C to expand the definition of “tax” to include “any levy, charge, or exaction of any kind imposed by a local government” except the following: (1) a charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit or granting the privilege; (2) a charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product; (3) a charge imposed for the reasonable regulatory costs to a local government for issuing licenses and permits, performing investigations, inspections, and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof; (4) a charge imposed for entrance to or use of local government property, or the purchase, rental, or lease of local government property; (5) a fine, penalty, or other monetary charge imposed by the judicial branch of government or a local government, as a result of a violation of law; (6) a charge imposed as a condition of property development; and (7) assessments and property-related fees imposed in accordance with the provisions of Article XIII D. Proposition 26 provides that the local government bears the burden of proving by a preponderance of the evidence that a levy, charge, or other exaction is not a tax, that the amount is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor’s burdens on, or benefits received from, the governmental activity. The District does not believe that the enactment of Proposition 26 affects its ability to charge for its water service.

Future Initiatives

Articles XIII B, XIII C and XIII D were adopted as measures that qualified for the ballot pursuant to the State’s initiative process. From time to time other initiatives could be proposed and adopted affecting the District’s revenues or ability to increase revenues.

APPROVAL OF LEGAL PROCEEDINGS

The valid, legal and binding nature of the 2015 Bonds is subject to the approval of Sidley Austin LLP, acting as Bond Counsel. The form of such legal opinion is attached hereto as Appendix C, and such legal opinion will be attached to each 2015 Bond. Bond Counsel expresses no opinion as to the accuracy, completeness or fairness of this Official Statement or other offering materials relating to the 2015 Bonds and expressly disclaims any duty to advise the Owners of the 2015 Bonds as to matters related to this Official Statement.

Certain legal matters will be passed upon for the District by The Law Offices of Jeffrey G. Scott, San Diego, California, General Counsel to the District, and by Stradling Yocca Carlson & Rauth, a Professional Corporation, as Disclosure Counsel, and for the Trustee by its counsel. The Underwriter is being represented by its counsel Ballard Spahr LLP.

Payment of the fees of Bond Counsel, Disclosure Counsel, and Underwriter’s Counsel is contingent upon the issuance of the 2015 Bonds.

TAX MATTERS

General

In the opinion of Sidley Austin LLP, San Francisco, California, Bond Counsel, based on existing statutes, regulations, rulings and judicial decisions and assuming compliance by the District with certain covenants in the Master Contract and the Indenture, and requirements of the Internal Revenue Code of 1986, as amended (the “Code”), regarding the use, expenditure and investment of proceeds of the 2015 Bonds and the

timely payment of certain investment earnings to the United States, interest on the 2015 Bonds is not includable in the gross income of the owners of the 2015 Bonds for federal income tax purposes. Failure to comply with such covenants and requirements may cause interest on the 2015 Bonds to be included in gross income retroactively to the date of issuance of the 2015 Bonds.

In the further opinion of Bond Counsel, interest on the 2015 Bonds is not treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals and corporations. Interest on the 2015 Bonds, however, is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation's alternative minimum tax liability.

Ownership of, or the receipt or accrual of interest on, tax-exempt obligations may result in collateral tax consequences to certain taxpayers, including, without limitation, financial institutions, property and casualty insurance companies, certain foreign corporations doing business in the United States, certain S corporations with excess passive income, individual recipients of Social Security or Railroad Retirement benefits, taxpayers that may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations and taxpayers who may be eligible for the earned income tax credit. Bond Counsel expresses no opinion with respect to any collateral tax consequences and, accordingly, prospective purchasers of the 2015 Bonds should consult their tax advisors as to the applicability of any collateral tax consequences.

Certain requirements and procedures contained or referred to in the Master Contract and the Indenture may be changed, and certain actions may be taken or not taken, under the circumstances and subject to the terms and conditions set forth in such documents, upon the advice or with the approving opinion of counsel nationally recognized in the area of tax-exempt obligations. Bond Counsel expresses no opinion as to the effect of any change to any document pertaining to the 2015 Bonds or of any action taken or not taken where such change is made or action is taken or not taken without our approval or in reliance upon the advice of counsel other than Sidley Austin LLP with respect to the exclusion from gross income of the interest on the 2015 Bonds for federal income tax purposes.

Original Issue Discount

The initial public offering price of certain of the 2015 Bonds (the "Discount Bonds") is less than the principal amount of the Discount Bonds. The difference between the principal amount of a Discount Bond and its initial public offering price is original issue discount. Original issue discount on a Discount Bond accrues over the term of such Discount Bond at a constant interest rate. To the extent it has accrued, original issue discount on a Discount Bond is treated as interest excludable from gross income for federal income tax purposes under the conditions and limitations described above. The amount of original issue discount that accrues on a Discount Bond in each year is not an item of tax preference for purposes of calculating federal alternative minimum taxable income, but is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation's alternative minimum tax liability. Additionally, such accrued original issue discount is taken into account in determining the distribution requirements of certain regulated investment companies. Consequently, owners of Discount Bonds should be aware that the accrual of original issue discount in each year may result in an alternative minimum tax liability, additional distribution requirements or other collateral federal income tax consequences although the owner may not have received cash in such year.

The accrual of original issue discount on a Discount Bond will increase the owner's adjusted basis in such Discount Bond. This will affect the amount of taxable gain or loss realized by the owner of the Discount Bond upon the redemption, prepayment, sale or other disposition of such Discount Bond. The effect of the accrual of original issue discount on the federal income tax consequences of a redemption, prepayment, sale or other disposition of a Discount Bond that is not purchased at the initial public offering price may be determined according to rules that differ from those described above. Owners of Discount Bonds should consult their tax advisors with respect to the precise determination for federal income tax purposes of the

amount of original issue discount that properly accrues with respect to the Discount Bonds, other federal income tax consequences of owning and disposing of the Discount Bonds and any state and local tax consequences of owning and disposing of the Discount Bonds.

Original Issue Premium

The excess, if any, of the tax adjusted basis of 2015 Bonds purchased as part of the initial public offering to a purchaser (other than a purchaser who holds such 2015 Bonds as inventory, stock in trade or for sale to customers in the ordinary course of business) over the amount payable at maturity is “bond premium.” Bond premium is amortized over the term of such 2015 Bonds for federal income tax purposes (or, in the case of a 2015 Bond with bond premium callable prior to its stated maturity, the amortization period and yield may be required to be determined on the basis of an earlier call date that results in the lowest yield on such 2015 Bond). Owners of 2015 Bonds with bond premium are required to decrease their adjusted basis in such 2015 Bonds by the amount of amortizable bond premium attributable to each taxable year such 2015 Bonds are held. The amortizable bond premium on such 2015 Bonds attributable to a taxable year is not deductible for federal income tax purposes. Owners of 2015 Bonds sold with bond premium should consult their tax advisors with respect to the determination for federal income tax purposes of the treatment of bond premium upon sale or other disposition of such 2015 Bonds and with respect to the state and local tax consequences of owning and disposing of such 2015 Bonds.

Information Reporting and Backup Withholding

Interest paid on tax-exempt obligations is subject to information reporting in a manner similar to interest paid on taxable obligations. While this reporting requirement does not, by itself, affect the excludability of interest from gross income for federal income tax purposes, the reporting requirement causes the payment of interest on the 2015 Bonds to be subject to backup withholding if such interest is paid to beneficial owners that (a) are not “exempt recipients,” and (b) either fail to provide certain identifying information (such as the beneficial owner’s taxpayer identification number) in the required manner or have been identified by the IRS as having failed to report all interest and dividends required to be shown on their income tax returns. Generally, individuals are not exempt recipients, whereas corporations and certain other entities are exempt recipients. Amounts withheld under the backup withholding rules from a payment to a beneficial owner are allowed as a refund or credit against such beneficial owner’s federal income tax liability so long as the required information is furnished to the IRS.

State Tax Exemption

In the further opinion of Bond Counsel, interest on the 2015 Bonds is exempt from personal income taxes imposed by the State of California.

Future Developments

Future or pending legislative proposals, if enacted, regulations, rulings or court decisions may cause interest on the 2015 Bonds to be subject, directly or indirectly, to federal income taxation or to state or local income taxation, or may otherwise prevent beneficial owners from realizing the full current benefit of the tax status of such interest. Legislation or regulatory actions and future or pending proposals may also affect the economic value of the federal or state tax exemption or the market value of the 2015 Bonds. Prospective purchasers of the 2015 Bonds should consult their tax advisors regarding any future, pending or proposed federal or state tax legislation, regulations, rulings or litigation as to which Bond Counsel expresses no opinion.

For example, various proposals have been made in Congress and by the President (the “Proposed Legislation”), which, if enacted, would subject interest on bonds that is otherwise excludable from gross income for federal income tax purposes, including interest on the 2015 Bonds, to a tax payable by certain bondholders with adjusted gross income in excess of thresholds specified in the Proposed Legislation. It is

unclear if the Proposed Legislation will be enacted, whether in its current or an amended form, or if other legislation that would subject interest on the 2015 Bonds to a tax or cause interest on the 2015 Bonds to be included in the computation of a tax, will be introduced or enacted. Prospective purchasers should consult their tax advisors as to the effect of the Proposed Legislation, if enacted, in its current form or as it may be amended, or such other legislation on their individual situations.

A copy of the proposed form of opinion of Bond Counsel is attached hereto as Appendix C.

FINANCIAL ADVISOR

The District has retained Fieldman, Rolapp & Associates, Irvine, California, as financial advisor (the “Financial Advisor”) in connection with the issuance of the 2015 Bonds. The Financial Advisor has not undertaken to make an independent verification or to assume responsibility for the accuracy, completeness, or fairness of the information contained in this Official Statement. The fees being paid to the Financial Advisor are contingent upon the issuance of the 2015 Bonds.

The Financial Advisor is an independent advisory firm and is not engaged in the business of underwriting, trading or distributing municipal or other public securities.

RATINGS

The District expects that S&P and Fitch will assign the 2015 Bonds the rating of “AA+” and “AA+”, respectively. There is no assurance that any credit rating given to the 2015 Bonds will be maintained for any period of time or that the ratings may not be lowered or withdrawn entirely by S&P or Fitch if, in the judgment of S&P or Fitch, as applicable, circumstances so warrant. Any downward revision or withdrawal of such ratings may have an adverse effect on the market price of the 2015 Bonds. Such ratings reflect only the views of S&P and Fitch, and an explanation of the significance of such ratings may be obtained from S&P and Fitch.

The District has covenanted in a Continuing Disclosure Agreement to file on EMMA, notices of any ratings changes on the 2015 Bonds. See the caption “CONTINUING DISCLOSURE” below and Appendix E—“FORM OF CONTINUING DISCLOSURE AGREEMENT.” Notwithstanding such covenant, information relating to ratings changes on the 2015 Bonds may be publicly available from the rating agencies prior to such information being provided to the District and prior to the date the District is obligated to file a notice of rating change on EMMA. Purchasers of the 2015 Bonds are directed to the ratings agencies and their respective websites and official media outlets for the most current ratings changes with respect to the 2015 Bonds after the initial issuance of the 2015 Bonds. Both S&P and Fitch currently submit rating changes to EMMA.

UNDERWRITING

The 2015 Bonds will be purchased by Citigroup Global Markets Inc. (the “Underwriter”), pursuant to a Purchase Contract, dated June 11, 2015 (the “Purchase Contract”), by and between the District and the Underwriter. Under the Purchase Contract, the Underwriter has agreed to purchase all, but not less than all, of the 2015 Bonds for an aggregate purchase price of \$52,550,953.60 (representing the principal amount of the 2015 Bonds, less an Underwriter’s discount of \$63,436.05, plus an original issue premium of \$7,299,389.65). The Purchase Contract provides that the Underwriter will purchase all of the 2015 Bonds if any are purchased, the obligation to make such a purchase being subject to certain terms and conditions set forth in the Purchase Contract, the approval of certain legal matters by counsel and certain other conditions.

The initial public offering prices stated on the inside front cover of this Official Statement may be changed from time to time by the Underwriter. The Underwriters may offer and sell the 2015 Bonds to certain dealers (including dealers depositing 2015 Bonds into investment trusts), dealer banks, banks acting as agents and others at prices lower than said public offering prices.

The Underwriter has entered into a retail distribution agreement with each of TMC Bonds L.L.C. (“TMC”) and UBS Financial Services Inc. (“UBSFS”). Under these distribution agreements, Citigroup Global Markets Inc. may distribute municipal securities to retail investors through the financial advisor network of UBSFS and the electronic primary offering platform of TMC. As part of this arrangement, the Underwriter may compensate TMC (and TMC may compensate its electronic platform member firms) and UBSFS for their selling efforts with respect to the 2015 Bonds.

The Underwriter and its affiliates are full service financial institutions engaged in various activities, which may include securities trading, commercial and investment banking, financial advisory, investment management, principal investment, hedging, financing and brokerage activities. The Underwriter and its affiliates have, from time to time, performed, and may in the future perform, various investment banking services for the District for which they received or will receive customary fees and expenses. In addition, certain affiliates of the Underwriter are lenders, and in some cases agents or managers for the lenders, under credit and liquidity facilities.

In the ordinary course of their various business activities, the Underwriter and its respective affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (which may include bank loans and/or credit default swaps) for their own account and for the accounts of their customers and may at any time hold long and short positions in such securities and instruments. Such investment and securities activities may involve securities and instruments of the District.

CONTINUING DISCLOSURE UNDERTAKING

The District has covenanted in a Continuing Disclosure Agreement dated the date of execution and delivery of the 2015 Bonds (the “Continuing Disclosure Agreement”) to provide annually certain financial information and operating data relating to the District by not later than 270 days following the end of its Fiscal Year (commencing with Fiscal Year 2015) including the audited Financial Statements of the District for each such Fiscal Year (together, the “Annual Report”), and to provide notices of the occurrence of certain other enumerated events.

The Annual Report will be filed by the District with the Municipal Securities Rulemaking Board’s Electronic Municipal Market Access System for municipal securities disclosures, maintained on the Internet at <http://emma.msrb.org/> (“EMMA”). The notices of enumerated events will be filed by the District with EMMA. The form of the Continuing Disclosure Certificate is attached hereto at Appendix E.

In the past five years, the District has been subject to certain continuing disclosure undertakings previously entered into with respect to the 2005A COPs (the “Prior Continuing Disclosure Undertaking”). Pursuant to the Prior Continuing Disclosure Undertaking, the District agreed to file its audited financial reports, certain operating data, notices of certain enumerated events and notices of the occurrence of certain other enumerated events, if material.

The District filed its 2013 Annual Report twelve days after the date required under the Prior Continuing Disclosure Undertaking, and filed the 2013 audited financial statements with the Bloomberg Municipal Repository instead of EMMA. Additionally, the District did not timely file notice of a change to the rating of the insurer of the 2005A COPs, which occurred on October 25, 2010. On June 2, 2015, the District filed the 2013 audited financial statements with EMMA and the notice of the aforementioned rating change. Other than the rating change of the insurer of the 2005A COPs described in this paragraph, the District is not aware of any events in the last five years which may have required the filing of significant event notices under the Prior Continuing Disclosure Undertaking that were not filed.

APPENDIX A

VALLECITOS WATER DISTRICT FINANCIAL STATEMENTS

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ANNUAL FINANCIAL REPORT
WITH REPORT ON AUDIT BY INDEPENDENT
CERTIFIED PUBLIC ACCOUNTANTS
JUNE 30, 2014

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Vallecitos Water District
San Marcos, California

We have audited the basic financial statements of the Vallecitos Water District (the District) as of and for the year ended June 30, 2014, and the related notes to the basic financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the State Controller's Minimum Audit Requirements for California Special Districts. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the District's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the Vallecitos Water District as of June 30, 2014 and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America, as well as the accounting systems prescribed by the State Controller's Office and State Regulations governing Special Districts.

Other Matters:**Summarized Comparative Information**

We have previously audited the Vallecitos Water District's 2013 financial statements, and our report dated November 25, 2013, expressed an unmodified opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2013, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and schedule of funding progress for OPEB, as identified in the accompanying table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during the audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Matters (Continued):

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the District's basic financial statements. The supplementary information, as identified in the accompanying table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated in all material respects in relation to the basic financial statements as a whole.

White Nelson Dick Evans LLP

Carlsbad, California
November 6, 2014

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal Year Ended June 30, 2014

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, 2014. 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; current-to-prior year analysis; discussion on restrictions, commitments and limitations; and discussion on significant activity involving capital assets and long-term debt.

FINANCIAL HIGHLIGHTS

During the fiscal year ended June 30, 2014 (2013/14), the following highlights impacted, or have the potential to impact, the finances of the District.

- Total reserves increased by \$7.4 million during 2013/14 primarily from transfers from operations (revenues in excess of expenses).
- Overall revenues increased \$4 million primarily due to increased water sales and ready-to-serve charges while expenses increased by \$0.4 million.
- Capital Facility Fees received and accounted for in the capacity fund (restricted for projects that increase capacity) were \$2.4 million as compared to \$7.3 million the prior year. The capacity fund deficit increased by \$4 million to \$7.7 million. However, the number of residential living units permitted by the City of San Marcos continues to increase: 407 in 2011, 561 in 2012, 817 in 2013.
- Capital spending increased to \$8.9 million from \$8.2 million in the prior year. Of the \$8.9 million, \$4.1 million was funded from debt proceeds received the prior year. The remainder was cash funded.
- Effective January 1, 2014, the wholesale cost per acre foot of treated water increased by 4%. Fixed wholesale costs increased 5.2%. The cost of water increased by \$2.2 million and purchases increased by 470 acre feet (3%) during the fiscal year.
- Overall non-current liabilities decreased by \$2.7 million as the District continues to reduce the principal balances on all debt. The District paid \$5.6 million in debt service compared to \$4.8 million in 2012/13.
- For the second year in a row, results of operations fully funded depreciation. Fiscal Year 2013/14 resulted in positive operating income.
- On June 18, 2014, the Board of Directors adopted the District budget for 2014/15 which anticipates increases in water rates charged by the District's wholesaler the San Diego County Water Authority. The increase in budgeted water purchases is \$766,000. Other than water purchases, the operating budget increased by \$368,000 from fiscal year 2013/14 due to outreach efforts related to the drought along with other miscellaneous increases. The 2014/15 budget reflects \$2.7 million less in capital expenditures during the budget year than the previous budget year.

VALLECITOS WATER DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

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.

Statement of Net Position

The Statement of Net Position presents the District's financial position (assets and liabilities) as of June 30, 2014. Assets in excess of liabilities (Net Position) are \$256,108,804 (compared to \$249,751,418 as of June 30, 2013). 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 recorded at fair value or developers' construction cost.

Statement of Revenues, Expenses, and Changes in Net Position

The Statement of Revenues, Expenses, and Changes in Net Position presents the District's results of operations for the year ended June 30, 2014. 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 treatment and disposal services, and processing and delivering recycled water). Non-operating revenues and expenses (e.g. investment income and interest expense) are not directly related to the core activities of the District. Operating income for the year ended June 30, 2014, of \$2,574,786 is combined with a net non-operating gain of \$779,700 and capital contributions of \$3,002,900 to arrive at an increase in net position of \$6,357,386. The increase in net position is added to beginning net position of \$249,751,418 to arrive at ending net position of \$256,108,804 as of June 30, 2014.

	2013/14	2012/13
Operating Income	\$ 2,574,786	\$ 1,075,415
Nonoperating revenues / (expenses)	779,700	(1,357,436)
Capital contributions	3,002,900	8,484,563
Change in net position	6,357,386	8,202,542
Total Net Position, Beginning of Year	249,751,418	241,548,876
Total Net Position, End of Year	<u>\$ 256,108,804</u>	<u>\$ 249,751,418</u>

Statement of Cash Flows

The Statement 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, 2014, is the increase in cash and cash equivalents of \$2,243,979, which is combined with beginning cash and cash equivalents of \$15,368,268 to arrive at ending cash and cash equivalents of \$17,612,247. Investments in the California Local Agency Investment Fund, San Diego County Investment Pool, and open-ended money market mutual funds, are the only cash equivalents held by the District as of June 30, 2014.

Beginning cash & cash equivalents	\$ 15,368,268
Increase in cash & cash equivalents	2,243,979
Ending cash & cash equivalents	<u>\$ 17,612,247</u>

VALLECITOS WATER DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

OVERVIEW OF THE FINANCIAL STATEMENTS (continued)

As of June 30, 2014, the ending cash and cash equivalents are represented on the Statement of Net Position as follows:

	2013/14	2012/13
Unrestricted cash & cash equivalents	\$ 14,592,877	\$ 8,105,509
Cash & cash equivalents restricted - current	3,019,370	7,262,759
Total cash & cash equivalents	<u>\$ 17,612,247</u>	<u>\$ 15,368,268</u>

ANALYSIS OF FINANCIAL POSITION AND RESULTS OF OPERATIONS

During the fiscal year ended June 30, 2014, the increase in total assets of \$4,349,785 and the decrease in total liabilities of \$2,007,601 resulted in an increase in net position of \$6,357,386.

Operating activities, capital facility fees, property taxes, and other sources helped fund \$8.9 million in capital acquisitions and construction, and \$5.6 million in debt service. The following table summarizes how these capital projects and debt service were financed during the year.

Vallecitos Water District - Sources and Uses of Cash & Investments <i>in millions</i>			
	2013/14	2012/13	2011/12
Sources:			
Operating activities	\$ 12.6	\$ 9.6	\$ 4.5
Property tax	3.1	4.4	3.3
Capital facility fees	2.4	7.3	4.8
Bond proceeds	-	7.1	-
Investment earnings & other receipts	0.7	0.3	0.2
Uses:			
Capital construction and acquisition	(8.9)	(8.2)	(6.1)
Debt service	(5.6)	(4.8)	(4.8)
Increase in cash and investments	<u>\$ 4.3</u>	<u>\$ 15.7</u>	<u>\$ 1.9</u>

CURRENT-TO-PRIOR YEAR ANALYSIS

Analysis of Net Position

The overall increase in net position noted in the table below is primarily attributed to results of operating activities, contributed capital, debt proceeds, and property tax received.

Vallecitos Water District's Net Position				
	2013/14	2012/13	Change	
			Amount	%
Cash and investments	\$ 43,499,742	\$ 39,157,244	\$ 4,342,498	11.1%
Capital assets	280,412,693	277,583,823	2,828,870	1.0%
Other assets	11,163,202	13,984,785	(2,821,583)	-20.2%
Total Assets	<u>335,075,637</u>	<u>330,725,852</u>	<u>4,349,785</u>	1.3%
Current liabilities	13,061,890	12,345,952	715,938	5.8%
Noncurrent liabilities	65,904,943	68,628,482	(2,723,539)	-4.0%
Total Liabilities	<u>78,966,833</u>	<u>80,974,434</u>	<u>(2,007,601)</u>	-2.5%
Net Position				
Net investment in capital assets	211,842,759	210,637,696	1,205,063	0.6%
Restricted	1,645,172	1,536,415	108,757	7.1%
Unrestricted	42,620,873	37,577,307	5,043,566	13.4%
Total Net Position	<u>\$ 256,108,804</u>	<u>\$ 249,751,418</u>	<u>\$ 6,357,386</u>	2.5%

VALLECITOS WATER DISTRICT

MANAGEMENT’S DISCUSSION AND ANALYSIS (Continued)

CURRENT-TO-PRIOR YEAR ANALYSIS (Continued)

Analysis of Net Position (continued)

- Cash and investments increased by \$4.3 million during the fiscal year 13/14. The increase is attributable to \$12.6 million in operating activities, \$6.2 million in property tax, capital facility fees and other receipts offset by capital expenditures and debt service as illustrated in the Sources and Uses table on the previous page.
- Other assets decreased significantly due to receiving a one-time reimbursement of capital paid toward the Phase V expansion at the Encina Wastewater Authority (EWA). The remaining balance reflects traditional receivables.
- Total liabilities decreased with the payment of principal on outstanding debt.

Selected Financial Ratios:

Vallecitos Water District Selected Financial Ratios		
	2013/14	2012/13
Current ratio	4.05	4.12
Quick ratio	3.90	3.98
Days of operations in cash	339	281
Capital assets-to-Long-term liabilities	4.25 / 1	4.04 / 1
Debt-to-equity	1 / 3.24	1 / 3.08

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 4.05 times its current debt from current assets. However, some current assets are not easily, or will 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 3.90 times its current obligations with assets readily convertible to cash. The District’s current and quick ratios show a high degree of solvency and a strong current position. The days of operations in cash is a common measure scrutinized by the investment community. It measures the number of days the District can operate without any cash inflow. The District’s goal is 308 days of operations in cash. The capital-assets-to-long-term-liabilities ratio indicates that for every dollar of debt the District has \$4.25 in capital assets (infrastructure, land, building, vehicles, equipment, furniture, etc., net of depreciation). The significantly higher numerator in this ratio and the higher denominator in 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 \$3.24 of net position (equity). The decreases in the current and quick ratios mixed with the increases in capital assets to long-term liabilities and debt to equity ratio, demonstrates the District is investing in long-term assets and building equity.

Analysis of Revenues and Expenses

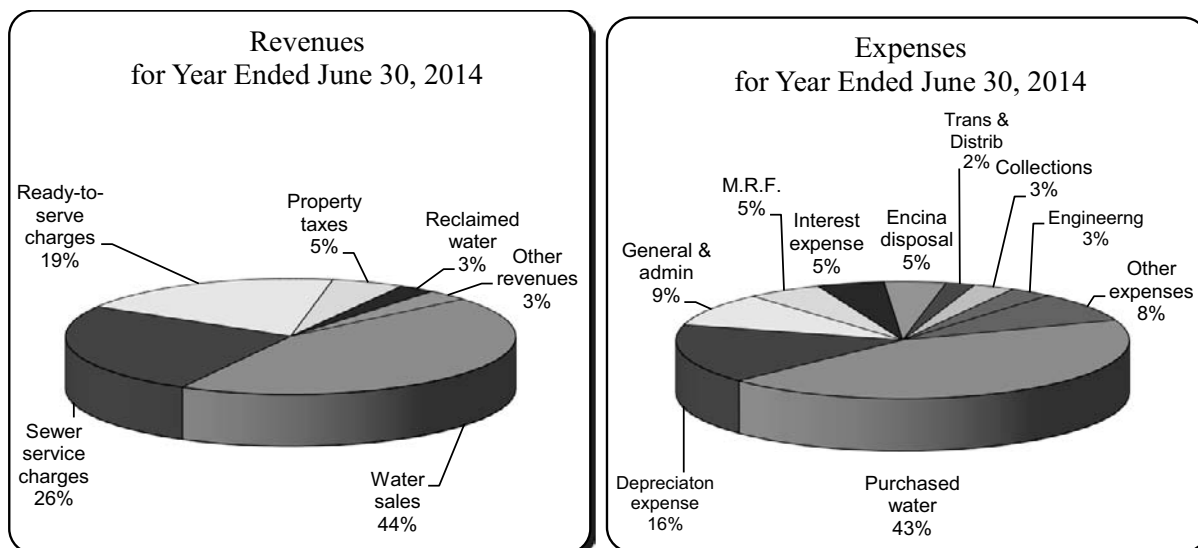
The composition of revenues and expenses for the 2013/14 fiscal year is illustrated in the following graphs. Water sales, ready-to-serve charges, and wastewater service charges continue to be the main sources of revenue funding District operations. Water sales are commodity charges assessed to cover 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.

Deductions from revenue to arrive at the operating income of \$2,574,786 include non-cash depreciation and amortization expense of \$9,160,497. Depreciation is the systematic allocation of a capital asset’s cost to expense over a specified period of time. The District has established reserve floors and ceilings for the replacement of aging infrastructure.

VALLECITOS WATER DISTRICT

MANAGEMENT’S DISCUSSION AND ANALYSIS (Continued)

CURRENT-TO-PRIOR YEAR ANALYSIS (Continued)



A comparative analysis of revenues, expenses and discussion of variances between fiscal years are presented below.

Vallecitos Water District's Revenues and Expenses				
	For Fiscal Year:		Change	
	2013/14	2012/13	Amount	%
Water sales	\$ 26,031,460	\$ 23,364,573	\$ 2,666,887	11.4%
Wastewater service charges	15,128,763	14,921,894	206,869	1.4%
Ready-to-serve charges	11,484,584	10,638,282	846,302	8.0%
Property taxes	3,077,966	3,519,081	(441,115)	-12.5%
Reclaimed water sales	1,533,203	1,718,013	(184,810)	-10.8%
Other revenues	1,812,762	915,889	896,873	97.9%
Total Revenues	59,068,738	55,077,732	3,991,006	7.2%
Purchased water	24,145,579	21,982,845	2,162,734	9.8%
Depreciation expense	9,160,497	8,955,355	205,142	2.3%
General and administrative	5,173,986	4,879,580	294,406	6.0%
Meadowlark Reclamation Facility (M.R.F.)	2,993,578	2,777,837	215,741	7.8%
Interest expense	2,672,296	2,758,728	(86,432)	-3.1%
Encina disposal	2,450,330	2,709,307	(258,977)	-9.6%
Engineering	1,698,699	1,703,359	(4,660)	-0.3%
Collections	1,632,347	1,633,839	(1,492)	-0.1%
Transmission & Distribution	1,154,882	1,068,907	85,975	8.0%
Other expenses	4,632,058	6,889,996	(2,257,938)	-32.8%
Total Expenses	55,714,252	55,359,753	354,499	0.6%
Net Income/(Loss) before contributions	3,354,486	(282,021)	3,636,507	1289.4%
Capital contributions	3,002,900	8,484,563	(5,481,663)	-64.6%
Change in Net Position	6,357,386	8,202,542	(1,845,156)	-22.5%
Total Net Position at Beginning of Year	249,751,418	241,548,876	8,202,542	3.4%
Total Net Position, End of Year	<u>\$ 256,108,804</u>	<u>\$ 249,751,418</u>	<u>\$ 6,357,386</u>	<u>2.5%</u>

VALLECITOS WATER DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

CURRENT-TO-PRIOR YEAR ANALYSIS (Continued)

- Water sales and Ready-to-serve changes are due to increases in the tier 1 water commodity rate of 39¢ per unit and \$2.13 monthly increase per single family residence Ready-to-Serve. Each rate increase took effect during fiscal year 2013/14.
- The District received \$1.4 million in property taxes from discontinued Redevelopment Agencies in fiscal year 13/14. A decrease of \$522,052 from the prior year mixed with an increase of \$80,937 in the 1% tax to arrive at the net decrease of \$441,115. The District anticipates receipts from discontinued Redevelopment Agencies to decrease in subsequent years.
- Other revenues increase is due to new annexations, investment income received, investment market valuation increases, recovery of damaged property and other miscellaneous fees and receipts.
- The purchased water increase was anticipated and offset with the rate increases mentioned above.
- The Encina disposal expense decrease is the result of fiscal year 2012/13's reconciliation of joint facility operating expenses. The prior year's reconciliation was a one time "true-up" adjustment and fiscal year 2013/14's expense reflects normal operating costs.
- Net other expenses decreased significantly due to prior year's accounting adjustments of the Investment in Encina Wastewater Authority (\$1.7 million) and implementation of a new overhead absorption rate (\$563,005) in fiscal year 2013/14.
- Capital contributions decreased in comparison to fiscal year 2012/13. Fiscal year 2012/13 capital contributions rose significantly as new and additional capacity was purchased by developers. Fiscal year 2013/14 is representative of the trend prior to 2012/13's spike.

RESTRICTIONS, COMMITMENTS, AND LIMITATIONS

The District's net revenue requirement is 1.15 times the total debt service of the District. The District's 2013/14 net revenue was 3.11 times debt service. Debt per capital within the District is \$648 exclusive of other debt such as San Diego County Water Authority and Metropolitan Water District.

2012 Certificates of Participation

In December 2012, the District received \$7.1 million in proceeds as the Board of Directors executed the 2nd Installment Purchase Agreement of the Master Agreement of the 2005 Certificates of Participation. The proceeds were used toward the following sewer projects: San Marcos Interceptor, Linda Vista, Encina Land Parallel Outfall and Rock Springs. The District pays debt service semi-annually on the certificates issued at a fixed rate of 1.98%. Interest payments are due each April and October 1st and principal is due each October 1st. Total debt service paid in fiscal year 13/14 related to the COPs was \$779,195. The outstanding principal balance at June 30, 2014, is \$6.5 million.

2008 Union Bank Tax-Exempt Private Placement Loan

On November 12, 2008, the District received \$7.9 million in proceeds from a variable rate tax-exempt private placement loan from Union Bank of California to fund a portion of EWA's treatment plant expansion. The District's share in solids capacity at EWA increased from 7.5 million gallons per day (MGD) to 10.5 MGD. The variable rate on the loan is indexed to LIBOR with the District's option to periodically change the LIBOR period and associated rate (adjusted by the bank's formula for a tax-exempt borrowing) currently at 1.00292%. Principal payments of \$200,000 are due every March 31st and September 30th. Interest payments are due at the end of the LIBOR period chosen by the District. Total debt service paid in fiscal year 13/14 related to the loan was \$449,547. The outstanding principal balance at June 30, 2014, of \$5.8 million is subordinate to existing certificates of participation.

VALLECITOS WATER DISTRICT

MANAGEMENT’S DISCUSSION AND ANALYSIS (Continued)

RESTRICTIONS, COMMITMENTS, AND LIMITATIONS (continued)

2005 Certificates of Participation

The District pays debt service semi-annually on certificates issued as variable-rate in 2005 and converted to a fixed rate of 4.736% (total-all-in-cost) in 2007. The January 1st payment of interest only was \$1.4 million and the July 1st principal and interest payment is \$3 million. Total debt service paid in fiscal year 13/14 related to the loan was \$4.4 million. The outstanding principal balance at June 30, 2014, is \$55.4 million.

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 capital budget. As of June 30, 2014, the water capacity fund had a deficit of \$5,308,364 and the sewer capacity had a deficit of \$2,384,466. (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 2014/15:

Project Description	2014/15 Budget	Spent Through	
		June 30, 2014	Remaining
Encina Land Parallel Outfall	\$ 28,150,000	\$ 138,880	\$ 28,011,120
San Marcos interceptor sewer line	18,650,000	12,891,967	5,758,033
Meadowlark Tank #3	4,434,000	488,961	3,945,039
Mountain Belle pump station and pipeline	3,860,000	99,350	3,760,650
Linda Vista Sewer East	2,750,000	620,150	2,129,850
MRF Solids Force Main Replacement	1,750,000	224,003	1,525,997
Rock Springs Sewer Replacement	1,595,000	259,256	1,335,744

The budget amounts in the previous table 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 construction has not yet been through the bidding process. Construction of the land outfall, Meadowlark tank, and Mountain Bell project will not commence unless there is significantly more growth than anticipated. Details are provided in the District’s 2014-15 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 additions to capital assets which were largely the result of reclassifying construction-in-progress to capital assets placed in service and depreciated.

Tank refurbishment	\$ 760,835
Vehicles	564,957
Water mains, service lines, meters, valves & fire hydrants	556,164
Sewer mains, manholes, and cleanouts	526,275
Treatment equipment	326,202

The \$55.4 million in re-issued COPs, the \$5.8 million loan and the \$6.5 million COPS balance are the only long-term debts owed by the District as of June 30, 2014.

VALLECITOS WATER DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

The District considered the following economic factors in establishing 2014/15 budget amounts:

- Increases to wholesale water rates as the Carlsbad desalination plant comes closer to becoming operational
- Continued drought conditions throughout the state,
- Slow but steady recovery in construction,
- Increasing regulatory compliance

As a result of these factors, the 2014/15 budget includes:

- A smooth rate ramp to absorb the increase of the Carlsbad desalination plant
- Water sales reflective of drought conservation efforts by customers,
- Staffing level increases from the 2013/14 budget as previously vacant positions are filled and reorganizations occur.

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.

VALLECITOS WATER DISTRICTSTATEMENTS OF NET POSITION
June 30, 2014
(with prior year data for comparison only)

	<u>2014</u>	<u>2013</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 14,592,877	\$ 8,105,509
Restricted cash and cash equivalents	3,019,370	7,262,759
Investments	25,887,495	23,788,976
Accounts Receivable:		
Water and wastewater sales and services, net	6,104,834	6,754,459
Taxes and assessments	99,417	95,430
From other governmental entities	735,270	2,509,923
Other	378,713	449,973
Accrued interest receivable	66,365	70,677
Current portion of note receivable	120,203	113,936
Inventories	1,115,354	975,560
Prepaid expenses	793,370	747,869
Total current assets	<u>52,913,268</u>	<u>50,875,071</u>
Non-current assets:		
Restricted capital facility fees receivable	56,412	22,985
Note receivable from City of San Marcos, net of current portion	401,745	521,947
Prepaid PERS contribution	1,291,519	1,722,026
Investment in Encina Wastewater Authority capital assets	34,161,875	32,850,882
Capital assets not being depreciated	24,315,510	17,253,705
Net capital assets being depreciated	221,935,308	227,479,236
Total non-current assets	<u>282,162,369</u>	<u>279,850,781</u>
Total Assets	<u>335,075,637</u>	<u>330,725,852</u>
LIABILITIES		
Current Liabilities:		
Accounts payable	7,048,797	6,451,474
Accrued compensation	1,705,430	1,430,255
Construction and service deposits	182,053	379,159
Accrued interest payable from restricted assets	1,430,610	1,475,064
Current portion of long-term debt	2,695,000	2,610,000
Total current liabilities	<u>13,061,890</u>	<u>12,345,952</u>
Non-current liabilities:		
Other post employment benefits obligation, net	30,009	18,090
Loan payable, net of current portion	5,400,000	5,800,000
Certificates of participation, net of amortized discount and current portion	60,474,934	62,810,392
Total non-current liabilities	<u>65,904,943</u>	<u>68,628,482</u>
Total Liabilities	<u>78,966,833</u>	<u>80,974,434</u>
NET POSITION		
Net investment in capital assets	211,842,759	210,637,696
Restricted for future capital projects	56,412	22,985
Restricted for debt service	1,588,760	1,513,430
Unrestricted	42,620,873	37,577,307
Total net position	<u>\$ 256,108,804</u>	<u>\$ 249,751,418</u>

See accompanying independent auditors' report and notes to basic financial statements.

VALLECITOS WATER DISTRICT

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

For the year ended June 30, 2014
(with prior year data for comparison only)

	<u>2014</u>	<u>2013</u>
OPERATING REVENUES		
Water sales	\$ 26,031,460	\$ 23,364,573
Wastewater service charges	15,128,763	14,921,894
Ready-to-serve charges	11,484,584	10,638,282
Reclaimed water sales	1,533,203	1,718,013
Pumping charges	192,427	171,107
Other services and abatements	912,212	590,667
Total operating revenues	<u>55,282,649</u>	<u>51,404,536</u>
OPERATING EXPENSES		
Purchased water	24,145,579	21,982,845
General and administrative	5,173,986	4,879,580
Meadowlark wastewater treatment plant	2,993,578	2,777,837
Encina disposal	2,450,330	2,709,307
Collection and conveyance	1,632,347	1,633,839
Engineering	1,698,699	1,703,359
Transmission and distribution	1,154,882	1,068,907
Customer accounts	825,805	886,279
Information technology	865,655	831,423
Meter reading and repairs	614,784	561,274
Building and grounds	600,159	496,637
Equipment and vehicles	443,827	490,875
Other water operating expenses	396,935	418,890
Other wastewater operating expenses	495,999	374,529
Water quality and treatment	434,191	410,473
Tanks and reservoirs	308,031	299,360
Pumping	352,823	325,591
Total operating expenses	<u>44,587,610</u>	<u>41,851,005</u>
Operating income before overhead absorption	10,695,039	9,553,531
Overhead absorption	1,040,244	477,239
Operating income before depreciation and amortization	11,735,283	10,030,770
Depreciation and amortization	(9,160,497)	(8,955,355)
Operating income (loss)	<u>2,574,786</u>	<u>1,075,415</u>
NON-OPERATING REVENUES (EXPENSES)		
Property taxes	3,077,966	3,519,081
Investment income	302,384	142,911
Unrealized appreciation (depreciation) of investments	76,224	(189,076)
Annexation fees	288,580	11,204
Change in Encina Joint Venture assets	(334,093)	(2,040,544)
Interest expense	(2,672,296)	(2,758,728)
Other non-operating revenues/(expenses), net	40,935	(42,284)
Total non-operating revenues (expenses), net	<u>779,700</u>	<u>(1,357,436)</u>
Net income (loss) before capital contributions	3,354,486	(282,021)
Capital contributions	3,002,900	8,484,563
Change in net position	6,357,386	8,202,542
Total Net Position, Beginning of Year	249,751,418	241,548,876
Total Net Position, End of Year	<u>\$ 256,108,804</u>	<u>\$ 249,751,418</u>

See accompanying independent auditors' report and notes to basic financial statements.

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VALLECITOS WATER DISTRICT

STATEMENTS OF CASH FLOWS
For the year ended June 30, 2014
(with prior year data for comparison only)

	<u>2014</u>	<u>2013</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from water and wastewater customers	\$ 55,910,187	\$ 49,937,208
Payments for water	(23,875,948)	(21,369,629)
Payments for services and supplies	(7,949,533)	(7,628,659)
Payments for employee wages, benefits and related costs	(11,522,941)	(11,310,494)
	<u>12,561,765</u>	<u>9,628,426</u>
Net cash provided by operating activities		
CASH FLOWS FROM NONCAPITAL AND RELATED FINANCING ACTIVITIES		
Receipts from taxes and assessments	<u>3,073,978</u>	<u>4,371,580</u>
Net Cash Provided by Noncapital and Related Financing Activities	<u>3,073,978</u>	<u>4,371,580</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Receipts from annexation fees & cell tower rentals	324,522	45,593
Acquisition and construction of utility plant	(9,294,330)	(6,211,209)
Proceeds from certificates of participation	-	7,055,000
Principal paid on long-term debt	(2,610,000)	(1,885,001)
Interest payments on long-term debt	(3,004,832)	(2,914,360)
Investment in Encina Wastewater Authority	395,981	(1,941,344)
Capacity fees received	<u>2,402,939</u>	<u>7,286,197</u>
Net Cash Provided/(Used) by Capital and Related Financing Activities	<u>(11,785,720)</u>	<u>1,434,876</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(13,493,898)	(23,553,760)
Proceeds from sale, call and maturity of investments	11,468,088	5,006,133
Investment earnings	305,831	127,304
Collections on note receivable from City of San Marcos	<u>113,935</u>	<u>107,997</u>
Net cash (used) by investing activities	<u>(1,606,044)</u>	<u>(18,312,326)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	2,243,979	(2,877,444)
Cash and Cash Equivalents, Beginning of Year	<u>15,368,268</u>	<u>18,245,712</u>
Cash and Cash Equivalents, End of Year	<u>\$ 17,612,247</u>	<u>\$ 15,368,268</u>

(Continued)

See accompanying independent auditors' report and notes to basic financial statements.

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VALLECITOS WATER DISTRICTSTATEMENTS OF CASH FLOWS (Continued)
For the year ended June 30, 2014
(with prior year data for comparison only)

	<u>2014</u>	<u>2013</u>
Reconciliation of operating income (loss) to net cash flows provided by operating activities:		
Operating income (loss)	\$ 2,574,786	\$ 1,075,415
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation and amortization of capital assets	9,160,497	8,955,355
Non-cash operating expense Encina Phase V adjustment	-	363,000
Changes in operating assets and liabilities:		
(Increase) Decrease in assets:		
Accounts receivable from water and wastewater sales	649,625	(1,254,725)
Accounts receivable from other governments	(93,347)	(79,270)
Accounts receivable – other	71,260	(133,331)
Inventories	(139,794)	(44,640)
Prepaid expenses	(45,501)	(9,276)
Increase (Decrease) in liabilities:		
Accounts payable	97,145	749,852
Accrued compensation	275,175	8,298
Other post employment benefits obligation, net	11,919	(2,252)
Total adjustments	<u>9,986,979</u>	<u>8,553,011</u>
Net cash provided by operating activities	<u>\$ 12,561,765</u>	<u>\$ 9,628,426</u>

Financial Statement Classification**Cash and cash equivalents**

Current assets:

Cash and cash equivalents	\$ 14,592,877	\$ 8,105,509
Restricted cash and cash equivalents	<u>3,019,370</u>	<u>7,262,759</u>
Total Cash and Cash Equivalents	<u>\$ 17,612,247</u>	<u>\$ 15,368,268</u>

Supplemental Disclosures:

Noncash Investing and Financing Activities

Contributions of assets by developers	\$ 428,956	\$ 934,777
Amortization related to PERS Sidefund	\$ 430,506	\$ 430,506
Unrealized appreciation (depreciation) of investments	\$ 76,224	\$ (189,076)

June 30, 2014

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 District is the primary governmental unit based on the foundation of a separately elected governing board elected by geographic division of 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 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. Measurement Focus, Basis of Accounting and Financial Statement Presentation

Measurement focus is a term used to describe "which" transactions are recorded within the various financial statements. Basis of accounting refers to "when" transactions are recorded regardless of the measurement focus applied. The accompanying financial statements are reported using the economic resources measurement focus, and the accrual basis of accounting. Under the economic measurement focus all assets and liabilities (whether current or noncurrent) associated with these activities are included on the Statement of Net Position. The Statement of Revenues, Expenses and Changes in Net Position present increases (revenues) and decreases (expenses) in total Net Position. Under the accrual basis of accounting, revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

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).

1. Reporting Entity and Summary of Significant Accounting Policies (Continued)

B. Measurement Focus, Basis of Accounting and Financial Statement Presentation (Continued)

Operating revenues and expenses, such as water sales and water purchases and wastewater service charges, 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.

The basic financial statements of the Vallecitos Water District have been prepared in conformity with accounting principles generally accepted in the United States of America. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for governmental accounting financial reporting purposes.

Net Position of the District are classified into three components: (1) net investment in capital assets, (2) restricted net position, and (3) unrestricted net position. These classifications are defined as follows:

Net Investment in Capital Assets

This component of net position consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of notes or borrowing that are attributable to the acquisition of the asset, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of net investment in capital assets.

Restricted Net Position

This component of net position consists of constraints placed on net position use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted Net Position

This component of net position consists of net position that does not meet the definition of “net investment in capital assets” or “restricted net position”.

1. Reporting Entity and Summary of Significant Accounting Policies (Continued)

C. New Accounting Pronouncements

Pending Accounting Standards

GASB has issued the following statements which may impact the District's financial reporting requirements in the future:

- GASB 68—“*Accounting and Financial Reporting for Pensions, an amendment of GASB Statement No. 27*”, effective for the fiscal years beginning after June 15, 2014.
- GASB 69—“*Government Combinations and Disposals of Government Operations*”, effective for periods beginning after December 15, 2013.
- GASB 71 - “*Pension Transition for Contributions Made Subsequent to the Measurement Date – an Amendment of GASB No. 68*”, effective for the fiscal years beginning after June 15, 2014.

D. Deferred Outflows/Inflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then. The District does not have any of these items as of June 30, 2014 or June 30, 2013.

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statements element, *deferred inflows of resources*, represents an acquisition of net position that applies to a future period(s) and will not be recognized as an inflow of resources (revenue) until that time. The District does not have any of these items as of June 30, 2014 or June 30, 2013.

E. 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 position during the reporting period. Actual results could differ from those estimates.

F. Statement of Cash Flows

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

1. Reporting Entity and Summary of Significant Accounting Policies (Continued)

G. 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.

H. 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.

I. 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 Position and as capital grant contribution or operating grant revenue, as appropriate, on the Statement of Revenues, Expenses and Changes in Net Position.

J. 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

K. 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.

L. 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.

M. Prepaid Expenses

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

1. Reporting Entity and Summary of Significant Accounting Policies (Continued)

N. 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 Position. 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 expenses meeting the criteria imposed on the use of restricted resources by a third party.

O. Capital Assets

Capital assets acquired and/or constructed are capitalized at historical cost. District policy has set the capitalization threshold for reporting capital assets expected to have a useful life of more than one year 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

P. 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 capital expenditures incurred by EWA. Ownership percentages are determined by joint agreements at the time the assets are acquired.

Q. Construction Deposits

Construction deposits represent deposits received in aid of construction, which are refundable if the applicable construction does not take place. Construction deposits are transferred to contributed capital when the District is no longer liable for the applicable construction project.

R. 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.

S. Interest Expense

The District incurs interest charges on long-term debt. For fiscal year ended June 30, 2014 the District expensed \$2,672,296 of interest incurred and capitalized \$249,813 as part of the cost of construction projects.

T. 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.

1. Reporting Entity and Summary of Significant Accounting Policies (Continued)**U. 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.

V. 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.

W. Prior Year Data

Selected information regarding the prior year has been included in the accompanying financial statements. This information has been included for comparison purposes only and does not represent a complete presentation in accordance with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the District's prior year financial statements, from which this selected financial data was derived.

2. Cash and Investments

Cash and Investments are classified in the accompanying financial statements as follows:

	<u>2014</u>	<u>2013</u>
Cash and cash equivalents	\$ 14,592,877	\$ 8,105,509
Restricted cash and cash equivalents	3,019,370	7,262,759
Investments	<u>25,887,495</u>	<u>23,788,976</u>
Total Cash and Investments	<u>\$ 43,499,742</u>	<u>\$ 39,157,244</u>

Cash and Investments consist of the following:

	<u>2014</u>	<u>2013</u>
Cash on hand	\$ 1,700	\$ 1,700
Deposits with financial institutions (over draft)	5,021,555	3,601,393
Investments	<u>38,476,487</u>	<u>35,554,151</u>
Total cash and investments	<u>\$ 43,499,742</u>	<u>\$ 39,157,244</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. Government Sponsored Entities	5 years	60%	20%
Commercial Paper	270 days	20%	10%
Certificates of Deposit	4 years	20%	5%
Repurchase Agreements	1 year	10%	10%
Local Government Investment Pools	N/A	40%	20%
Local Agency Investment Fund (LAIF)	N/A	60%	None
State and Local Agency Bonds	5 years	20%	25%
FDIC - Backed Medium - Term Notes	4 years	20%	FDIC limit
Savings Accounts	N/A	10%	10%

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 \$893,328 and \$955,352 as of June 30, 2014 and 2013, respectively. Of the bank balances, up to \$250,000 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.

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 any time 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 is 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 22. 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, 2014, are as follows:

Investment Type	Total	Remaining Maturity (in Months)		
		12 Months Or Less	13 - 24 Months	25 - 60 Months
Federal Farm Credit Banks	\$ 3,290,787	504,690	675,742	2,110,355
Federal Home Loan Bank	6,271,338	251,258	-	6,020,080
Federal Home Loan Mortgage Association	3,854,933	-	534,330	3,320,603
Federal National Mortgage Association	4,569,289	-	499,290	4,069,999
Commerical Paper	3,497,230	3,497,230	-	-
Local Agency Investment Fund (LAIF)	8,916,541	8,916,541	-	-
San Diego County Investment Pool	5,057,000	5,057,000	-	-
Held by bond trustee:				
Money market funds	3,019,369	3,019,369	-	-
Total	\$ 38,476,487	21,246,088	1,709,362	15,521,037

2. Cash and Investments (Continued)

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 Moody’s rating as of year-end for each investment type.

Credit ratings of investments as of June 30, 2014 were as follows:

Investment Types	Total	Minimum Legal Rating	Rating as of Year End			
			AAA	AA+	A1	Not Rated
Federal Farm Credit Banks	\$ 3,290,787	N/A	3,290,787	-	-	-
Federal Home Loan Bank	6,271,338	AA+	6,271,338	-	-	-
Federal Home Loan Mortgage Corporation	3,854,933	AA+	3,854,933	-	-	-
Federal National Mortgage Association	4,569,289	AA+	4,569,289	-	-	-
Commercial Paper	3,497,230	N/A	-	-	3,497,230	-
Local Agency Investment Fund (LAIF)	8,916,541	N/A	-	-	-	8,916,541
San Diego County Investment Pool	5,057,000	N/A	5,057,000	-	-	-
Held by bond trustee:						
Money market funds	3,019,369	N/A	-	3,019,369	-	-
Total	\$ 38,476,487		23,043,347	3,019,369	3,497,230	8,916,541

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 at June 30, 2014 are as follows:

Issuer	Investment Type	Reported Amount
Federal Farm Credit Banks	U.S. Government Sponsored Entities	\$ 3,290,787
Federal Home Loan Bank	U.S. Government Sponsored Entities	\$ 6,271,338
Federal Home Loan Mortgage Association	U.S. Government Sponsored Entities	\$ 3,854,933
Federal National Mortgage Association	U.S. Government Sponsored Entities	\$ 4,569,289

3. Accounts Receivable

The balance at June 30, consists of the following:

	<u>2014</u>	<u>2013</u>
Accounts receivable - water and wastewater sales and services	\$ 6,143,492	\$ 6,793,266
Allowance for uncollectible accounts	(38,658)	(38,807)
Accounts receivable - water sales, net	<u>\$ 6,104,834</u>	<u>\$ 6,754,459</u>

Property Tax Receivable

Taxes and assessments receivable of \$104,034 and \$100,242 have been reduced by an allowance for estimated uncollectible taxes of \$4,617 and \$4,812 at June 30, 2014 and 2013, respectively.

4. Capital Assets

Changes in capital assets for 2014 are as follow:

	<u>Balance 2013</u>	<u>Additions/ Transfers</u>	<u>Deletions/ Transfers</u>	<u>Balance 2014</u>
Capital Assets, Not Depreciated				
Land	\$ 4,761,505	\$ -	\$ -	\$ 4,761,505
Construction-in-process	12,492,200	10,363,390	(3,301,585)	19,554,005
Total Capital Assets, Not Depreciated	<u>17,253,705</u>	<u>10,363,390</u>	<u>(3,301,585)</u>	<u>24,315,510</u>
Capital Assets, Being Depreciated				
Water transmission and distribution system	187,395,706	1,473,235	(8,993)	188,859,948
Wastewater system	115,092,483	696,280		115,788,763
Buildings	15,252,215	48,212		15,300,427
Transportation equipment	3,793,371	564,957	(12,807)	4,345,521
Field and shop equipment	10,309,062	375,441	(14,165)	10,670,338
Office equipment	2,473,211	30,253	(54,171)	2,449,293
Total Capital Assets, Being Depreciated	<u>334,316,048</u>	<u>3,188,378</u>	<u>(90,136)</u>	<u>337,414,290</u>
Less Accumulated Depreciation:				
Water transmission and distribution system	(53,915,109)	(4,260,663)	6,677	(58,169,095)
Wastewater system	(32,956,065)	(2,104,435)	-	(35,060,500)
Buildings	(8,641,371)	(1,265,316)	-	(9,906,687)
Transportation equipment	(2,637,122)	(336,872)	12,807	(2,961,187)
Field and shop equipment	(7,169,877)	(569,609)	14,165	(7,725,321)
Office equipment	(1,517,268)	(193,095)	54,171	(1,656,192)
Total Accumulated Depreciation	<u>(106,836,812)</u>	<u>(8,729,990)</u>	<u>87,820</u>	<u>(115,478,982)</u>
Total Capital Assets, Being Depreciated, net	<u>227,479,236</u>	<u>(5,541,612)</u>	<u>(2,316)</u>	<u>221,935,308</u>
Total Capital Assets, net	<u>\$ 244,732,941</u>	<u>\$ 4,821,778</u>	<u>\$ (3,303,901)</u>	<u>\$ 246,250,818</u>

In 2014, major capital assets additions during the year included vehicles, sewer and water mains, manholes, sewer buildings and improvements, and valves and fire hydrants.

Depreciation expense for the ended June 30, 2014 was \$8,729,990 and is included in Depreciation and Amortization expense on the Statement of Revenues, Expense and Changes in Net Position.

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:

Project Name	2013	2014
<i>District Financed</i>		
SM interceptor - SM Blvd/Discovery	\$ 7,806,534	\$ 12,891,967
Wulff Reservoir/Pressure Reducing Station	1,155,491	1,188,362
San Elijo Road Facilities	641,279	641,279
Linda Vista Sewer Upgrade	320,942	620,150
Meadowlark Tank #3	488,961	488,961
San Elijo Hills Pump Station Project	91,498	340,602
Rock Springs Sewer Replacement	154,340	259,256
MRF Solids Force Main Replacement	121,588	224,003
Aeration Panel Membranes	-	185,648
Secondary skimmer controls	162,532	-
Encina Land Parallel Outfall	138,591	138,880
Primary Skimmer Controls (3)	-	114,050
Telescoping Valve Control	-	103,996
205070 - Flow Monitoring Station	58,374	102,471
Mountain Belle Pump Station & Pipeline Design	99,350	99,350
Water & Sewer Master Plan	-	96,168
Lift Station No 1 Pump Improvements	44,528	89,479
Mahr Reservoir Aeration	-	78,559
Mrf Nutrient Removal Study	-	65,243
Environmental Mitigation Property	59,646	59,646
Mobile Maximo	-	56,402
Coggan Pump Station - Hydro Tank Replacement	54,079	-
Refurbish 3-Stage Vertical Turbine Eff Pump	-	53,617
Supplemental Chlorine Injection Sys	-	49,891
Land Outfall Clearing & Access Rd	-	46,229
Sluice Gate Dam	-	45,938
Scada Radio Antenna Masts Fy12/13	-	41,556
Effluent Chlorine Analyzer @ T.O. Res	40,984	-
Desalinated Water Connection	-	37,075
204484 - Pavement and Access Roads	34,742	-
Coggan Pump Station Flow Meter	-	31,526
Old Questhaven Sewer Replacement	718	718
Subtotal - District Financed	11,474,177	18,151,022
<i>Developer Financed</i>		
High Point Hydropneum	93,073	98,634
San Elijo Hills K Lower Unit 19	80,302	-
San Elijo Hills K Lower Unit 18	76,134	-
Palos Vista Estates	59,394	59,545
San Elijo Hills V2 West	54,924	-
Palomar Station	24,119	59,505
SEH PH 3 PA T U - 205626	-	51,257
Seh Ph 5 Pa S Ip U3 -	-	29,839
Seh Ph5 Pa S U4 - San	-	23,524
Fairfield Inn - Carlsbad	-	20,975
Odor Control Study	-	20,228
Seh Ph5 Pa S U5 - San	-	16,823
San Marcos Creek Improvement Plan	15,513	16,244
Developer Impact Fee Study	15,985	-
Grand Avenue City	14,879	14,879
Autumn Drive and Buelow Park	14,206	14,206
Pump Station Meadowlark	9,617	9,617
Civic Center Market Place	8,764	8,764
Subtotal - Developer Financed	466,910	444,040
Various Other Projects	551,113	958,943
Total	\$ 12,492,200	\$ 19,554,005

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, 2014, the Member Agencies have the following approximate ownership interest:

City of Vista	25%
City of Carlsbad	24%
Buena Sanitation District	7%
Vallecitos Water District	23%
Leucadia Wastewater District	17%
City of Encinitas	4%

The latest available financial statements of EWA, dated June 30, 2013 and 2012, are available directly from EWA (6200 Avenida Encinas, Carlsbad, California 92009), and show the following:

	<u>2013</u>	<u>2012</u>
Total assets	\$ 126,543,408	\$ 126,498,731
Total liabilities	<u>2,608,176</u>	<u>2,981,429</u>
Total net position	<u>\$ 123,935,232</u>	<u>\$ 123,517,302</u>
Increase (decrease) in net position	<u>\$ 417,930</u>	<u>\$ (917,397)</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, 2014, the following amounts are due to the District:

<u>Fiscal Year</u>	<u>Principal Amount</u>
2015	\$ 120,203
2016	126,813
2017	133,788
2018	<u>141,144</u>
Total	521,948
Current Portion	<u>(120,203)</u>
Non-current Portion	<u>\$ 401,745</u>

7. 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 are netted against the long-term portion of the Certificates of Participation on the Statements of Net Position (see note 8).

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

	<u>2014</u>	<u>2013</u>
Deferred charges from debt retirement	\$ 77,001	\$ 77,001
Accumulated amortization	(26,522)	(23,552)
Deferred charges from debt retirement, net	<u>\$ 50,479</u>	<u>\$ 53,449</u>

8. 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 prestressed 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 are due in annual installments from July 1, 2008 to July 1, 2035 bearing interest at 4.00% to 5.50%. This debt contains a rate covenant which requires the District to maintain annual net revenues of at least 115% of the annual debt service. In Fiscal Year 2014 the District was in compliance with this rate covenant.

8. Long-Term Debt (Continued)

2005 Certificates of Participation (Continued)

The balance at June 30, 2014 net of unamortized premiums, discounts and deferred charges is as follows:

	Balance 2013	Additions	Payments/ Deletions	Balance 2014
2005 Series A COP	\$ 56,975,000	\$ -	\$ 1,565,000	\$ 55,410,000
Add: Bond Premium	1,354,636	-	58,897	1,295,739
Less: Unamortized Discount	(355,795)	-	(15,469)	(340,326)
Less: Deferred charges	(53,449)	-	(2,970)	(50,479)
Total	<u>57,920,392</u>	<u>\$ -</u>	<u>\$ 1,605,458</u>	<u>56,314,934</u>
Less: Current Portion	<u>(1,565,000)</u>			<u>(1,635,000)</u>
Long-Term Portion	<u>\$ 56,355,392</u>			<u>\$ 54,679,934</u>

Annual debt service payments are as follows:

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.

Fiscal Year	Principal	Interest	Total
2015	\$ 1,635,000	\$ 2,736,038	\$ 4,371,038
2016	1,715,000	2,656,175	4,371,175
2017	1,810,000	2,559,238	4,369,238
2018	1,910,000	2,459,325	4,369,325
2019	1,985,000	2,359,563	4,344,563
2020-2024	11,800,000	10,068,514	21,868,514
2025-2029	15,225,000	6,631,250	21,856,250
2030-2034	14,120,000	2,835,419	16,955,419
2035-2036	<u>5,210,000</u>	<u>263,747</u>	<u>5,473,747</u>
Total	55,410,000	<u>\$ 32,569,269</u>	<u>\$ 87,979,269</u>
Less current portion	<u>(1,635,000)</u>		
Total non-current portion	<u>\$ 53,775,000</u>		

8. Long-Term Debt (Continued)

2012 Certificates of Participation

On December 5, 2012, the Board of Directors of the Vallecitos Water District authorized the issuance of debt. The District received \$7.1 million of proceeds at a 1.98% fixed interest rate over the ten year life of the loan. The proceeds will support the San Marcos Sewer Interceptor and Linda Vista Sewer Line projects.

Changes in long-term debt amounts for the 2014 fiscal year were as follows:

	<u>2013</u>	<u>Additions</u>	<u>Deletions</u>	<u>2014</u>
2012 COPS	\$ 7,100,000	\$ -	\$ 645,000	\$ 6,455,000
Less: Current Portion	<u>(645,000)</u>			<u>(660,000)</u>
Long-Term Portion	<u>\$ 6,455,000</u>			<u>\$ 5,795,000</u>

Annual debt service payments are as follows:

<u>Fiscal Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 660,000	\$ 121,275	\$ 781,275
2016	673,000	108,078	781,078
2017	688,000	94,604	782,604
2108	702,000	80,843	782,843
2019	741,000	66,558	807,558
2020-2023	<u>2,991,000</u>	<u>119,998</u>	<u>3,110,998</u>
Totals	6,455,000	<u>\$ 591,356</u>	<u>\$ 7,046,356</u>
Less current portion	(660,000)		
Total non-current portion	<u>\$ 5,795,000</u>		

8. Long-Term Debt (Continued)

2008 Loan Payable

On November 12, 2008, the District entered into a variable rate tax-exempt private placement loan with Union Bank of California (UBOC) in the amount of \$8,000,000 to partially finance the District's share of the expansion costs at the Encina Wastewater Authority's treatment plant. Terms of the agreement call for interest to accrue at an interest rate per annum equal to 64.72% of the LIBOR index plus 0.79% (1.033% at June 30, 2014). Principal payments of \$200,000 plus interest are payable semi-annually and maturing in 2028.

Loan payables for the year ended June 30, 2014 is as follows:

	<u>Balance 2013</u>	<u>Additions</u>	<u>Payments/ Deletions</u>	<u>Balance 2014</u>
2008 UBOC Loan	\$ 6,200,000	\$ -	\$ 400,000	\$ 5,800,000
Less: Current Portion	<u>(400,000)</u>			<u>(400,000)</u>
Long-Term Portion	<u>\$ 5,800,000</u>			<u>\$ 5,400,000</u>

Annual debt service payments are as follows:

<u>Fiscal Year</u>	<u>Principal</u>	<u>Interest*</u>	<u>Total</u>
2015	\$ 400,000	\$ 59,749	\$ 459,749
2016	400,000	58,938	458,938
2017	400,000	57,807	457,807
2018	400,000	56,320	456,320
2019	400,000	54,437	454,437
2020-2024	2,000,000	226,893	2,226,893
2025-2029	<u>1,800,000</u>	<u>91,040</u>	<u>1,891,040</u>
Total	5,800,000	<u>\$ 605,184</u>	<u>\$ 6,405,184</u>
Less current portion	<u>(400,000)</u>		
Total non-current portion	<u>\$ 5,400,000</u>		

* - Interest rate of 1.033% used for future years is interest rate set by Union Bank on 9/30/2014 for effective dates 3/31/2014-9/30/2014.

9. Net Position

a. Net Investment In Capital Assets

Net Investment in Capital Assets at June 30, consists of the following:

	<u>2014</u>	<u>2013</u>
Investment in Encina Wastewater Authority capital assets	\$ 34,161,875	\$ 32,850,882
Capital assets not being depreciated	24,315,511	17,253,705
Net capital assets being depreciated	221,935,307	227,479,236
Certificates of participation - current portion	(2,295,000)	(2,210,000)
Loan payable - UBOC - current portion	(400,000)	(400,000)
Certificates of participation - noncurrent portion	(60,474,934)	(58,536,127)
Loan payable - UBOC - noncurrent portion	(5,400,000)	(5,800,000)
Total net investment in capital assets	<u>\$ 211,842,759</u>	<u>\$ 210,637,696</u>

b. Restricted Net Position

Restricted net position at June 30, consists of the following:

	<u>2014</u>	<u>2013</u>
Restricted for debt service	\$ 1,588,760	\$ 1,513,430
Restricted for future capital projects	56,412	22,985
Total restricted net position	<u>\$ 1,645,172</u>	<u>\$ 1,536,415</u>

c. Unrestricted Net Position

Unrestricted net position at June 30, consists of the following:

	<u>2014</u>	<u>2013</u>
Non-spendable net position:		
Inventories	\$ 1,115,354	\$ 975,560
Prepaid expenses	2,084,889	2,469,895
Total non-spendable net position	<u>3,200,243</u>	<u>3,445,455</u>
Spendable net position:		
Unrestricted	<u>39,420,630</u>	<u>34,131,852</u>
Total spendable net position	<u>39,420,630</u>	<u>34,131,852</u>
Total unrestricted net position	<u>\$ 42,620,873</u>	<u>\$ 37,577,307</u>
Total net position	<u>\$ 256,108,804</u>	<u>\$ 249,751,418</u>

10. Defined Benefit Pension Plan

Plan Description

The District 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. For employees hired before January 1, 2013, the District pays 4% of the contributions. For employees hired after January 1, 2013, under the California Employee's Pension Reform Act (PEPRA) provisions, the contribution rate for plan members in the CalPERS 2.0% at 62 Risk Pool Retirement Plan is 6.25% of their annual covered salary. The District is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the CalPERS Board of Administration. The required employer contribution rate for the fiscal year ended June 30, 2014 was 15.724%. The District is required to contribute the actuarially determined remaining amounts necessary to fund the 3.0% at age 60 retirement plan benefits for its classic members and 2.0% at age 62 for its new members (employees hired after December 31, 2012) under the PEPRA provisions. The contribution requirements of the Plan members are established by State statute and the employer contribution rate is established and may be amended by the CalPERS.

Annual Pension Costs

For the fiscal year ended June 30, 2014, the District's annual pension cost and actual contribution was \$1,184,618. The required contribution for the fiscal year ended June 30, 2014 was determined as part of the June, 30 2011 actuarial valuation.

The following is a summary of the actuarial assumptions and methods:

Valuation Date	June 30, 2011
Actuarial Cost Method	Entry Age Normal Cost Method
Amortization Method	Level Percent of Payroll
Average Remaining Period	19 Years as of the Valuation Date
Asset Valuation Method	15 Year Smoothed Market
Actuarial Assumptions:	
Investment Rate of Return	7.50% (Net of Administrative Expenses)
Projected Salary Increase	3.30% to 14.20% Depending on Age, Service, and Type of Employment
Inflation	2.75%
Payroll Growth	3.00%
Individual Salary Growth	A merit scale varying by duration of employment coupled with an assumed annual inflation component of 2.75% and an annual production growth of 0.25%.

Initial unfunded liabilities are amortized over a closed period that depends on the Plan's date of entry into CalPERS. Subsequent Plan amendments are amortized as a level percentage of pay over a closed 20-year period. Gains and losses that occur in the operation of the plan are amortized over a rolling period, which results in an amortization of 6% of unamortized gains and losses each year. If the plan's accrued liability exceeds the actuarial value of the plan assets, then the amortization payment of the total unfunded liability may be lower than the payment calculated over a 30-year amortization period.

10. Defined Benefit Pension Plan (Continued)

Annual Pension Costs (continued)

Three Year Trend Information for PERS

<u>Fiscal Year</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>	<u>APC Percentage of Payroll</u>
2012	\$ 1,045,353	100%	-	13.477%
2013	\$ 1,064,666	100%	-	15.100%
2014	\$ 1,184,618	100%	-	15.498%

Funding Status

As of June 30, 2004, the District’s miscellaneous plan became part of a CalPERS Risk Pool for employers with less than 100 active plan members. As part of a cost-sharing multiple-employer defined benefit plan, disclosure of the schedule of funding progress is not required as information is not specific to the District.

11. Other Post-Employment Benefits Plan

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. At June 30, 2014, there were twenty-nine retired employees who met 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, 2014 and 2013 was \$357,639 and \$385,258, respectively.

Plan Description

The District administers the Other Post-Employment Benefit Plan (OPEB), a multi-employer defined benefit plan.

For employees who retired before July 1, 2013, The District’s 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.

For employees who retire after June 30, 2013, the District’s OPEB provides continued medical coverage for an eligible retired employee and spouse or registered domestic partner until they become entitled to Medicare Benefits at age 65. Medical premiums paid by the District are established per the most current Memorandum of Understanding (MOU). Plan premiums elected by the retiree above those established in the MOU are paid by the retiree.

11. Other Post-Employment Benefits Plan (Continued)

Plan Description (Continued)

To become eligible for partial OPEB benefits, non-retired employees hired before July 1, 2013, must be age 50 and have five years of continuous service with the District. OPEB benefits increase with each year of continuous service up to ten years when the employee becomes 100% vested to receive the maximum amount of premium established in the most current MOU at retirement.

The OPEB benefit is not offered to employees hired after July 1, 2013.

Eligible retirees may enroll in any of the plans the District offers through the ACWA Program. The activity and liability from the OPEB plan are included in these financial statements.

Funding Policy

The District’s Resolution No. 788, established the authority for the plan and provides that the District will pay 100% of the cost of the OPEB plan. Resolution No. 1389 authorized the District to establish and maintain an irrevocable trust to fund OPEB and seek reimbursement from the trust to cover current retiree benefit premiums which are paid by the District on a pay-as-you-go basis. The District began funding the trust in March of 2012.

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:

	2014	2013
Annual required contribution	\$ 387,648	\$ 435,652
Interest on net post employment benefits payable obligation	-	-
Adjustment to annual required contribution	-	-
	<hr/>	<hr/>
Annual post employment benefits payable obligation cost (expense)	387,648	435,652
Contributions made:		
Retired employees post employment medical benefits payments	(375,729)	(437,904)
	<hr/>	<hr/>
Increase (decrease) in net post employment benefits payable obligation	11,919	(2,252)
Post employment benefits payable, net - beginning of year	18,090	20,342
	<hr/>	<hr/>
Post employment benefits payable, net - end of year	<u>\$ 30,009</u>	<u>\$ 18,090</u>

Funded Status of the Plan

The most recent valuation (dated January 1, 2013) includes an Actuarial Accrued Liability of \$4,707,625 and an Unfunded Actuarial Accrued Liability of \$1,896,023. The covered payroll (annual payroll of active employees covered by the plan) for the year ended June 30, 2014 is \$7,445,301. The ratio of the unfunded actuarial liability to annual payroll covered is 25.47%. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for the benefits.

11. Other Post-Employment Benefits Plan (Continued)

Three 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:

<u>Fiscal Year Ended</u>	<u>Annual OPEB Costs</u>	<u>Percentage of Annual OPEB Cost Contributed</u>	<u>Net OPEB Obligation</u>
June 30, 2012	\$ 595,722	486.98%	\$ 20,342
June 30, 2013	\$ 435,652	100.52%	\$ 18,090
June 30, 2014	\$ 387,648	96.93%	\$ 30,009

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 7% discount rate. The high rate of annual health care cost increases experienced in recent years is assumed to gradually decrease, 16.3% in 2014 and 10.0% in 2015. A level dollar amortization of the Unfunded Actuarial Accrued Liability is used over a closed 30-year period.

12. 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, 2014, 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 \$2,000,000, combined single limit at \$1,000,000 per occurrence. The District purchased additional excess coverage layers: \$58 million for general, auto and public officials liability, which increases the limits on the insurance coverage noted above.

12. 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 \$100 million per occurrence, subject to a \$10,000 deductible per occurrence. Total risk financed self-insurance limits is \$50,000 with additional insurance purchased with coverage limits of \$100 million.
- Boiler and machinery coverage for the replacement cost up to \$100 million per occurrence, subject to various deductibles depending on the type of equipment.
- Workers' compensation insurance up to California statutory limits for all work related injuries/illnesses covered by California law, with total risk financed self-insurance limits of \$2 million.

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, 2014 and 2013. 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, 2014 and 2013.

13. Segment Information

The District's 2005A COPs are payable solely from the net revenues of the District's water and sewer systems. Summary financial information for the water and sewer systems is presented for June 30, 2014.

Condensed Statement of Net Position

	2014			2013
	Water	Sewer	Total	Total
Assets:				
Current assets	\$ 22,258,256	\$ 30,655,012	\$ 52,913,268	\$ 50,875,071
Non-current assets	936,934	812,742	1,749,676	2,266,958
Capital assets, net	145,064,264	135,348,429	280,412,693	277,583,823
Total assets	168,259,454	166,816,183	335,075,637	330,725,852
Liabilities:				
Current liabilities	8,007,127	5,054,763	13,061,890	12,349,952
Non-current liabilities	27,189,241	38,715,702	65,904,943	68,628,482
Total liabilities	35,196,368	43,770,465	78,966,833	80,978,434
Net Position:				
Net investment in capital assets	117,053,782	94,788,977	211,842,759	210,637,696
Restricted for future capital facilities	13,496	42,916	56,412	22,985
Restricted for debt service	833,850	754,910	1,588,760	1,513,430
Unrestricted	15,161,961	27,458,912	42,620,873	37,577,307
Total net position	\$ 133,063,089	\$ 123,045,715	\$ 256,108,804	\$ 249,751,418

14. Segment Information (Continued):

Condensed Statement of Revenues, Expenses and Changes in Net Position

	2014			2013
	Water	Sewer	Total	Total
Revenues				
Operating Revenues	\$ 38,532,143	\$ 16,750,506	\$ 55,282,649	\$ 51,404,536
Non-Operating Revenues	1,884,011	1,904,269	3,788,280	3,547,360
Total Revenues	40,416,154	18,654,775	59,070,929	54,951,896
Expenses:				
Operating Expenses	33,283,213	10,264,153	43,547,366	41,373,769
Depreciation and Amortization	5,371,169	3,789,328	9,160,497	8,955,356
Non-Operating Expenses	1,424,737	1,583,843	3,008,580	4,904,792
Total Expenses	40,079,119	15,637,324	55,716,443	55,233,917
Net Income/(Loss) before Capital Contributions	337,035	3,017,451	3,354,486	(282,021)
Capital Contributions	1,097,734	1,905,166	3,002,900	8,484,563
Change in Net Position	1,434,769	4,922,617	6,357,386	8,202,542
Total Net Position, Beginning of Year	131,628,319	118,123,099	249,751,418	241,548,876
Net position, end of year	\$ 133,063,088	\$ 123,045,716	\$ 256,108,804	\$ 249,751,418

Condensed Statement of Cash Flows

	2014			2013
	Water	Sewer	Total	Total
Net cash provided (used) by:				
Operating activities	\$ 5,916,124	\$ 6,645,641	\$ 12,561,765	\$ 9,628,426
Non-capital financing activities	1,636,966	1,437,012	3,073,978	4,371,580
Capital and related financing activities	(3,267,580)	(8,518,140)	(11,785,720)	1,434,875
Investing activities	(1,337,688)	(268,356)	(1,606,044)	(18,312,325)
Net cash provided	2,947,822	(703,843)	2,243,979	(2,877,444)
Cash and cash equivalents, beginning of year	1,507,976	13,860,292	15,368,268	18,245,712
Cash and cash equivalents, end of year	\$ 4,455,798	\$ 13,156,449	\$ 17,612,247	\$ 15,368,268

15. 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 \$2,171,128 in open construction contracts as of June 30, 2014. These include the following:

Project Name	Total Approved Contract(s)	Spent Through June 30, 2014	Remaining
Meadowlark Tank 1 and 2 Refurbishment	\$ 467,581	\$ 178,806	\$ 288,775
Linda Vista Sewer Upgrade	1,882,353	-	1,882,353
	<u>\$ 2,349,934</u>	<u>\$ 178,806</u>	<u>\$ 2,171,128</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.

16. Prepaid PERS Contribution

During fiscal year 2012, the District prepaid the accumulated PERS side fund liability resulting from risk pooling as of June 30, 2003, valued at \$3,013,545. This value was determined based on a valuation as of June 30, 2009. The prepayment is amortizable over a seven year period and will result in a decrease to the District’s 2013/2014 PERS employer contribution rate of 6.508%. The amount amortizable during fiscal year 2014/2015 \$430,506 is reported as current prepaid asset on the Statement of Net Position. The balance of \$1,291,519 which will be amortizable in years after fiscal year 2014/2015 is shown as the non-current asset Prepaid PERS Contribution on the Statement of Net Position.

REQUIRED SUPPLEMENTARY INFORMATION
YEAR ENDED JUNE 30, 2014

Schedule of Funding Progress for OPEB

Actuarial Valuation Date	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
6/30/2013	\$ 2,635,608	\$ 5,078,124	\$ 2,442,516	51.90%	\$ 7,445,301	32.81%
6/30/2011	\$ -	\$ 4,911,102	\$ 4,911,102	0.00%	\$ 7,759,756	63.29%
6/30/2009	\$ -	\$ 6,021,764	\$ 6,021,764	0.00%	\$ 7,984,313	75.42%

**SUPPLEMENTARY INFORMATION
YEARS ENDED JUNE 30, 2014 AND 2013**

VALLECITOS WATER DISTRICTSchedule of Operating Expenses - Water Division
For the Fiscal Years Ended June 30, 2014 and 2013

	2014	2013
Purchased Water	\$ 24,145,579	\$ 21,982,845
Pumping:		
Labor	71,895	74,752
Materials and supplies	16,907	30,444
Outside repair	26,212	11,817
Power	237,788	208,578
Total Pumping	<u>352,802</u>	<u>325,591</u>
Water Quality and Treatment:		
Labor	322,813	319,206
Materials and supplies	31,075	51,192
Outside Repair	76,152	40,075
Power	4,151	-
Total Water Treatment	<u>434,191</u>	<u>410,473</u>
Tanks and Reservoirs:		
Labor	215,602	229,972
Materials and supplies	32,115	20,394
Outside repair	56,215	45,282
Power	4,098	3,712
Total Tanks and Reservoirs	<u>308,030</u>	<u>299,360</u>
Transmission and Distribution:		
Labor	814,296	805,358
Materials and supplies	218,476	122,114
Outside repair	107,140	129,585
Power	8,913	8,327
Total Transmission and Distribution	<u>1,148,825</u>	<u>1,065,384</u>
Services:		
Labor	75,461	69,653
Materials and supplies	31,831	34,093
Outside repair	26,630	24,572
Total Services	<u>133,922</u>	<u>128,318</u>
Meters:		
Labor	550,572	506,748
Materials and supplies	31,147	40,787
Outside repair	33,065	13,739
Total Meters	<u>614,784</u>	<u>561,274</u>

VALLECITOS WATER DISTRICTSchedule of Operating Expenses - Water Division, continued
For the Fiscal Years Ended June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Backflow Prevention:		
Labor	68,079	73,432
Materials and supplies	32	2,127
Total Backflow Prevention	<u>68,111</u>	<u>75,559</u>
Customer Accounts:		
Labor	372,353	436,764
Materials and supplies	62,779	73,313
Uncollectible accounts	31,944	84,551
Outside Repair	17,903	22,254
Total Customer Accounts	<u>484,979</u>	<u>616,882</u>
Equipment and Vehicles:		
Labor, fuel and repairs	244,321	222,480
Materials and supplies	40,115	58,694
Total Equipment and Vehicles	<u>284,436</u>	<u>281,174</u>
Building and Grounds:		
Labor	186,856	195,385
Materials and supplies	79,411	50,900
Outside Repair	152,703	97,034
Power	22,776	26,209
Total Building and Grounds	<u>441,746</u>	<u>369,528</u>
Engineering:		
Labor	1,132,373	1,172,516
Materials and supplies	18,607	7,839
Outside Repair	26,327	41,417
Total Engineering	<u>1,177,307</u>	<u>1,221,772</u>
Safety:		
Labor	177,269	192,472
Materials and supplies	9,499	7,787
Safety support	8,133	14,754
Total Safety	<u>194,901</u>	<u>215,013</u>

VALLECITOS WATER DISTRICTSchedule of Operating Expenses - Water Division, continued
For the Fiscal Years Ended June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Information Technology		
Labor	296,828	275,835
Travel	1,501	1,817
Dues and subscriptions	-	1,750
Meetings and seminars	909	1,628
Other materials and supplies	33,383	39,521
Phone	17,660	21,390
Equipment Rent	22,388	25,891
Outside Repair	137,657	162,705
Total Information Technology	<u>510,326</u>	<u>530,537</u>
General and Administration:		
Salaries	1,632,194	1,542,826
Other taxes/benefits	12,259	8,771
Social security	158,784	189,356
Group insurance	529,739	571,887
Public employees' retirement	351,699	336,005
Workers' compensation insurance	33,863	31,211
District insurance	163,014	156,919
Director's expense	44,020	42,107
Director's fees	28,543	32,614
Public awareness	98,292	92,752
Travel	14,982	6,333
Postage	1,530	4,559
Office supplies	27,882	36,344
Dues and subscriptions	61,308	62,958
Meetings and seminars	23,119	16,281
Legal	131,789	209,947
Auditing	15,055	16,125
Outside services	125,576	164,492
Election and annexations	-	4,392
Other	90,811	(59,017)
Administrative credits transferred	(561,185)	(226,388)
Total General and Administration	<u>2,983,274</u>	<u>3,240,474</u>
Total Water Division Expenses	<u>\$ 33,283,213</u>	<u>\$ 31,324,184</u>

VALLECITOS WATER DISTRICTSchedule of Operating Expenses - Wastewater Division
For the Fiscal Years Ended June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Collection System:		
Labor	\$ 1,316,901	\$ 1,341,673
Materials and supplies	92,688	60,457
Chemicals	174,336	149,310
Outside repair	52,995	84,309
Power	1,505	1,613
Total Collection System	<u>1,638,425</u>	<u>1,637,362</u>
Lift Stations:		
Labor	103,000	81,460
Materials and supplies	10,662	9,923
Chemicals	24,524	12,813
Outside repair	14,901	25,864
Power	39,112	34,846
Total Lift Stations	<u>192,199</u>	<u>164,906</u>
Peroxide Station:		
Labor	851	621
Outside repair	120	122
Power	198	199
Total Peroxide Station	<u>1,169</u>	<u>942</u>
Industrial Waste:		
Labor	135,022	80,010
Materials and supplies	33,679	21,230
Total Industrial Waste	<u>168,701</u>	<u>101,240</u>
Encina Disposal	<u>2,450,330</u>	<u>2,709,307</u>
Meadowlark Lift Station:		
Labor	52,221	71,306
Materials and supplies	8,109	9,579
Chemicals	240,099	211,969
Outside repair	7,944	30,989
Power	79,778	65,964
Total Meadowlark Lift Station	<u>388,151</u>	<u>389,807</u>

VALLECITOS WATER DISTRICTSchedule of Operating Expenses - Wastewater Division, continued
For the Fiscal Years Ended June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Meadowlark Plant:		
Labor	907,801	842,614
Materials and supplies	269,229	188,870
Chemicals	611,456	471,442
Outside repair	293,474	372,086
Power	403,964	345,539
Telephone	3,247	2,856
Total Meadowlark Plant	<u>2,489,171</u>	<u>2,223,407</u>
Mahr Reservoir:		
Labor	50,736	61,056
Materials and supplies	15,943	68,946
Chemicals	8,820	
Outside repairs	40,758	34,621
Total Mahr Reservoir	<u>116,257</u>	<u>164,623</u>
Customer Accounts:		
Labor	250,831	188,855
Materials and supplies	57,560	47,811
Uncollectible accounts	15,567	17,828
Outside Services	16,868	14,903
Total Customer Accounts	<u>340,826</u>	<u>269,397</u>
Equipment and Vehicles:		
Labor, fuel and repairs	69,179	112,033
Materials and supplies	40,213	32,171
Fuel	49,999	65,497
Total Equipment and Vehicles	<u>159,391</u>	<u>209,701</u>
Buildings and Grounds:		
Labor	72,589	60,245
Materials and supplies	14,801	13,176
Outside repair	50,247	36,165
Power	20,775	17,523
Total Buildings and Grounds	<u>158,412</u>	<u>127,109</u>
Engineering:		
Labor	506,119	481,587
Materials and supplies	98	-
Outside repair	15,175	-
Total Engineering	<u>521,392</u>	<u>481,587</u>

VALLECITOS WATER DISTRICTSchedule of Operating Expenses - Wastewater Division, continued
For the Fiscal Years Ended June 30, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Safety:		
Labor	129,147	100,238
Materials and supplies	581	859
Outside services	4,203	6,344
Total Safety	<u>133,931</u>	<u>107,441</u>
Information Technology		
Labor	193,311	141,247
Materials and supplies	48,466	46,062
Outside services	113,553	113,577
Total Information Technology	<u>355,330</u>	<u>300,886</u>
General and Administration:		
Salaries	700,218	517,481
Other taxes/benefits	5,759	3,967
Social security	67,873	66,774
Group insurance	324,536	297,681
Public employees' retirement	141,620	122,171
Workers' compensation insurance	10,924	8,243
District insurance	143,953	104,613
Director's fees	21,479	26,519
Travel	16	-
Office supplies	12,456	11,594
Dues and subscriptions	203	318
Meetings and seminars	1,061	-
Legal	131,735	191,232
Auditing	14,465	8,550
Outside services	43,027	52,825
Other	10,202	750
Administrative credits transferred	(479,059)	(250,851)
Total General and Administration	<u>1,150,468</u>	<u>1,161,867</u>
Total Wastewater Division Expenses	<u>\$ 10,264,153</u>	<u>\$ 10,049,582</u>

APPENDIX B

DEFINITIONS AND SUMMARY OF PRINCIPAL LEGAL DOCUMENTS

The following is a brief summary of certain provisions of the documents pertaining to the Bonds. Such summaries are not intended to be definitive. Reference is directed to the Master Contract and the Indenture of Trust for the complete text thereof. Copies of the Master Contract and Indenture of Trust are available from the District.

Definitions

“Accountant’s Report” means a report signed by an Independent Certified Public Accountant.

“Adjusted Annual Debt Service” means, for any Fiscal Year or twelve (12) calendar month period, the Annual Debt Service for such Fiscal Year or twelve (12) calendar month period minus the amount of such Annual Debt Service paid from (i) the proceeds of Parity Obligations (other than amounts excluded from Annual Debt Service pursuant to the subparagraph (F) of the definition of “Assumed Interest Rate”), or (ii) any interest earnings on and releases of amounts on deposit in all Reserve Funds established in connection with Parity Obligations, as set forth in a Certificate of the District.

“Adjusted Annual Net Revenues” means, for any Fiscal Year or twelve (12) calendar month period, the Adjusted Annual Revenues during such Fiscal Year or twelve (12) calendar month period minus the Maintenance and Operation Costs during such Fiscal Year or twelve (12) calendar month period.

“Adjusted Annual Revenues” means, for any Fiscal Year or twelve (12) calendar month period, the Revenues during such Fiscal Year or twelve (12) calendar month period plus the withdrawals from the Rate Stabilization Account in such Fiscal Year or twelve (12) calendar month period minus the deposits into the Rate Stabilization Account in such Fiscal Year or twelve (12) calendar month period, as set forth in a Certificate of the District.

“Ad Valorem Taxes” means, for any period, the ad valorem property taxes received by the District during such period pursuant to Article XIII A of the California Constitution and Section 95 et seq. of the California Revenue and Taxation Code, including any such taxes levied to pay any voter approved general obligation indebtedness of the District.

“Annual Debt Service” means, for any Fiscal Year or twelve (12) calendar month period, the Parity Payments required to be made under all Parity Obligations in such Fiscal Year or twelve (12) calendar month period.

“Assumed Interest Rate” means the amount of interest calculated in accordance with the following provisions:

(A) Generally. Except as otherwise provided in subparagraph (B) below with respect to Variable Interest Rate Obligations, in subparagraph (C) below with respect to Obligations with respect to which a Payment Agreement is in force, and in subparagraph (D) below with respect to Balloon Obligations, interest on any Obligation will be calculated based on the actual amount of interest that is payable under such Obligation;

(B) Interest on Variable Interest Rate Obligations. Interest deemed to be payable on any Variable Interest Rate Obligations for periods when the actual interest rate can be determined will be the actual Variable Interest Rates and for periods when the actual interest rate cannot yet be determined will be calculated on the assumption that the interest rate on such Variable Interest Rate Obligations would be equal to (i) the average rate that accrued on such Variable Interest Rate

Obligations over the preceding twelve (12) months, or (ii) if the Variable Interest Rate Obligations has not been accruing interest at a variable rate for twelve (12) months, the average interest rate that accrued on any outstanding Variable Interest Rate Obligations of the District for which interest is computed on substantially the same basis during the preceding twelve (12) month period, or (iii) if no such comparable Variable Interest Rate Obligations were outstanding during the twelve (12) months preceding the date of calculation, then (x) if the interest on such Variable Interest Rate Obligations is excluded from gross income for purposes of Federal income taxation, 90% of the average rate of interest for The Bond Buyer Revenue Bond Index over the preceding twelve (12) months, or, if that index is no longer published, a similar index selected by the District and acceptable to each Credit Provider providing a Credit Support Instrument for an outstanding Obligation, or, if the District fails to select a replacement index, an interest rate equal to 80% of the yield for outstanding United States Treasury bonds having an equivalent maturity as the Variable Rate Interest Obligations, or if there are no such Treasury bonds having equivalent maturities, 80% of the lowest prevailing prime rate of any of the five largest commercial banks in the United States, ranked by assets, and (y) if interest on such Variable Interest Rate Obligations is not excluded from gross income for purposes of Federal income taxation, 110% of the yield for outstanding United States Treasury bonds having an equivalent maturity as the Variable Rate Interest Obligations, or if there are no such United States Treasury bonds having equivalent maturities, 110% of the lowest prevailing prime rate of any of the five largest commercial banks in the United States, ranked by assets;

(C) Interest on Obligations with respect to which a Payment Agreement is in force. Interest deemed to be payable on any Obligation with respect to which a Payment Agreement is in force will be based on the net economic effect on the District expected to be produced by the terms of such Obligation and such Payment Agreement, including but not limited to the effects that (i) such Obligation would, but for such Payment Agreement, be treated as an Obligation bearing interest at a Variable Interest Rate instead will be treated as an Obligation bearing interest at a fixed interest rate, and (ii) such Obligation would, but for such Payment Agreement, be treated as an Obligation bearing interest at a fixed interest rate instead will be treated as an Obligation bearing interest at a Variable Interest Rate; and accordingly, the amount of interest deemed to be payable on any Obligation with respect to which a Payment Agreement is in force will be an amount equal to the amount of interest that would be payable at the rate or rates stated in such Obligation plus the Payment Agreement Payments minus the Payment Agreement Receipts, and for the purpose of calculating as nearly as practicable the Payment Agreement Receipts and the Payment Agreement Payments under such Obligation, the following assumptions will be made:

(1) District Obligated to Pay Net Variable Payments. If a Payment Agreement has been entered into by the District with respect to an Obligation resulting in the payment of a net variable interest rate with respect to such Obligation and Payment Agreement by the District, the interest rate on such Obligation for future periods when the actual interest rate cannot yet be determined will be assumed (but only during the period the Payment Agreement is in effect) to be equal to the sum of (i) the fixed rate or rates stated in such Obligation, minus (ii) the fixed rate paid by the Qualified Counterparty to the District, plus (iii) the lesser of (A) the interest rate cap, if any, provided by a Qualified Counterparty with respect to such Payment Agreement (but only during the period that such interest rate cap is in effect) and (B) the applicable Variable Interest Rate calculated in accordance with paragraph (B) above; and

(2) District Obligated to Pay Net Fixed Payments. If a Payment Agreement has been entered into by the District with respect to an Obligation resulting in the payment of a net fixed interest rate with respect to such Obligation and Payment Agreement by the District, the interest on such Obligation will be included in the calculation of Payments (but only during the period the Payment Agreement is in effect) by including for each Fiscal Year or

twelve (12) calendar month period an amount equal to the amount of interest payable at the fixed interest rate pursuant to such Payment Agreement;

(D) Interest on Balloon Obligations. If any outstanding Obligations constitute Balloon Obligations (and such Obligations do not constitute Short-Term Obligations excluded from the calculation of the Payments pursuant to clause (E), below) or if Obligations proposed to be incurred would constitute Balloon Obligations (and such Obligations would not constitute Short-Term Obligations excluded from the calculation of the Payments pursuant to clause (E), below), then such Balloon Obligations will be treated as if the principal amount of such Obligations was amortized from the date originally incurred in substantially equal installments of principal and interest over a term of 30 years (provided, however, that the full principal amount of such Balloon Obligations will be included in making such calculation if such principal amount is due within 90 days of the date such calculation is being made); and, if interest accrues under such Balloon Obligations at other than a fixed rate, the interest rate used for such computation will be (x) if the interest on such Balloon Obligations is excluded from gross income for purposes of Federal income taxation, 90% of the average rate of interest for The Bond Buyer Revenue Bond Index over the preceding 12 months, or if that index is no longer published, a similar index selected by the District and acceptable to each Credit Provider providing a Credit Support Instrument for an outstanding Obligation, or if the District fails to select a replacement index, an interest rate equal to 80% of the yield for outstanding United States Treasury bonds having an equivalent maturity as the Balloon Obligations on the date incurred, or if there are no such United States Treasury bonds having equivalent maturities, 80% of the lowest prevailing prime rate of any of the five largest commercial banks in the United States, ranked by assets, and (y) if the interest on such Balloon Obligations is not excluded from gross income for purposes of Federal income taxation, the rate equal to 110% of the yield for outstanding United States Treasury bonds having an equivalent maturity as the Balloon Obligations, or, if there are no such United States Treasury bonds having equivalent maturities, 110% of the lowest prevailing prime rate of any of the five largest commercial banks in the United States, ranked by assets;

(E) Exclusion of Certain Short-Term Obligations. If any outstanding Obligations constitute Short-Term Obligations or if Obligations proposed to be incurred would constitute Short-Term Obligations, and such Short-Term Obligations are or will be payable only out of Revenues of the Fiscal Year in which such Short-Term Obligations are incurred, then such Short-Term Obligations will be disregarded and not included in calculating Payments;

(F) Credit for Accrued and Capitalized Interest. If amounts constituting accrued interest or capitalized interest have been deposited with the Trustee, then the interest payable from such amounts with respect to the Obligations will be disregarded and not included in calculating Payments for such Obligations.

“**Authorized Officer**” means the President or Secretary of the Board of Directors, the General Manager, Assistant General Manager, or any other person authorized by the Board of Directors of the District to perform an act or sign a document on behalf of the District under or with respect to the Indenture or the Master Contract.

“**Average Annual Debt Service**” means the sum of the Annual Debt Service for the remaining Fiscal Years to the last Fiscal Year in which any Parity Payments are due under any outstanding Parity Obligations divided by the number of such Fiscal Years.

“**Balloon Obligations**” means any Obligations 50% or more of the principal of which matures or is payable on the same date and which is not required by the instrument pursuant to which such Obligations were incurred to be amortized by payment or redemption prior to such date.

“Beneficial Owner” means any person who (a) has the power, directly or indirectly, to vote or consent with respect to, or to dispose of ownership of, any Bond (including a person holding a Bond through a nominee, depository or other intermediary), or (b) is treated as the owner of any Bond for federal income tax purposes.

“Board of Directors” means the Board of Directors of the District.

“Bonds” means all bonds secured on a parity basis by Net Revenues and authorized by, and at any time Outstanding pursuant to, the Indenture.

“Bond Obligation” means as of any given date of calculation, with respect to any Outstanding Bond or Parity Obligations, the principal amount thereof.

“Business Day” means any day other than (1) a Saturday, Sunday, or a day on which commercial banks in New York, New York or the city in which the Corporate Trust Office of the Trustee is located, is closed, and (2) for purposes of payments and other actions relating to Bonds secured by a Credit Facility, a day upon which commercial banks in the city in which is located the office of the Credit Provider at which demands for payment under the Credit Facility are to be presented are authorized or obligated by law or executive order to be closed.

“Capital Facility Fees” means capital facility, capacity, connection and other similar fees imposed by the District for the privilege of connecting any user directly or indirectly to the Enterprise.

“Certificate,” “Statement,” “Request,” “Requisition” or “Order” of the District mean, respectively, a written certificate, statement, request, requisition or order signed in the name of the District by an Authorized Officer. Any such instrument and supporting opinions or representations, if any, may, but need not, be combined in a single instrument with any other instrument, opinion or representation, and the two or more so combined will be read and construed as a single instrument.

“Closing Date” means on or about July 9, 2015.

“Code” means the Internal Revenue Code of 1986, and the regulations issued thereunder, as the same may be amended from time to time, and any successor provisions of law. Reference to a particular section of the Code will be deemed to be of reference to any successor to any such section.

“Common Reserve” means all Reserve Funds established with respect to Parity Obligations which have been designated by the District to be a part of the Common Reserve.

“Common Reserve Requirement” means, as of any date of computation by the District, an amount equal to the lowest of (i) Maximum Annual Debt Service on all outstanding Parity Obligations entitled to the benefit of the Common Reserve; (ii) 1.25 times the average Annual Debt Service on all outstanding Parity Obligations entitled to the benefit of the Common Reserve; and (iii) ten percent (10%) of the initial principal amount of all Parity Obligations entitled to the benefit of the Common Reserve; provided, however, that, if, upon issuance of a Parity Obligation entitled to the benefit of the Common Reserve, such amount would require moneys to be credited to the Common Reserve from the proceeds of such Parity Obligations in an amount in excess of the maximum amount permitted under the Code, the Common Reserve Requirement will mean an amount equal to the sum of the Common Reserve Requirement immediately preceding issuance of such Parity Obligation and the maximum amount permitted under the Code to be deposited therein from the proceeds of such Parity Obligation, as certified in a Certificate of the District.

“Continuing Disclosure Agreement” means any Continuing Disclosure Agreement executed and delivered by the District relating to any Series of Bonds.

“Contract Resource Obligation” means an obligation of the District, designated as a Contract Resource Obligation and entered into pursuant to the Master Contract, to make payments to another party for the acquisition of capacity or right of service, supply or use in or from water and wastewater facilities to be used by the District in providing the services of the Enterprise.

“Contracts” means the Master Contract and all Supplemental Contracts.

“Corporate Trust Office” means the office of the Trustee at which at any particular time its corporate trust business will be principally administered, which office at the date of the Indenture is located in Los Angeles, California or such other place as designated by the Trustee except that, with respect to presentation of Bonds for payment or for registration of transfer and exchange, such term will mean the office or agency of the Trustee at which, at any particular time, its corporate trust agency business will be conducted.

“Corporation” means the Vallecitos Water District Financing Corporation, a nonprofit public benefit corporation duly organized and existing under the laws of the State, whose members as of the date hereof are the members of the Board of Directors of the District, until a successor organization will have become such, and thereafter “Corporation” will mean such successor organization.

“Costs of Issuance” means all items of expense directly or indirectly payable by or reimbursable to the District and related to the authorization, execution, sale and delivery of any Series of Bonds, including but not limited to advertising and printing costs, costs of preparation and reproduction of documents, filing and recording fees, travel expenses and costs relating to rating agency meetings and other meetings concerning the Bonds, initial fees and charges of the Trustee, legal fees and charges, fees and disbursements of consultants and professionals, financial advisor fees and expenses, rating agency fees, fees and charges for preparation, execution, transportation and safekeeping of Bonds, surety, insurance and credit enhancement costs, and any other cost, charge or fee in connection with the delivery of Bonds.

“Costs of Issuance Fund” means the Costs of Issuance Fund established under the Indenture.

“Coverage Requirement” means, for any Fiscal Year or twelve (12) calendar month period, (i) an amount of Adjusted Annual Net Revenues which equals at least one hundred fifteen percent (115%) of the Adjusted Annual Debt Service for such Fiscal Year or twelve (12) calendar month period, and (ii) an amount of Net Revenues which equals one hundred per cent (100%) of all Payments and all other amounts which are payable from Net Revenues payable in such Fiscal Year or twelve (12) calendar month period; provided, that, for purposes of determining compliance with the Coverage Requirement, it will be assumed that all Obligations accrue interest at the applicable Assumed Interest Rate.

“Credit Facility” means an irrevocable letter of credit, bond insurance or line of credit or other similar agreement or agreements or combinations of such agreements or any other agreement or agreements used to provide credit support for any Bonds of a Series which provides for the payment of the principal and interest on, and the purchase price of, such Bonds under certain circumstances by the provider thereof, issued and delivered to the Trustee in accordance with the terms of any Supplemental Indenture and any such instrument or agreement delivered in substitution for any Credit Facility.

“Credit Provider” means any municipal bond insurance company, bank or other financial institution or organization which is performing in all material respects its obligations under any Credit Support Instrument for some or all of the Obligations.

“Credit Provider Reimbursement Obligations” means obligations of the District to pay from the Net Revenues amounts due under a Credit Support Agreement, including without limitation amounts advanced by a Credit Provider pursuant to a Credit Support Instrument as credit support or liquidity for Obligations and the interest with respect thereto.

“Credit Support Agreement” means, with respect to any Credit Support Instrument, the agreement or agreements (which may be the Credit Support Instrument itself) between the District and the applicable Credit Provider, as originally executed or as it may from time to time be replaced, supplemented or amended in accordance with the provisions thereof, providing for the reimbursement to the Credit Provider for payments under such Credit Support Instrument or for extensions of credit made to the District by the Credit Provider, and the interest thereon, and includes any subsequent agreement pursuant to which a substitute Credit Support Instrument is provided, together with any related pledge agreement, security agreement or other security document.

“Credit Support Instrument” means a policy of insurance, a letter of credit, a standby purchase agreement, revolving credit agreement or other credit arrangement pursuant to which a Credit Provider provides credit and/or liquidity support with respect to the payment of any Obligations.

“Director of Finance” means the Director of Finance of the District.

“District” means the Vallecitos Water District, a county water district duly established and existing under the Law.

“DTC” means The Depository Trust Company, New York, New York, and its successors and assigns.

“Engineer’s Report” means a report signed by an Independent Engineer.

“Enterprise” means, collectively, the Water System and the Wastewater System.

“Event of Default” means any event of default specified as such in the Indenture or the Master Contract.

“Excluded Principal Payments” means each payment of principal (or the principal component of lease or installment purchase payments) of Bonds or Parity Obligations which the District determines on a date not later than the date of issuance thereof that the District intends to pay with moneys that are not Net Revenues, but from the proceeds of future debt obligations of the District and the Trustee may rely conclusively on such determination of the District.

“First Supplemental Contract” means the First Supplemental Installment Purchase Contract, dated as of June 15, 2005, by and between the District and the Corporation, as originally executed and entered into and as it may from time to time be amended or supplemented in accordance therewith; the First Supplemental Contract is the first supplement to the Master Contract.

“Fiscal Year” means the period beginning on July 1 of each year and ending on the next succeeding June 30, or any other annual accounting period hereafter selected and designated by the Board of Directors as the Fiscal Year of the District.

“Fitch” means Fitch Ratings, Inc., a corporation duly organized and existing under and by virtue of the laws of the State of Delaware, and its successors or assigns, but only to the extent that such entity is then rating any Parity Obligations at the request of the District.

“Funds” means, collectively, the Revenue Fund, the Parity Obligation Payment Fund, the Debt Service Fund, the Reserve Fund, the Rebate Fund and the Costs of Issuance Fund created pursuant to the Indenture.

“General Obligation Bonds” means any outstanding general obligation bonds of the District, including all general obligation bonds issued prior to the date of the Master Contract, for which the voters of

the District have authorized the District to levy Ad Valorem Taxes unlimited as to rate or amount as a source of repayment for such bonds.

“Generally Accepted Accounting Principles” means the uniform accounting and reporting procedures set forth in publications of the American Institute of Certified Public Accountants or its successor, or by any other generally accepted authority on such procedures, and includes, as applicable, the standards set forth by the Governmental Accounting Standards Board or its successor.

“Government Obligations” means and include any of the following: (i) Direct obligations (other than an obligation subject to variation in principal repayment) of the United States of America (“United States Treasury Obligations”), (ii) obligations fully and unconditionally guaranteed as to timely payment of principal and interest by the United States of America, (iii) obligations fully and unconditionally guaranteed as to timely payment of principal and interest by any agency or instrumentality of the United States of America when such obligations are backed by the full faith and credit of the United States of America, or (iv) evidences of ownership of proportionate interests in future interest and principal payments on obligations described above held by a bank or trust company as custodian, under which the owner of the investment is the real party in interest and has the right to proceed directly and individually against the obligor and the underlying government obligations are not available to any person claiming through the custodian or to whom the custodian may be obligated.

“Indenture” means the Indenture of Trust, dated as of June 1, 2015, by and between the District and the Trustee, as originally executed and as it may from time to time be supplemented or amended by any Supplemental Indenture delivered pursuant to the provisions contained in the Indenture.

“Independent Certified Public Accountant” means any firm of certified public accountants duly licensed and entitled to practice and practicing as such under the laws of the State, appointed and paid by the District, and each of whom –

- (1) is in fact independent and not under the domination of the District;
- (2) does not have a substantial financial interest, direct or indirect, in the operations of the District; and
- (3) is not connected with the District as a director, officer or employee of the District, but may be regularly retained to audit the accounting records of and make reports thereon to the District.

“Independent Engineer” means any registered engineer or firm of registered engineers of national reputation generally recognized to be well qualified in engineering matters relating to water delivery and wastewater collection systems, appointed and paid by the District, and who or each of whom –

- (1) is in fact independent and not under the domination of the District;
- (2) does not have a substantial financial interest, direct or indirect, in the operations of the District; and
- (3) is not connected with the District as a director, officer or employee of the District, but may be regularly retained to make reports to the District.

“Improvement Fund” means the Fund by that name created pursuant to the Master Contract.

“Information Services” means national information services that disseminate securities prepayment notices; or, in accordance with then-current guidelines of the Securities and Exchange Commission, such other

services providing information with respect to called bonds as the District may specify in a Written Order to the Trustee.

“Installment Payments” means all installment payments scheduled to be paid by the District under Supplemental Contracts.

“Interest Payment Date” means a date on which any interest installment of the Payments is due and payable.

“Issuing Document” means any indenture, trust agreement or other document the Obligations issued or delivered pursuant to which are secured in whole or in part by Payments; provided that, if a trustee is appointed under an Issuing Document, the trustee for all Parity Obligations will be the Trustee.

“Law” means the California County Water District Law, being Division 12 of the California Water Code (commencing at California Water Code Section 30,000) and all laws amendatory thereof or supplemental thereto, including Articles 10 and 11 of Chapter 3 of Part 1 of Division 2 of Title 5 of the Government Code of the State of California

“Maintenance and Operation Costs” means, for any Fiscal Year or twelve (12) calendar month period, all reasonable and necessary costs paid or incurred by the District during such Fiscal Year or twelve (12) calendar month period for maintaining and operating the Enterprise, determined in accordance with Generally Accepted Accounting Principles, including all reasonable expenses of management and repair and other expenses necessary to maintain and preserve the Enterprise in good repair and working order, all amounts due under Contract Resource Obligations (but only under the circumstances described under the Master Contract), all administrative costs of the District that are charged directly or apportioned to the operation of the Enterprise, such as salaries and wages of employees, overhead, taxes (if any), insurance premiums and payments into pension funds, and all other reasonable and necessary costs of the District or charges required to be paid by it to comply with the terms of the Master Contract or of any resolution authorizing the execution or issuance of any Parity Obligation or of such Parity Obligation, such as compensation, reimbursement and indemnification of the Trustee and fees and expenses of Independent Certified Public Accountants and Independent Engineers, but excluding in all cases depreciation, replacement and obsolescence charges or reserves therefor and amortization of intangibles.

“Master Contract” means the Master Installment Purchase Contract, dated as of June 15, 2005, by and between the District and the Corporation, as originally executed and entered into and as it may from time to time be amended or supplemented in accordance therewith.

“Maximum Annual Debt Service” means the highest Annual Debt Service for any Fiscal Year or twelve (12) calendar month period through the final maturity date of all outstanding Parity Obligations; provided, however, for purposes of such calculation, the interest on all Parity Obligations will be computed at the applicable Assumed Interest Rate.

“Moody’s” means Moody’s Investors Service, a corporation duly organized and existing under and by virtue of the laws of the State of Delaware, and its successors or assigns, but only to the extent that such entity is then rating any Parity Obligations at the request of the District.

“Net Proceeds” means, when used with respect to any condemnation award or any insurance proceeds received with respect to the Enterprise, the amount of such condemnation award or insurance proceeds remaining after payment of all expenses (including attorneys’ fees) incurred in the collection of such award or proceeds.

“Net Revenues” means, for any Fiscal Year or twelve (12) calendar month period, the Revenues during such Fiscal Year or twelve (12) calendar month period less the Maintenance and Operation Costs during such Fiscal Year or twelve (12) calendar month period.

“Obligations” means all Parity Obligations and all Subordinate Obligations.

“Opinion of Bond Counsel” means a written opinion of a law firm of national standing in the field of public finance retained by the District.

“Outstanding” when used as of any particular time with reference to Bonds (subject to certain provisions of the Indenture relating to certain disqualified Bonds, such as Bonds held by or for the account of the District or any obligor of the Bonds other than a Credit Provider) issued pursuant to the Indenture, means all Bonds theretofore, or thereupon being, authenticated and delivered by the Trustee under the Indenture except (1) Bonds theretofore cancelled by the Trustee or surrendered to the Trustee for cancellation; (2) Bonds with respect to which all liability of the District will have been discharged pursuant to the Indenture; and (3) Bonds for the transfer or exchange of or in lieu of or in substitution for which other Bonds will have been authenticated and delivered by the Trustee pursuant to the Indenture.

“Owner” or **“Bondholder”** or **“Bondowner,”** whenever used with respect to a Bond, means the person in whose name such Bond is registered.

“Parity Obligation Payment Fund” means the fund established under the Master Contract.

“Parity Obligations” means all Bonds, Supplemental Contracts and Payment Agreements, the Parity Payments under which (other than Termination Payments) are secured by a senior lien on Net Revenues and are payable on a parity therefrom.

“Parity Payment Agreement” means a Payment Agreement which is a Parity Obligation.

“Parity Payments” means Debt Service on the Bonds and all Installment Payments or debt service to be paid by the District under other Parity Obligations.

“Parity Payments Date” means the date on which any Parity Payments are due on a Parity Obligation.

“Payment Agreement” means a written agreement for the purpose of managing or reducing the District’s exposure to fluctuations in interest rates or for any other interest rate, investment, asset or liability managing purposes, entered into either on a current or forward basis by the District and a Qualified Counterparty as authorized under any applicable laws of the State in connection with, or incidental to, the entering into of any Obligation, that provides for an exchange of payments based on interest rates, ceilings or floors on such payments, options on such payments or any combination thereof, or any similar device.

“Payment Agreement Payments” means the amounts periodically required to be paid by the District to all Qualified Counterparties under all Payment Agreements.

“Payment Agreement Receipts” means the amounts periodically required to be paid by all Qualified Counterparties to the District under all Payment Agreements.

“Payment Date” means the date designated for payment of the principal of, either at maturity or upon earlier redemption, and interest on any Bonds of a Series, as set forth in the Supplemental Indenture pursuant to which such Bonds were issued.

“Payments” means the Parity Payments and the Subordinate Payments.

“Permitted Investments” means and includes any of the following securities:

Government Obligations.

Federal Housing Administration debentures.

The listed obligations of government-sponsored agencies which are not backed by the full faith and credit of the United States of America:

Federal Home Loan Mortgage Corporation (FHLMC);

Participation certificates (excluded are stripped mortgage securities which are purchased at prices exceeding their principal amounts) Senior Debt obligations;

Farm Credit Banks (formerly: Federal Land Banks, Federal Intermediate Credit Banks and Banks for Cooperatives) Consolidated system-wide bonds and notes;

Federal Home Loan Banks (FHL Banks) Consolidated debt obligations;

Federal National Mortgage Association (FNMA) Senior debt obligations Mortgage-backed securities (excluded are stripped mortgage securities which are purchased at prices exceeding their principal amounts);

Student Loan Marketing Association (SLMA) Senior debt obligations (excluded are securities that do not have a fixed par value and/or whose terms do not promise a fixed dollar amount at maturity or call date);

Financing Corporation (FICO) Debt obligations; and

Resolution Funding Corporation (REFCORP) Debt obligations.

Deposits, unsecured certificates of deposit, time deposits, and bankers’ acceptances (having maturities of not more than 30 days) of any bank the short-term obligations of which are rated “A-1” or better by Standard & Poor’s.

Deposits the aggregate amount of which are fully insured by the Federal Deposit Insurance Corporation (FDIC), in banks which have capital and surplus of at least \$5 million.

Commercial paper (having original maturities of not more than 270 days) rated “A-1+” by Standard & Poor’s and “Prime-1” by Moody’s.

Money market funds rated “AAm” or “AAm-G” by Standard & Poor’s, or better, including funds for which the Trustee, its parent holding company, if any, or any affiliates or subsidiaries of the Trustee or such holding company, provide investment advisory or other management services.

“State Obligations,” which means:

Direct general obligations of any state of the United States of America or any subdivision or agency thereof to which is pledged the full faith and credit of a state the unsecured general obligation debt of which is rated “A3” by Moody’s and “A” by Standard & Poor’s, or better, or any obligation fully and unconditionally guaranteed by any state, subdivision or agency whose unsecured general obligation debt is so rated.

Direct general short-term obligations of any state agency or subdivision or agency thereof described in (a) above and rated “A-1+” by Standard & Poor’s and ‘MIG-1’ by Moody’s.

Special Revenue Bonds (as defined in the United States Bankruptcy Code) of any state, state agency or subdivision described in (a) above and rated “AA” or better by Standard & Poor’s and “Aa” or better by Moody’s.

Pre-refunded municipal obligations rated “AAA” by Standard & Poor’s and “Aaa” by Moody’s meeting the following requirements:

the municipal obligations are (1) not subject to redemption prior to maturity or (2) the trustee for the municipal obligations has been given irrevocable instructions concerning their call and redemption and the issuer of the municipal obligations has covenanted not to redeem such municipal obligations other than as set forth in such instructions;

the municipal obligations are secured by cash or United States Treasury Obligations which may be applied only to payment of the principal of, interest and premium on such municipal obligations;

the principal of and interest on the United States Treasury Obligations (plus any cash in the escrow) has been verified by the report of independent certified public accountants to be sufficient to pay in full all principal of, interest, and premium, if any, due and to become due on the municipal obligations (“Verification”);

the cash or United States Treasury Obligations serving as security for the municipal obligations are held by an escrow agent or trustee in trust for owners of the municipal obligations;

no substitution of a United States Treasury Obligation will be permitted except with another United States Treasury Obligation and upon delivery of a new Verification; and

the cash or United States Treasury Obligations are not available to satisfy any other claims, including those by or against the trustee or escrow agent.

Repurchase agreements:

With (1) any domestic bank, or domestic branch of a foreign bank, the long term debt of which is rated at least “A” by Standard & Poor’s and Moody’s; or (2) any broker-dealer with “retail customers” or a related affiliate thereof which broker-dealer has, or the parent company (which guarantees the provider) of which has, long-term debt rated at least “A” by Standard & Poor’s and Moody’s, which broker-dealer falls under the jurisdiction of the Securities Investors Protection Corporation; or (3) any other entity rated “A” or better by Standard & Poor’s and Moody’s and acceptable to the 2005 Insurer, provided that:

The market value of the collateral is maintained at levels and upon such conditions as would be acceptable to Standard & Poor’s and Moody’s to maintain an “A” rating in an “A” rated structured financing (with a market value approach);

The Trustee or a third party acting solely as agent therefor or for the District (the “Holder of the Collateral”) has possession of the collateral or the collateral has been transferred to the Holder of the Collateral in accordance with applicable state and federal laws (other than by means of entries on the transferor’s books);

The repurchase agreement states and an opinion of counsel is rendered at the time such collateral is delivered that the Holder of the Collateral has a perfected first priority security interest in the collateral, any substituted collateral and all proceeds thereof (in the case of bearer securities, this means the Holder of the Collateral is in possession);

All other requirements of Standard & Poor's in respect of repurchase agreements are met.

The repurchase agreement provides that if during its term the provider's rating by either Moody's or Standard & Poor's is withdrawn or suspended or falls below "A-" by Standard & Poor's or "A3" by Moody's, as appropriate, the provider must, at the direction of the District or the Trustee (who will give such direction if so directed by the 2005 Insurer), within 10 days of receipt of such direction, repurchase all collateral and terminate the agreement, with no penalty or premium to the District or Trustee.

Notwithstanding the above, if a repurchase agreement has a term of 270 days or less (with no evergreen provision), collateral levels need not be as specified in (a) above, so long as such collateral levels are 103% or better and the provider is rated at least "A" by Standard & Poor's and Moody's, respectively,

Investment agreements with a domestic or foreign bank or corporation (other than a life or property casualty insurance company) the long-term debt of which, or, in the case of a guaranteed corporation the long-term debt, or, in the case of a monoline financial guaranty insurance company, claims paying ability, of the guarantor is rated at least "AA" by Standard & Poor's and "Aa" by Moody's; provided that, by the terms of the investment agreement:

interest payments are to be made to the Trustee at times and in amounts as necessary to pay debt service (or, if the investment agreement is for the construction fund, construction draws) on the Bonds;

the invested funds are available for withdrawal without penalty or premium, at any time upon not more than seven days' prior notice; the District and the Trustee agree to give or cause to be given notice in accordance with the terms of the investment agreement so as to receive funds thereunder with no penalty or premium paid;

the investment agreement states that is the unconditional and general obligation of, and is not subordinated to any other obligation of, the provider thereof or, if the provider is a bank, the agreement or the opinion of counsel states that the obligation of the provider to make payments thereunder ranks *pari passu* with the obligations of the provider to its other depositors and its other unsecured and unsubordinated creditors;

the District or the Trustee receives the opinion of domestic counsel (which opinion is addressed to the District) that such investment agreement is legal, valid, binding and enforceable upon the provider in accordance with its terms and of foreign counsel (if applicable) in form and substance acceptable, and addressed to, the District;

the investment agreement will provide that if during its term

the provider's rating by either Standard & Poor's or Moody's falls below "AA-" or "Aa3," respectively, the provider will, at its option, within 10 days of receipt of publication of such downgrade, either (i) collateralize the investment

agreement by delivering or transferring in accordance with applicable state and federal laws (other than by means of entries on the provider's books) to the District, the Trustee or a third party acting solely as agent therefor (the "Holder of the Collateral") collateral free and clear of any third-party liens or claims the market value of which collateral is maintained at levels and upon such conditions as would be acceptable to Standard & Poor's and Moody's to maintain an "A" rating in an "A" rated structured financing (with a market value approach); or (ii) repay the principal of and accrued but unpaid interest on the investment, and

the provider's rating by either Standard & Poor's or Moody's is withdrawn or suspended or falls below "A-" or "A3," respectively, the provider must, at the direction of the District or the Trustee, within 10 days of receipt of such direction, repay the principal of and accrued but unpaid interest on the investment, in either case with no penalty or premium to the District or Trustee, and

The investment agreement states and an opinion of counsel is rendered, in the event collateral is required to be pledged by the provider under the terms of the investment agreement, at the time such collateral is delivered, that the Holder of the Collateral has a perfected first priority security interest in the collateral, any substituted collateral and all proceeds thereof (in the case of bearer securities, this means the Holder of the Collateral is in possession);

The investment agreement must provide that if during its term;

the provider defaults in its payment obligations, the provider's obligations under the investment agreement will, at the direction of the District or the Trustee, be accelerated and amounts invested and accrued but unpaid interest thereon will be repaid to the District or Trustee, as appropriate, and

the provider becomes insolvent, not pay its debts as they become due, be declared or petition to be declared bankrupt, etc. ("event of insolvency"), the provider's obligations will automatically be accelerated and amounts invested and accrued but unpaid interest thereon will be repaid to the District or Trustee, as appropriate.

The Local Agency Investment Fund or similar pooled fund operated by or on behalf of the State and which is authorized to accept investments by or on behalf of the District of the moneys held by the Trustee in any of the accounts or funds established pursuant hereto to the extent deposits and withdrawals may be made by the Trustee directly. The Trustee may restrict investments in LAIF if required to keep moneys available for the purposes of the Trust Agreement.

"President" means the President of the Board of Directors.

"Principal Payment Date" means a date on which any principal installment of the Payments is due and payable.

"Project(s)" means any additions, betterments and improvements to the Enterprise designated by the Board of Directors in a Supplemental Contract as a designated Project, the acquisition and construction of which (together with the incidental costs and expenses related thereto) will be financed or refinanced by the

proceeds of any Supplemental Contract; “Projects” means, collectively, all Projects financed or refinanced by the proceeds of the Supplemental Contracts.

“**Project Account**” means an account established in the Improvement Fund by a Supplemental Contract to finance the acquisition and construction of a Project; “Project Accounts” means, collectively, all Project Accounts established in the Improvement Fund by the Supplemental Contracts to finance the acquisition and construction of the Projects.

“**Rate Stabilization Account**” means the account established under the Master Contract.

“**Rating Agencies**” means Fitch Inc., Moody’s Investor’s Service and Standard & Poor’s Rating Services, and their successors and assigns, or the agency or agencies then providing a rating on the Bonds; if any Rating Agency ceases to act as a securities rating agency, the District may appoint any other nationally recognized securities rating agency as a replacement.

“**Rebate Fund**” means the Fund by that name created pursuant to the Indenture.

“**Rebate Fund**” means that fund established under Indenture.

“**Rebate Requirement**” means the Rebate Requirement defined in the Tax Certificate.

“**Redemption Price**” means, with respect to any Bond (or portion thereof) the Bond Obligation of such Bond (or portion thereof) plus the applicable premium, if any, payable upon redemption thereof pursuant to the provisions of such Bond and the Indenture.

“**Reserve Fund**” means the Fund by that name created pursuant to the Indenture.

“**Reserve Fund Credit Facility Costs**” means the repayment of draws, expenses and accrued interest or other similar costs payable in connection with a line of credit, letter of credit, insurance policy, surety bond or other credit source deposited with the Trustee for the credit of a Reserve Fund.

“**Revenue Fund**” means the fund established under the Master Contract.

“**Revenues**” means, for any Fiscal Year or twelve (12) calendar month period, all income and revenue received or receivable by the District during such Fiscal Year or twelve (12) calendar month period from the ownership or operation of the Enterprise, determined in accordance with Generally Accepted Accounting Principles, including all Ad Valorem Taxes, ad valorem assessments, Capital Facility Fees, standby charges, rates, fees and charges received by the District for the Service, all proceeds of insurance covering business interruption loss relating to the Enterprise, all connection fees and charges payable to the District for the Service made available or provided by the Enterprise, all payments for the lease of property comprising a part of the Enterprise, all other income and revenue howsoever derived by the District from the ownership or operation of the Enterprise or arising from the Enterprise, all Payment Agreement Receipts, and all income from the investment of amounts on deposit in the Revenue Fund and the Parity Obligation Payment Fund, but excluding in all cases: (i) any proceeds of taxes (including Ad Valorem Taxes) and assessments levied and collected by or on behalf of the District for obligations that are payable solely from such taxes or assessments and not from any other Revenues, (ii) any refundable deposits made to establish credit and any advances or contributions in aid of construction, and (iii) any income from the investment of amounts on deposit in the Improvement Fund.

“**Second Supplemental Contract**” means the Second Supplemental Installment Purchase Contract, dated as of December 1, 2012, by and between the District and the Corporation, as originally executed and entered into and as it may from time to time be amended or supplemented in accordance therewith; the Second Supplemental Contract is the second supplement to the Master Contract.

“Securities Depositories” means the following: The Depository Trust Company, 55 Water Street, 50th Floor, New York, New York 10041-0099, Attention: Call Notification Department, Fax (212) 855-7232; or, in accordance with then-current guidelines of the Securities and Exchange Commission, to such other addresses and/or such other securities depositories, or no such depositories, as the District may designate in a request of the District delivered to the Trustee.

“Separate Reserve Fund” means a Reserve Fund, created pursuant to an Issuing Document for a Parity Obligation, that is not a part of the Common Reserve.

“Serial Bonds” means Bonds, maturing in specified years, for which no mandatory sinking fund payments are provided.

“Series” whenever used with respect to Bonds issued pursuant to the Indenture, means all of the Bonds designated as being of the same series, authenticated and delivered in a simultaneous transaction, regardless of variations in maturity, interest rate, redemption and other provisions, and any Bonds thereafter authenticated and delivered upon transfer or exchange or in lieu of or in substitution for (but not to refund) such Bonds as provided in the Indenture.

“Service” means the Water System and Wastewater System services furnished, made available or provided by the Enterprise.

“Short-Term Obligations” means Obligations having an original maturity of less than or equal to one year and which are not renewable at the option of the District for a term greater than one year beyond the date of original incurrence.

“Standard & Poor’s” means Standard and Poor’s Ratings Services, a Standard & Poor’s Financial Services LLC business, its successors or assigns, but only to the extent that such entity is then rating any Parity Obligations at the request of the District.

“State” means the State of California.

“Subordinate Obligations” means all Bonds, Supplemental Contracts or Payment Agreements the Subordinate Payments under which (other than Termination Payments related to Subordinate Payment Agreements) are secured by the subordinate lien on Net Revenues created by the Master Contract and are payable on a parity therefrom.

“Subordinate Payment Agreements” means a Payment Agreement which is a Subordinate Obligation.

“Subordinate Payments” means all Installment Payments and other debt service payments scheduled to be paid by the District under all Subordinate Obligations.

“Supplemental Contracts” means all installment purchase contracts supplemental to the Master Contract executed and entered into by the District and the Corporation.

“Supplemental Indenture” means any indenture hereafter duly executed and delivered, supplementing, modifying or amending the Indenture, but only if and to the extent that such Supplemental Indenture is specifically authorized in accordance with the provisions of the Indenture.

“Tax Certificate” means the Tax Certificate delivered by the District at the time of the issuance and delivery of any Series of Bonds, as the same may be amended or supplemented in accordance with its terms.

“Term Bonds” means Bonds payable at or before their specified maturity date or dates from mandatory sinking fund payments established for that purpose and calculated to retire such Bonds on or before their specified maturity date or dates.

“Trustee” means MUFG Union Bank, N.A., a national banking association organized under the laws of the United States of America, and its successor or successors under the Indenture.

“Variable Interest Rate” means any variable interest rate or rates to be paid under any Obligations, the method of computing which variable interest rate will be as specified in the applicable Obligation, which Obligation will also specify either (i) the payment period or periods or time or manner of determining such period or periods or time for which each value of such variable interest rate will remain in effect, and (ii) the time or times based upon which any change in such variable interest rate will become effective, and which variable interest rate may, without limitation, be based on the interest rate on certain bonds or may be based on interest rate, currency, commodity or other indices.

“Variable Interest Rate Obligations” means, for any period of time, any Obligations that bear a Variable Interest Rate during such period, except that no Obligation will be treated as a Variable Interest Rate Obligations if the net economic effect of interest rates on any particular Payments or such Obligation and interest rates on any other Payments of the same Obligation, as set forth in such Obligation, or the net economic effect of a Payment Agreement with respect to any particular Payments, in either case is to produce obligations that bear interest at a fixed interest rate, and any Obligation with respect to which a Payment Agreement is in force will be treated as a Variable Interest Rate Obligations if the net economic effect of the Payment Agreement is to produce obligations that bear interest at a Variable Interest Rate.

“Wastewater System” means all property rights, contractual rights and facilities of the District for the collection, conveyance, treatment and/or disposal of wastewater now owned by the District and all other property rights, contractual rights and facilities acquired or constructed by the District and determined to be a part of the Wastewater System, together with all additions, betterments and improvements to such facilities or any part thereof acquired or constructed by the District.

“Water System” means all property rights, contractual rights and facilities of the District for the production, treatment, conservation, storage, transmission and/or distribution of water and the generation and delivery of hydroelectric power in connection therewith now owned by the District and all other property rights, contractual rights and facilities acquired or constructed by the District and determined to be a part of the Water System, together with all additions, betterments and improvements to such facilities or any part thereof acquired or constructed by the District.

“2005 Installment Payments” has the meaning ascribed thereto in the Recitals to this First Supplement.

“2015 Bonds” means the Vallecitos Water District Water and Wastewater System 2015 Refunding Revenue Bonds, as described in the Indenture.

MASTER CONTRACT

Acquisition, Construction and Sale of Projects; Funds and Pledge.

Acquisition, Construction and Sale of Projects. The Corporation agrees to cause the Projects to be acquired, constructed and installed by the District, as agent of the Corporation, and to sell the Projects to the District, and the District agrees to buy the Projects from the Corporation; and in order to implement this provision, the Corporation appoints the District as its agent for the purpose of such acquisition and construction, and the District agrees to enter into such construction contracts and purchase orders as may be necessary, as agent for the Corporation, to provide for the complete acquisition and construction of the

Projects, and the District agrees that as such agent it will cause the acquisition and construction of the Projects to be diligently completed after the deposit of funds in the Improvement Fund for such purpose under the Master Contract, and that it will use its best efforts to cause the acquisition and construction of the Projects to be completed in a timely fashion, except for unforeseeable delays beyond the reasonable control of the District. Notwithstanding the foregoing, it is by the Master Contract expressly understood and agreed that the Corporation will be under no liability of any kind or character whatsoever for the payment of any costs or expenses incurred by the District for the acquisition and construction of the Projects and that all such costs and expenses will be paid by the District, regardless of whether the funds deposited in the Improvement Fund are sufficient to cover all such costs and expenses.

Changes to the Project. The District may make any changes in the composition and description of any Project or any component thereof whenever the District deems such changes to be necessary and appropriate; provided, however, that no such change will impair the ability of the District to make Payments or cause to be included in any Project any property not constituting property useful in the performance of the District's powers, projects and purposes.

Improvement Fund. There is established by the Master Contract the "Vallecitos Water District Improvement Fund," which fund the District agrees to hold and maintain until the completion of the acquisition and construction of all Projects to be financed from the Project Accounts established in such fund as provided in all Supplemental Contracts; and all money in the Improvement Fund (and interest earnings thereon) will be used and withdrawn by the District to pay the costs of the acquisition and construction of the Projects (or to reimburse the District for such costs paid by it). After the completion of the acquisition and construction of each Project to be financed from the related Project Account in the Improvement Fund, any remaining balance of money in such Project Account will be transferred to the District for any lawful purpose of the District subject to the provisions of any Tax Certificate.

Reserve Funds. In each Supplemental Contract, the District may direct that a Reserve Fund be established. With respect to each Reserve Fund established with respect to a Parity Obligation, the District may elect to treat such Reserve Fund as a part of the Common Reserve securing all Parity Obligations designated by the District to participate in the Common Reserve. Each time that the District elects to secure Parity Obligations with the Common Reserve, it will deposit funds in the Common Reserve in an amount sufficient to increase the balance in the Common Reserve to the Common Reserve Requirement calculated to take into account such additional Parity Obligations. If the District establishes a Reserve Fund for any Parity Obligation but does not elect to make such Reserve Fund a part of the Common Reserve, then any Reserve Fund so established will be a Separate Reserve Fund and will secure only the Parity Obligations for which such Reserve Fund was created. The District may establish a separate Reserve Fund for an issue of Subordinate Obligations which will secure only the Subordinate Obligations for which such Reserve Fund was created or may create a common Reserve Fund to secure more than one issue of Subordinate Obligations.

The Trustee may withdraw amounts from the Common Reserve in accordance with each Issuing Document to make payments to the owners of the Parity Obligations issued under the Issuing Document when due.

Revenue Fund; Pledge of Net Revenues. There is established by the Master Contract the "Vallecitos Water District Revenue Fund," which fund may be the General Fund of the District and which fund the District agrees to hold and maintain so long as any Payments due under the Master Contract will be Outstanding. The District irrevocably grants and pledges the Net Revenues first, to secure Parity Obligations and second, to secure Subordinate Obligations, provided that, out of Net Revenues there may be apportioned such sums for such purposes as are expressly permitted by the Master Contract. Such lien and pledge will constitute a first lien on Net Revenues. The District represents and states that it has not previously granted any lien or charge on any of the Net Revenues. All Parity Obligations will be of equal rank without preference, priority or distinction of any Parity Obligations over any other Parity Obligations. Unless expressly stated to the contrary in a particular Subordinate Obligation, all Subordinate Obligations will be of equal rank without preference,

priority or distinction of any Subordinate Obligations over any other Subordinate Obligations. In order to carry out and effectuate the obligation of the District contained in the Master Contract and in all Obligations to pay the Payments, the District agrees and covenants that all Revenues received by it will be deposited when and as received in the Revenue Fund. Additionally, amounts may, from time to time as the District deems necessary or appropriate, be transferred from the Rate Stabilization Account and deposited in the Revenue Fund. All money on deposit in the Revenue Fund will be applied and used only in the following order:

(A) The District will pay all Maintenance and Operation Costs (including amounts reasonably required to be set aside in contingency reserves for Maintenance and Operation Costs the payment of which is not then immediately required) from the Revenue Fund as they become due; and

(B) On or before the fifth Business Day immediately preceding each Interest Payment Date and Principal Payment Date, the District will, from the remaining money then on deposit in the Revenue Fund, deposit in the "Vallecitos Water District Parity Obligation Payment Fund," which fund the District agrees to hold and maintain so long as any Parity Payments due under the Master Contract will be Outstanding, the following amounts in the following order of priority:

(1) a sum equal to (A) the interest and principal payments becoming due and payable under all Parity Obligations, plus (B) the net payments becoming due and payable on all Parity Payment Agreements (except any Termination Payments), plus (C) any other amounts due with respect to Parity Obligations (including any letter of credit and remarketing fees), in each case, during the next succeeding month; plus

(2) all amounts due to make up any deficiency in the Reserve Funds for Parity Obligations in accordance with the provisions of the applicable Issuing Document, including all Reserve Fund Credit Facility Costs.

From time to time, moneys on deposit in the Parity Obligation Payment Fund will be transferred by the District to the Trustee or other third party payee thereof in accordance with the terms of the Parity Obligations to make and satisfy the Parity Payments due on the next applicable Payment Dates on such Parity Obligations. In the event that any Parity Obligation has been paid from amounts made available pursuant to a Credit Support Instrument, moneys on deposit in the Parity Obligation Payment Fund, and any such amounts transferred by the District from the Parity Obligation Property Fund to the Trustee or other third party payee for such Parity Obligation pursuant to the Master Contract, will be paid to the applicable Credit Provider as a Credit Support Reimbursement Obligation for the amounts so paid.

(C) After the payments contemplated by subparagraphs (A) and (B) above have been made, any amounts thereafter remaining in the Revenue Fund will be used for the payment of the interest and principal payments becoming due and payable under all Subordinate Obligations and the net payments becoming due and payable on all Subordinate Payment Agreements (except any Termination Payments) and any other amounts becoming due and payable with respect to Subordinate Obligations (including any letter of credit and remarketing fees and any other amounts becoming due and payable to make up any deficiency in the Reserve Funds for Subordinate Obligations, including all Reserve Fund Credit Facility Costs, or any Credit Support Reimbursement Obligations with respect to Subordinate Obligations) and any Termination Payments on Parity Payment Agreements; so long as the following conditions are met:

(1) all Maintenance and Operations Costs are being and have been paid and are then current; and

(2) all deposits and payments contemplated by subparagraphs (A) and (B) above will have been made in full and no deficiency in any Reserve Fund for Parity Obligations will exist and no Reserve Fund Credit Facility Costs or Credit Support Reimbursement Obligations with respect to Parity

Obligations will be due and payable, and there will have been paid, or segregated within the Revenue Fund, the amounts currently payable pursuant to subparagraphs (A) and (B) above.

(D) After deposits contemplated by subparagraphs (A), (B) and (C) have been made, any amounts thereafter remaining in the Revenue Fund may be used for any lawful purpose, including, but not limited to (i) the payment of any Termination Payments on Subordinate Payment Agreements or (ii) transfer to the Rate Stabilization Account.

Rate Stabilization Account. If and when it deems the establishment of such an account to be necessary or appropriate for the management of its financial affairs, the District may establish and maintain an account designated the "Vallecitos Water District Rate Stabilization Account." The District may at any time, as determined by the District, deposit in the Rate Stabilization Account any Revenues (subject to the satisfaction of the requirements of the Master Contract) and any other money received and available to be used therefor, and the District may at any time withdraw any or all of the money from the Rate Stabilization Account for inclusion in Adjusted Annual Revenues; provided, that any such withdrawal may be made up to and including the date one hundred and eighty (180) days after the end of the Fiscal Year for which the withdrawal will be included as Adjusted Annual Revenues.

Additional Obligations

Conditions for the Execution of Parity Obligations. The District may at any time issue or execute any Parity Obligations (other than the Parity Obligations represented by the First Supplemental Contract) payable as provided in the Master Contract; provided:

(A) There will be on file with the District either:

(1) A Certificate of the District demonstrating that, during the last audited Fiscal Year or any consecutive twelve (12) calendar month period during the immediately preceding eighteen (18) calendar month period, the Adjusted Annual Net Revenues were at least equal to 115% of Maximum Annual Debt Service on all outstanding Parity Obligations plus the Parity Obligations proposed to be issued or executed; provided, that for the purpose of providing this Certificate, the District may adjust the foregoing Adjusted Annual Net Revenues to reflect:

(a) An allowance for Net Revenues that would have resulted from any increase or decrease in the rates, fees and charges fixed and prescribed for Service which, during any part of such Fiscal Year or twelve (12) calendar month period, was not in effect, in an amount equal to the estimated change in Net Revenues that would have resulted from such increase or decrease in rates, fees and charges if it had been in effect for the entire Fiscal Year or twelve (12) calendar month period, and

(b) An allowance for Net Revenues that would have been derived from each new use or user of the Enterprise that, during any part of such Fiscal Year or twelve (12) calendar month period, was not in existence, in an amount equal to the estimated additional Net Revenues that would have been derived from each such new use or user if it had been in existence for the entire Fiscal Year or twelve (12) calendar month period; or

(2) An Engineer's Report that the estimated Adjusted Annual Net Revenues for each of the five (5) Fiscal Years next following the earlier of (i) the end of the period during which interest on the Parity Obligations proposed to be issued or executed is to be capitalized or, if no interest is capitalized, the Fiscal Year in which the Parity Obligations proposed to be issued or executed is issued or executed, or (ii) the date on which substantially all Projects financed with the Parity Obligations proposed to be issued or executed are expected to commence operations, will be at least equal to 115% of the Maximum Annual Debt Service for such period; provided, that for the purpose of providing this Engineer's Report, the Independent Engineer may adjust the foregoing estimated Adjusted Annual Net Revenues to reflect:

(a) An allowance for Net Revenues that are estimated to result from any increase or decrease in the rates, fees and charges for Service then in effect and being charged, or from any increase or decrease in the rates, fees and charges for Service that are expected to become effective and be charged, and

(b) An allowance for Net Revenues that are estimated to be derived from additional use or users of the Enterprise anticipated to be served by the additions, betterments or improvements to the Enterprise to be financed by the Parity Obligations proposed to be executed together with any additional Supplemental Contracts expected to be issued or executed into during such five (5)-year period.

(B) Without regard to paragraph (A) above, the District may, at any time and from time to time, enter into Credit Support Agreements or otherwise become obligated for Credit Provider Reimbursement Obligations with respect to Parity Obligations.

Notwithstanding the foregoing provisions, there will be no limitations on the ability of the District to issue or execute any Parity Obligations at any time to refund any outstanding Parity Obligations so long as the Annual Debt Service payable by the District for each Fiscal Year with respect to such refunding Parity Obligations is less than or equal to 105% of the Annual Debt Service for each corresponding Fiscal Year for such Parity Obligations being refunded.

Conditions for the Execution of Subordinate Obligations. The District may at any time issue or execute any Subordinate Obligations payable as provided in the Master Contract; provided that no Event of Default has occurred and is continuing; and provided, further, that, upon the issuance or execution of such Subordinate Obligations, the District will continue to satisfy the test contained in paragraph (ii) of the definition of "Coverage Requirement."

Procedure for the Execution or Issuance of Additional Obligations. Before the execution of any Supplemental Contract (other than the First Supplemental Contract) or other Issuing Document, there will first be delivered to the Director of Finance the following documents or money or securities:

- (A) An executed counterpart of the Supplemental Contract or other Issuing Document;
- (B) A Request of the District as to the delivery of such Supplemental Contract or other Issuing Document;
- (C) An Opinion of Counsel to the effect that the Supplemental Contract or other Issuing Document has been duly and lawfully executed and delivered by the District in accordance with the Law and with the Master Contract, is in full force and effect and is valid and binding upon the District and enforceable in accordance with its terms (except as enforcement may be limited by bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, the application of equitable principles, the exercise of judicial discretion in appropriate cases and the limitations on legal remedies against public agencies in the State);
- (D) A Certificate of the District containing such statements as may be reasonably necessary to show compliance with the requirements of the Master Contract; and
- (E) Such further documents, money and securities as are required by the provisions of the Master Contract and the resolution, indenture, contract or other instrument providing for the issuance of the Obligation.

Covenants of the District

Compliance with Contracts. The District will punctually pay the Payments in strict conformity with the terms of the Master Contract, and will faithfully observe and perform all the agreements, conditions, covenants and terms contained in the Master Contract required to be observed and performed by it, and will not terminate the Contracts for any cause including, without limiting the generality of the foregoing: any acts or circumstances that may constitute failure of consideration, destruction of or damage to the Projects or the Enterprise; commercial frustration of purpose; any change in the tax or other laws of the United States of America or of the State or any political subdivision of either of them; any failure of the Corporation to observe or perform any agreement, condition, covenant or term contained in the Master Contract required to be observed and performed by it, whether express or implied, or any duty, liability or obligation arising out of or connected with the Master Contract; the insolvency, or deemed insolvency, or bankruptcy or liquidation of the Corporation or the Trustee; any force majeure, including acts of God, tempest, storm, earthquake, war, rebellion, riot, civil disorder, acts of public enemies, blockade or embargo, strikes, industrial disputes, lockouts, lack of transportation facilities, fire, explosion; or any acts or regulations of governmental authorities.

Use of Proceeds. The Corporation and the District agree that the proceeds of the Supplemental Contracts will be used by the District, as agent for the Corporation, to pay the costs of financing or refinancing the acquisition and construction of the Projects and to pay the incidental costs and expenses related thereto as provided in the Master Contract.

Against Encumbrances. The District will not mortgage or otherwise encumber, pledge or place any charge upon the Enterprise or any part thereof, or upon any of the Revenues that would impair the District's ability to comply with its obligations under the Contracts.

So long as any Obligations of the District are outstanding, the District will not issue or incur Obligations payable from Revenues or secured by a pledge, lien or charge upon Revenues, except as provided in the Master Contract.

Against Sale or Other Disposition of Property. The District will not sell, lease or otherwise dispose of the Enterprise or any part thereof essential to the proper operation of the Enterprise or to the maintenance of Revenues; provided, however, that any real or personal property which has become non-operative or which is not needed for the efficient and proper operation of the Enterprise, or any material or equipment which has become worn out, may be sold if such sale will not materially reduce Net Revenues and if the proceeds of such sale are deposited in the Revenue Fund. The District will not enter into any agreement or lease which impairs the operation of the Enterprise or any part thereof necessary to secure adequate Revenues for the payment of Obligations or which would otherwise impair the rights of the Corporation with respect to Revenues or the operation of the Enterprise.

Prompt Acquisition and Construction of the Projects. The District will take all necessary and appropriate steps to acquire and construct the Projects, as agent of the Corporation, with all practicable dispatch and in an expeditious manner and in conformity with law so as to complete the same as soon as possible.

Maintenance and Operation of the Enterprise; Budgets. The District will maintain and preserve the Enterprise in good repair and working order at all times and in accordance with sound engineering practices, will operate the Enterprise in an efficient and economical manner, and will pay all Maintenance and Operation Costs as they become due and payable. The District will adopt and file with the Corporation, not later than 90 days after the start of each Fiscal Year, a budget approved by the Board of Directors setting forth the estimated Revenues and Maintenance and Operation Costs for the then current Fiscal Year; provided, that any such budget may be amended at any time during any Fiscal Year and such amended budget will be filed by the District with the Corporation.

Compliance with Contracts for Use of the Enterprise. The District will comply with, keep, observe and perform all agreements, conditions, covenants and terms, express or implied, required to be performed by it contained in all contracts for the use of the Enterprise and all other contracts affecting or involving the Enterprise to the extent that the District is a party thereto.

Investment of Amounts in Funds. The District covenants to invest amounts in the Revenue Fund, the Parity Obligation Payment Fund and the Improvement Fund only in Permitted Investments.

Insurance. The District will procure and maintain such insurance relating to the Enterprise which it deems advisable or necessary to protect its interests and the interests of the Corporation and the Trustee, which insurance will afford protection in such amounts and against such risks as are usually covered in the State in connection with water and wastewater enterprises comparable to the Enterprise; provided, that any such insurance may be maintained under a self-insurance program so long as such self-insurance is maintained in the amounts and manner usually maintained in connection with water and wastewater enterprises in the State comparable to the Enterprise and is, in the opinion of an accredited actuary, actuarially sound. All policies of insurance required to be maintained in the Master Contract will provide that the Corporation and the Trustee will be given thirty (30) days' written notice of any intended cancellation or reduction of coverage provided thereby.

Accounting Records; Financial Statements and Other Reports.

(A) The District will keep appropriate accounting records in which complete and correct entries will be made of all transactions relating to the Enterprise, the Revenues and the Maintenance and Operation Costs, which records will be available for inspection by the Corporation and the Trustee at reasonable hours and under reasonable conditions.

(B) The District will prepare and file with the Corporation and the Trustee annually within two hundred ten (210) days after the close of each Fiscal Year (commencing with the Fiscal Year ending June 30, 2005) financial statements of the District for the preceding Fiscal Year prepared in accordance with Generally Accepted Accounting Principles, together with an Accountant's Report thereon and a special report prepared by the Independent Certified Public Accountant who examined such financial statements stating that nothing came to his attention in connection with such examination that caused him to believe that the District was not in compliance with any of the financial agreements or covenants contained in the Master Contract.

Protection of Security and Rights of the Corporation. The District will preserve and protect the security of the Master Contract and the rights of the Corporation to the Payments under the Master Contract and will warrant and defend such rights against all claims and demands of all persons.

Payment of Taxes and Compliance with Governmental Regulations. The District will pay and discharge all taxes, assessments and other governmental charges which may after the Master Contract be lawfully imposed upon the Enterprise or any part thereof when the same become due. The District will duly observe and conform with all valid regulations and requirements of any governmental authority relative to the operation of the Enterprise or any part thereof, but the District will not be required to comply with any regulations or requirements so long as the validity or application thereof is contested in good faith.

Amount of Rates, Fees and Charges. The District will at all times fix, prescribe and collect rates, fees and charges for the Service during each Fiscal Year which are reasonably fair and nondiscriminatory and which are estimated to yield Adjusted Annual Net Revenues and Net Revenues, as applicable, for such Fiscal Year in an amount not less than the Coverage Requirement for such Fiscal Year. The District may make adjustments from time to time in such fees and charges and may make such classification thereof as it deems necessary, but will not reduce the rates, fees and charges then in effect unless the Adjusted Annual Net

Revenues from such reduced rates, fees and charges are estimated to be sufficient to meet the requirements of the Master Contract.

Collection of Rates, Fees and Charges. The District will have in effect at all times rules and regulations requiring each consumer or customer located on any premises connected with the Enterprise to pay the rates, fees and charges applicable to the Service to such premises and providing for the billing thereof and for a due date and a delinquency date for each bill. The District will not permit any part of the Enterprise or any facility thereof to be used or taken advantage of free of charge by any corporation, firm or person, or by any public agency (including the United States of America, the State and any city, county, district, political subdivision, public corporation or agency of any thereof); provided, that the District may without charge use the Enterprise and, so long as no Event of Default exists under the Master Contract, may waive or reduce rates, fees and charges for one or more customers and consumers so long as the total amount waived or reduced does not exceed 1% of Revenues collected in the most recent Fiscal Year and such waiver or reduction, upon implementation, will not cause the District to be in default of its covenant under the Master Contract.

Eminent Domain and Insurance Proceeds. If all or any part of the Enterprise is taken by eminent domain proceedings, or if the District receives any insurance proceeds resulting from a casualty loss to the Enterprise, the Net Proceeds thereof, at the option of the District, is applied either to the prepayment of the Payments or to acquire and construct additions, betterments or improvements to the Enterprise to replace the condemned or destroyed portion of the Enterprise.

Contact Resource Obligations. The District may at any time enter into one or more Contract Resource Obligations related to existing facilities or facilities to be constructed. The District may determine that, and may agree under a Contract Resource Obligation to provide that, all payments under that Contract Resource Obligation will be Maintenance and Operation Costs if the following requirements are met at the time such a Contract Resource Obligation is entered into:

- (A) No Event of Default as defined in the Master Contract has occurred and is continuing;
- (B) There is on file a certificate of an Independent Engineer stating that (i) the payments to be made by the District in connection with the Contract Resource Obligation are reasonable; (ii) the facilities, services, supply or use for which the Contract Resource Obligation will be incurred are technically and economically feasible and are available or are likely to be available no later than a date set forth in the Independent Engineer's certification; and (iii) the Adjusted Annual Net Revenues (further adjusted by the Independent Engineer's estimate of the payments to be made in accordance with the Contract Resource Obligation) for the five (5) Fiscal Years following the year in which the Contract Resource Obligation is incurred, as such Adjusted Annual Net Revenues are estimated by the Independent Engineer in accordance with the provisions of and adjustments permitted in the Master Contract, will be at least equal to the Coverage Requirement; and
- (C) Payments required to be made under Contract Resource Obligations are not subject to acceleration.

Nothing in the Master Contract will be deemed to prevent the District from treating any obligation it has to make payments to another party existing on the date of the Master Contract, for the acquisition of capacity, right of service, supply or use in water or wastewater facilities and used by the District in providing the services of the Enterprise, as Maintenance and Operation Costs; and nothing in the Master Contract will be deemed to prevent the District from entering into any obligation to make payments to another party for the acquisition of capacity, right of service or use in water or wastewater facilities and to be used by the District in providing the services of the Enterprise, payments under which constitute a lien and charge on Net Revenues subordinate to that of the Contracts.

Additional Covenants. The District may provide additional covenants pursuant to any Obligations, including covenants relating to any Credit Support Instrument obtained for Obligations; provided, however, that such additional covenants do not materially and adversely affect the right of holders of outstanding Obligations.

Further Assurances. The District will adopt, deliver, execute and make any and all further assurances, instruments and resolutions as may be reasonably necessary or proper to carry out the intention or to facilitate the performance of the Master Contract and for the better assuring and confirming unto the Corporation of the rights and benefits provided to it in the Master Contract.

Events of Default and Remedies

Events of Default. If one or more of the following Events of Default will happen, that is to say –

(A) if default is made in the due and punctual payment of any Payment under any Parity Obligation when and as the same will become due and payable;

(B) if default is made by the District in the performance of any of the agreements or covenants contained in the Master Contract, other than as described in clause (A) above, or in any Parity Obligation required to be performed by it, and such default will have continued for a period of thirty (30) days after the District will have been given notice in writing of such default by the Corporation or the Trustee; or

(C) if the District files a petition or answer seeking arrangement or reorganization under the federal bankruptcy laws or any other applicable law of the United States of America or any state, or if a court of competent jurisdiction approves a petition filed with or without the consent of the District seeking arrangement or reorganization under the federal bankruptcy laws or any other applicable law of the United States of America or any state, or if under the provisions of any other law for the relief or aid of debtors any court of competent jurisdiction will assume custody or control of the District or of the whole or any substantial part of its property, then and in each and every such case during the continuance of such Event of Default specified in clause (A) above, the Corporation will, and for any other such Event of Default the Corporation may, by notice in writing to the District given not later than three (3) Business Days after it receives notice of an Event of Default or direction to proceed under an Event of Default, declare an Event of Default under the Master Contract; provided, that if at any time after an Event of Default has been declared and before any judgment or decree for the payment of the money due has been obtained or entered the District will deposit with the Corporation a sum sufficient to pay the unpaid principal amount of the Payments due and payable prior to such declaration and the accrued interest thereon, with interest on such overdue installments at the rate or rates applicable to such unpaid principal amounts of the Payments if paid in accordance with their terms, and the reasonable expenses of the Corporation, and any and all other defaults known to the Corporation has been made good or cured to the satisfaction of the Corporation or provision deemed by the Corporation to be adequate will have been made therefor, then and in every such case the Corporation, by written notice to the District, may rescind and annul such declaration of an Event of Default and its consequences; but no such rescission and annulment will extend to or will affect any subsequent default or will impair or exhaust any right or power consequent thereon.

The payment of principal and interest on the Payments will not be accelerated upon the declaration of an Event of Default under the Master Contract.

Application of Net Revenues Upon Event of Default. All Net Revenues upon the date of the declaration of an Event of Default by the Corporation, as provided in the Master Contract and all Net Revenues thereafter received will be applied in the following order –

First, to the payment of the fees, costs and expenses of the Corporation and the Trustee, if any, in carrying out the provisions of the Master Contract, including reasonable compensation to its agents, accountants and counsel and including any indemnification expenses;

Second, to the payment of the interest then due and payable on the principal amount of the unpaid Parity Payments (except any Termination Payments) and any unpaid Credit Support Reimbursement Obligations representing reimbursement for interest payments paid with respect to Parity Payments from amounts made available pursuant to a Credit Support Instrument for such Parity Payments, and, if the amount available is not sufficient to pay in full all such interest then due and payable, then to the payment thereof ratably, according to the amounts due thereon without any discrimination or preference;

Third, to the payment of the unpaid principal amount of the Parity Payments (except any Termination Payments) and any unpaid Credit Support Reimbursement Obligations representing reimbursement for principal payments paid with respect to Parity Payments from amounts made available pursuant to a Credit Support Instrument for such Parity Payments then due and payable, with interest on the overdue principal at the rate or rates of interest then applicable to such Parity Payments if paid in accordance with their terms, and, if the amount available is not sufficient to pay in full all the amounts due with respect to the Parity Payments on any date, together with such interest, then to the payment thereof ratably, according to the principal amount due on such date, without any discrimination or preference;

Fourth, to the payment of any other amounts becoming due and payable with respect to Parity Obligations (including any letter of credit and remarketing fees);

Fifth, to the payment of the Subordinate Payments (except any Termination Payments) then due and payable and any other amounts becoming due and payable with respect to Subordinate Obligations (including any letter of credit and remarketing fees) and any Termination Payments on all Parity Payment Agreements; and

Sixth, to the payment of all other amounts due and payable by the District, including, but not limited to the payment of any Termination Payments on all Subordinate Payment Agreements.

Other Remedies. The Corporation will have the right –

(A) by mandamus or other action or proceeding or suit at law or in equity to enforce its rights against the District or any Board of Director, officer or employee thereof, and to compel the District or any such Director, officer or employee to perform and carry out its or his duties under the Law and the agreements and covenants required to be performed by it or him contained in the Master Contract;

(B) by suit in equity to enjoin any acts or things which are unlawful or violate the rights of the Corporation; or

(C) by suit in equity upon the happening of an Event of Default to require the District and its Board of Directors, officers and employees to account as the trustee of an express trust.

Non-Waiver. Nothing in the Master Contract or in any other provision of the Master Contract will affect or impair the obligation of the District, which is absolute and unconditional, to pay from Net Revenues, first, the Parity Payments, and second, the Subordinate Payments at the respective due dates or upon prepayment, or will affect or impair the right of the Corporation and the Trustee, which is also absolute and unconditional, to institute suit to enforce such payment by virtue of the contract embodied in the Master Contract.

A waiver of any default or breach of duty or contract by the Corporation will not affect any subsequent default or breach of duty or contract or impair any rights or remedies on any such subsequent

default or breach of duty or contract. No delay or omission by the Corporation to exercise any right or remedy accruing upon any default or breach of duty or contract will impair any such right or remedy or will be construed to be a waiver of any such default or breach of duty or contract or an acquiescence to any such default or breach of duty or contract, and every right or remedy conferred upon the Corporation by the Law or any other applicable law or by the Master Contract may be enforced and exercised from time to time and as often as is deemed expedient by the Corporation.

If any action, proceeding or suit to enforce any right or exercise any remedy is abandoned or determined adversely to the Corporation, the District and the Corporation will be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

Remedies Not Exclusive. No remedy in the Master Contract conferred upon or reserved to the Corporation is intended to be exclusive of any other remedy, and each such remedy will be cumulative and will be in addition to every other remedy given under the Master Contract or now or after the date of the Master Contract existing in law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by the Law or any other law.

Discharge of Obligations

Discharge of Obligations.

(A) If the District pays or cause to be paid all the Payments at the times and in the manner provided in the Master Contract, the right, title and interest of the Corporation in the Master Contract and the obligations of the District under the Master Contract and under the Obligations to which such Payments relate will cease, terminate, become void and be completely discharged and satisfied.

(B) All or any portion of the Payments will, prior to their payment dates or dates of prepayment, be deemed to have been paid within the meaning of and with the effect expressed in the Master Contract if the District makes payment of such Payments and the prepayment premium, if applicable, in the manner provided in the applicable Issuing Document, or if not so provided in the applicable Issuing Document, in the manner provided in the Master Contract.

(C) All or any portion of the Payments will, prior to their payment dates or dates of prepayment, be deemed to have been paid within the meaning of and with the effect expressed in paragraph (A) of the Master Contract if (i) notice is provided by the District to the Corporation, (ii) there has been deposited with the Corporation either money in an amount which will be sufficient, or Government Obligations which are not subject to redemption except by the holder thereof prior to maturity, the interest on and principal of which when paid will provide money which, together with money, if any, deposited with the Corporation or the Trustee, will be sufficient (as evidenced by a report of an Independent Certified Public Accountant or other party satisfactory to the Trustee regarding such sufficiency) to pay when due the Payments or such portions thereof on and prior to their payment dates or their dates of prepayment, as the case may be, and the prepayment premiums, if any, applicable thereto and (iii) all fees and expenses with respect to the Obligations to which such Payments relate has been paid.

(D) After the payment of all Payments and prepayment premiums, if any, as provided in the Master Contract, and the payment in full of all fees and expenses of the Corporation, the Corporation, upon receipt of a Request of the District, will cause an accounting for such period or periods as may be requested by the District to be prepared and filed with the District and the Corporation and will execute and deliver to the District and the Corporation all such instruments as may be necessary or desirable to evidence such total discharge and satisfaction of the Master Contract, and the Corporation will pay over and deliver to the District, as an overpayment of Payments, all such money or investments held by it pursuant to the Master Contract other than such money and such investments as are required for the payment or prepayment of the Payments, which money and investments will continue to be held in trust for the payment of the Payments.

Miscellaneous

Liability of District Limited to Net Revenues. Notwithstanding anything contained in the Master Contract, the District will not be required to advance any money derived from any source of income other than the Net Revenues for the payment of first, the Parity Payments and second, the Subordinate Payments or for the performance of any agreements or covenants required to be performed by it contained in the Master Contract; provided, that the District may advance money for any such purpose so long as such moneys are derived from a source legally available for such purpose and may be legally used by the District for such purpose.

The obligation of the District to make first, the Parity Payments and second, the Subordinate Payments is a special obligation of the District payable solely from the Net Revenues as provided in the Master Contract, and such obligations do not constitute a debt of the District or of the State or of any political subdivision thereof within the meaning of any constitutional or statutory debt limitation or restriction.

INDENTURE OF TRUST

Pledge of Net Revenues; Revenue Fund

Pursuant to the Master Contract, the District has agreed to maintain a fund, designated as the “Vallecitos Water District Revenue Fund,” which fund the District agrees to hold and maintain so long as any Payments are Outstanding. The District has irrevocably granted and pledged the Net Revenues first, to secure Parity Obligations (including the Bonds) and second, to secure Subordinate Obligations, provided that, out of Net Revenues there may be apportioned such sums for such purposes as are expressly permitted by any Issuing Document including the Indenture. Such lien and pledge constitutes a first lien on Net Revenues. All Parity Obligations will be of equal rank without preference, priority or distinction of any Parity Obligations over any other Parity Obligations. Unless expressly stated to the contrary in a particular Subordinate Obligation, all Subordinate Obligations will be of equal rank without preference, priority or distinction of any Subordinate Obligations over any other Subordinate Obligations. In order to carry out and effectuate the obligation of the District contained in the Indenture and in all Obligations to pay the Payments, the District agrees and covenants that all Revenues received by it will be deposited when and as received in the Revenue Fund. Additionally, amounts may, from time to time as the District deems necessary or appropriate, be transferred from the Rate Stabilization Account and deposited in the Revenue Fund.

Payments into Other Funds; Rate Stabilization Fund

Pursuant to the Master Contract, the District will withdraw or transfer from the Revenue Fund and pay or deposit such amounts for the following purposes in the following order, the amounts set forth below:

The District will pay all Maintenance and Operation Costs (including amounts reasonably required to be set aside in contingency reserves for Maintenance and Operation Costs the payment of which is not then immediately required) from the Revenue Fund as they become due; and

On or before the fifth Business Day immediately preceding each Interest Payment Date and Principal Payment Date, the District will, from the remaining money then on deposit in the Revenue Fund, deposit in the “Vallecitos Water District Parity Obligation Payment Fund,” which fund the District agrees to hold and maintain so long as any Parity Payments will be Outstanding, the following amounts in the following order of priority:

- (1) a sum equal to (A) the interest and principal payments becoming due and payable under all Parity Obligations, plus (B) the net payments becoming due and payable on all Parity Payment Agreements (except any Termination Payments), plus (C) any other amounts due with

respect to Parity Obligations (including any letter of credit and remarketing fees), in each case, during the next succeeding month; plus

(2) all amounts due to make up any deficiency in the Reserve Funds for Parity Obligations including any Reserve Fund established with respect to a Series of Bonds in accordance with the provisions of the applicable Supplemental Indenture or other Issuing Document, including all Reserve Fund Credit Facility Costs.

Moneys on deposit in the Parity Obligation Payment Fund representing Debt Service on the Bonds will be transferred by the District to the Trustee for deposit to the Debt Service Fund to make and satisfy the Parity Payments due on the next applicable Payment Dates with respect to the Bonds as provided in the Indenture. In the event that any Bond has been paid from amounts made available pursuant to a Credit Support Instrument, moneys on deposit in the Parity Obligation Payment Fund, and any such amounts transferred by the District from the Parity Obligation Payment Fund to the Trustee for such the Bonds, will be paid to the applicable Credit Provider as a Credit Support Reimbursement Obligation for the amounts so paid.

After the payments contemplated above have been made, any amounts remaining in the Revenue Fund will be used for the payment of the interest and principal payments becoming due and payable under all Subordinate Obligations and the net payments becoming due and payable on all Subordinate Payment Agreements (except any Termination Payments) and any other amounts becoming due and payable with respect to Subordinate Obligations (including any letter of credit and remarketing fees and any other amounts becoming due and payable to make up any deficiency in the Reserve Funds for Subordinate Obligations, including all Reserve Fund Credit Facility Costs, or any Credit Support Reimbursement Obligations with respect to Subordinate Obligations) and any Termination Payments on Parity Payment Agreements; so long as the following conditions are met:

(1) all Maintenance and Operations Costs are being and have been paid and are then current; and

(2) all deposits and payments described by the two preceding full paragraphs above will have been made in full and no deficiency in any Reserve Fund for Parity Obligations will exist and no Reserve Fund Credit Facility Costs or Credit Support Reimbursement Obligations with respect to Parity Obligations will be due and payable, and there will have been paid, or segregated within the Revenue Fund, the amounts currently payable pursuant to subparagraphs (a) and (b) above.

After deposits contemplated by subparagraphs (a), (b) and (c) have been made, any amounts thereafter remaining in the Revenue Fund may be used for any lawful purpose, including, but not limited to (i) the payment of any Termination Payments on Subordinate Payment Agreements or (ii) transfer to the Rate Stabilization Account.

Debt Service Fund.

(a) The Trustee will establish and maintain and hold in trust so long as any Bonds remain Outstanding, a special fund designated as the "Debt Service Fund." The Trustee will pay out of the Debt Service Fund: (i) on or before each interest payment date for any Outstanding Bonds, the amount required for the interest payable on such date; (ii) on or before each principal payment date or redemption date, the amount required for the Bond Obligation payable on such due date (including any mandatory sinking fund payment to be paid on such date); and (iii) on or before any redemption date for Outstanding Bonds, the amount required for the payment of interest on such Bonds then to be redeemed. Such amounts will be applied for such purposes by the Trustee on the due date thereof. The Trustee will also pay out of the Debt Service Fund the accrued interest included in the purchase price of any Bonds, the Debt Service of which may be paid from the moneys in such fund, purchased for retirement.

(b) On or prior to the forty-fifth (45th) day preceding the due date of each mandatory sinking fund payment, any amounts then on deposit in the Debt Service Fund with respect to any mandatory sinking fund payment (exclusive of amounts, if any, set aside in said fund which were deposited from the proceeds of Bonds, but inclusive of amounts accumulated with respect to interest on the Bonds for which such mandatory sinking fund payment is to be paid) may, and if so directed by the District will, be applied by the Trustee to the purchase of Bonds of the Series and maturity for which such mandatory sinking fund payment was established in an amount not exceeding that necessary to complete the retirement of the unsatisfied balance of such mandatory sinking fund payment. All purchases of any Bonds pursuant to this subsection (b) will be made at prices not exceeding the applicable sinking fund Redemption Price of such Bonds plus accrued interest, and such purchases will be made by the Trustee as directed by the District. If directed by the District, on or prior to the forty-fifth (45th) day next preceding a mandatory sinking fund payment due date, there will be applied as a credit against such mandatory sinking fund payment, and there will be deemed to constitute part of the Debt Service Fund until such mandatory sinking fund payment due date, for the purpose of calculating the amount on deposit in such fund, the applicable sinking fund Redemption Price (or principal amount of maturing Bonds) of any Bonds of the Series and maturity for which such mandatory sinking fund payment was established, that were cancelled or delivered to the Trustee for cancellation on or prior to the forty-fifth (45th) day next preceding such mandatory sinking fund payment due date and that was not previously applied as a credit against a mandatory sinking fund payment, including any Bonds purchased pursuant to this subsection (b) and as to which the District has properly claimed a credit against the next mandatory sinking fund payment. As soon as practicable after the forty-fifth (45th) day preceding the due date of any such mandatory sinking fund payment, the Trustee will proceed to call for redemption on such date, Bonds of the Series and maturity for which such mandatory sinking fund payment was established (except in the case of Bonds maturing on a mandatory sinking fund payment due date). The Trustee will pay out of the Debt Service Fund, on or before such redemption date (or maturity date), the amount required for the redemption of the Bonds so called for redemption (or for the payment of such Bonds then maturing), and such amounts will be applied to such redemption (or payment).

(c) The amount, if any, deposited in the Debt Service Fund, including any subaccount, from the proceeds of each Series of Bonds will be set aside in such fund and applied to the payment of interest on Bonds as provided in the Supplemental Indenture relating to the issuance of such Series of Bonds and will be deemed available to pay Debt Service only to the extent so provided.

(d) In the event of the refunding of one or more Bonds, the Trustee may, upon the direction of the District with the advice of Bond Counsel, withdraw from the Debt Service Fund amounts accumulated with respect to Debt Service on the Bonds being refunded and deposit such amounts as directed by the District, to be held for the payment of the principal or Redemption Price, if applicable, or interest on the Bonds being refunded; provided that such withdrawal will not be made unless (A) immediately thereafter the Bonds being refunded will be deemed to have been paid pursuant to Article X hereof, and (B) the amount remaining in the Debt Service Fund after such withdrawal will not be less than the requirement for such fund.

(e) Notwithstanding anything in the Indenture to the contrary, if any payment of principal, interest on or Redemption Price of any Bonds will be made with funds drawn under a Credit Facility, amounts on deposit in the Debt Service Fund will be applied to reimburse the Credit Provider for such payment on the date so drawn or as soon thereafter as amounts are available.

(f) Any provisions of the Indenture to the contrary notwithstanding, so long as there will be held in the Debt Service Fund an amount sufficient to pay in full all Outstanding Bonds in accordance with their terms (including principal or Redemption Price, if applicable, and interest thereon), no deposits will be required to be made into the Debt Service Fund.

Reserve Fund.

(a) In each Supplemental Indenture, the District may direct that a Reserve Fund be established. With respect to each Reserve Fund established with respect to a Series of Bonds, the District may elect to treat such Reserve Fund as a part of the Common Reserve securing all Series of Bonds designated by the District to participate in the Common Reserve. Each time that the District elects to secure a Series of Bonds with the Common Reserve, it will deposit funds in the Common Reserve in an amount sufficient to increase the balance in the Common Reserve to the Common Reserve Requirement calculated to take into account such additional Series of Bonds. If the District establishes a Reserve Fund for any Series of Bonds but does not elect to make such Reserve Fund a part of the Common Reserve, then any Reserve Fund so established will be a Separate Reserve Fund and will secure only the Series of Bonds for which such Reserve Fund was created.

The Trustee may withdraw amounts from the Common Reserve to make payments to the owners of the Bonds when due.

Investment of Moneys in Funds and Accounts. Unless otherwise limited in a Supplemental Indenture, all moneys in any of the funds and accounts held by the Trustee and established pursuant to the Indenture will be invested, as directed by the District, solely in Permitted Investments; provided, however, that Permitted Investments purchased with moneys held by the Trustee in the Reserve Fund will have an average weighted term to maturity not greater than five years. All Permitted Investments will, as directed by the District in writing, be acquired subject to the limitations as to maturities described below and such additional limitations or requirements consistent with the foregoing as may be established by Request of the District. The Trustee may conclusively rely upon any investment direction from the District as a certification to the Trustee that such investment constitutes an Investment Security. If and to the extent the Trustee does not receive investment instructions from the District with respect to the moneys in the funds and accounts held by the Trustee pursuant to the Indenture, such moneys will be invested in Permitted Investments described in clause (vii) of the definition thereof, provided, however, that any such investment will be made by the Trustee only if, prior to the date on which such investment is to be made, the Trustee will have received a written direction from the District specifying a specific money market fund and, if no such written direction from the District is so received, the Trustee will hold such moneys uninvested.

Unless otherwise provided in the Indenture or in a Supplemental Indenture, all interest, profits and other income received from the investment of moneys in any fund or account, other than the Rebate Fund, will be transferred to the Revenue Fund. All interest, profits and other income received from the investment of moneys in the Rebate Fund will be deposited in the Rebate Fund, except as provided in the Indenture. Notwithstanding anything to the contrary contained in the Indenture, an amount of interest received with respect to any Investment Security equal to the amount of accrued interest, if any, paid as part of the purchase price of such Investment Security will be credited to the fund or account from which such accrued interest was paid.

The Trustee may commingle any of the funds or accounts established pursuant to the Indenture into a separate fund or funds for investment purposes only, provided that all funds or accounts held by the Trustee under the Indenture will be accounted for separately as required by the Indenture and further provided that any funds or accounts established pursuant to a Supplemental Indenture for the proceeds of a draw on a Credit Facility or the proceeds of the remarketing of any Bonds subject to tender will not be commingled. The Trustee may act as principal or agent in the making or disposing of any investment and, with the prior written consent of the District, may impose its customary charge therefor. The Trustee may sell or present for redemption, any Permitted Investments so purchased whenever it will be necessary to provide moneys to meet any required payment, transfer, withdrawal or disbursement from the fund or account to which such Investment Security is credited, and the Trustee will not be liable or responsible for any loss resulting from such investment.

The Trustee and the District will each keep proper books of record and accounts containing complete and correct entries of all transactions made by it relating to the receipt, investment, disbursement, allocation and application of the moneys related to the Bonds, including moneys derived from, pledged to, or to be used to make payments on the Bonds. Such records will specify the account or fund to which each investment (or portion thereof) is to be allocated and will set forth, in the case of each investment security, (a) its purchase price, (b) identifying information, including par amount, coupon rate, and payment dates, (c) the amount received at maturity or its sale price, as the case may be, including accrued interest, (d) the amounts and dates of any payments made with respect thereto, and (e) the dates of acquisition and disposition or maturity.

The Trustee will furnish the District periodic cash transaction statements which include detail for all investment transactions made by the Trustee under the Indenture. Upon the District's election, such statements will be delivered via the Trustee's online service and upon electing such service, paper statements will be provided only upon request.

The Trustee may make any investments under the Indenture through its own bond or investment department or trust investment department, or those of its parent or any affiliate.

The Trustee or any of its affiliates may act as sponsor, advisor or manager in connection with any investments made by the Trustee under the Indenture.

The Trustee will also provide to the District in accordance with a Request of the District, with respect to each Investment Security such documentation as is reasonably available to the Trustee and specified by the District to the Trustee in writing and is required by the Code or other applicable law to be obtained by the District as evidence to establish that each investment had been acquired and disposed of on an established market in an arm's-length transaction at a price equal to its fair market value and with no amounts having been paid to reduce the yield on the investments, or will be United States Treasury Obligations-State and Local Government Series as set forth in the Tax Certificate.

Covenants

Punctual Payment; Preservation of Security and Rights of the Owners. The District will punctually pay or cause to be paid the Parity Payments, in strict conformity with the terms of the Master Contract, the Bonds and of the Indenture, according to the true intent and meaning thereof, and will punctually pay or cause to be paid all mandatory sinking fund payments, but in each case only out of Net Revenues, as provided in the Master Contract and the Indenture. The District will preserve and protect the security hereof and the rights of the District to the Payments under the Indenture and will warrant and defend such rights against all claims and demands of all persons.*Extension of Payment of Bonds.* The District will not directly or indirectly extend or assent to the extension of the maturity of any of the Bonds or the time of payment of any Bonds or claims for interest of such Bonds or claims for interest and in case the maturity of any of the Bonds or the time of payment of any such claims for interest will be extended, such Bonds or claims for interest will not be entitled, in case of any default under the Indenture, to the benefits of the Indenture, except subject to the prior payment in full of the principal of all of the Bonds then Outstanding and of all claims for interest thereon which will not have been so extended. Nothing in this section will be deemed to limit the right of the District to issue Refunding Bonds, and such issuance will not be deemed to constitute an extension of maturity of Bonds.

Waiver of Laws. The District will not at any time insist upon or plead in any manner whatsoever, or claim or take the benefit or advantage of, any stay or extension law now or at any time hereafter in force that may affect the covenants and agreements contained in the Master Contract and the Indenture or in the Bonds, and all benefit or advantage of any such law or laws is expressly waived by the District to the extent permitted by law.

Further Assurances. The District will adopt, make, execute and deliver any and all such further assurances, instruments and resolutions as may be reasonably necessary or proper to carry out the intention or

to facilitate the performance of the Indenture and for the better assuring and confirming unto the Owners of the Bonds and any Credit Provider of the rights and benefits provided in the Indenture.

Against Encumbrances. The District will not mortgage or otherwise encumber, pledge or place any charge upon the Enterprise or any part thereof, or upon any of the Revenues that would impair the District's ability to comply with its obligations under the Contracts or any other Issuing Document including the Indenture.

So long as any Obligations of the District are outstanding, the District will not issue or incur Obligations payable from Revenues or secured by a pledge, lien or charge upon Revenues, except as provided in the Master Contract and in the Indenture.

Accounting Records; Financial Statements and Other Reports. The District will comply with the terms of the Master Contract.

Tax Covenants. The District covenants that it will not take any action, or fail to take any action, if any such action or failure to take action would adversely affect the exclusion from gross income of the interest on the Bonds under Section 103 of the Code; provided that, prior to the issuance of any Series of Bonds, the District may exclude the application of the covenants contained in the Indenture to such Series of Bonds. The District will not directly or indirectly use or permit the use of any proceeds of the Bonds or any other funds of the District, or take or omit to take any action that would cause the Bonds to be arbitrage bonds within the meaning of Section 148(a) of the Code. To that end, the District will comply with all requirements of Section 148 of the Code to the extent applicable to the Bonds. In the event that at any time the District is of the opinion that for purposes of the Indenture it is necessary to restrict or limit the yield on the investment of any moneys held by the Trustee under the Indenture, the District will so instruct the Trustee in writing, and the Trustee will take such action as may be necessary in accordance with such instructions.

Without limiting the generality of the foregoing, the District agrees that there will be paid from time to time all amounts required to be rebated to the federal government of the United States of America pursuant to Section 148(f) of the Code and any temporary, proposed or final Treasury Regulations as may be applicable to the Bonds from time to time. The District specifically covenants to pay or cause to be paid to the federal government of the United States of America the Rebate Requirement at the times and in the amounts determined under and as described in the Tax Certificate.

Notwithstanding any provision of the Indenture, if the District receives an Opinion of Bond Counsel to the effect that any action required under the Indenture is no longer required, or to the effect that some further action is required, to maintain the exclusion from gross income of the interest on the Bonds pursuant to Section 103 of the Code, the District and the Trustee may rely conclusively on such opinion in complying with the provisions hereof, and the covenants under the Indenture will be deemed to be modified to that extent.

Maintenance and Operation of the Enterprise; Budgets. Pursuant to the Master Contract, the District will maintain and preserve the Enterprise in good repair and working order at all times and in accordance with sound engineering practices, will operate the Enterprise in an efficient and economical manner, and will pay all Maintenance and Operation Costs as they become due and payable. The District will adopt and file with the Trustee, not later than 90 days after the start of each Fiscal Year, a budget approved by the Board of Directors setting forth the estimated Revenues and Maintenance and Operation Costs for the then current Fiscal Year; provided, that any such budget may be amended at any time during any Fiscal Year and such amended budget will be filed by the District with the Trustee.

Against Sale or Other Disposition of Property. Pursuant to the Master Contract, the District will not sell, lease or otherwise dispose of the Enterprise or any part thereof essential to the proper operation of the Enterprise or to the maintenance of Revenues; provided, however, that any real or personal property which has become non-operative or which is not needed for the efficient and proper operation of the Enterprise, or any

material or equipment which has become worn out, may be sold if such sale will not materially reduce Net Revenues and if the proceeds of such sale are deposited in the Revenue Fund. The District will not enter into any agreement or lease which impairs the operation of the Enterprise or any part thereof necessary to secure adequate Net Revenues for the payment of Obligations or which would otherwise impair the rights of the Owners with respect to Net Revenues or the operation of the Enterprise.

Continuing Disclosure Agreement. The District will comply with and carry out all of its obligations under any Continuing Disclosure Agreement executed in connection with a Series of Bonds. Upon the failure of the District to comply with the Continuing Disclosure Agreement relating to any Series of Bonds, any Owner or Beneficial Owner may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the District, to comply with its obligations under this section.

Compliance with Contracts for Use of the Enterprise. The District will comply with, keep, observe and perform all agreements, conditions, covenants and terms, express or implied, required to be performed by it contained in all contracts for the use of the Enterprise and all other contracts affecting or involving the Enterprise to the extent that the District is a party thereto.

Investment of Amounts in Funds. The District covenants to invest amounts in the Revenue Fund, the Parity Obligation Payment Fund and the Improvement Fund created pursuant to the Master Contract only in Permitted Investments.

Contract Resource Obligations. Pursuant to the Master Contract, the District may at any time enter into one or more Contract Resource Obligations related to existing facilities or facilities to be constructed. The District may determine that, and may agree under a Contract Resource Obligation to provide that all payments under that Contract Resource Obligation will be Maintenance and Operation Costs if the requirements of the Master Contract are met.

Compliance with Contracts and the Indenture. The District will punctually pay the Payments in strict conformity with the terms hereof, and will faithfully observe and perform all the agreements, conditions, covenants and terms contained in the Indenture required to be observed and performed by it, and will not terminate the Indenture or the Contracts for any cause including, without limiting the generality of the foregoing: any acts or circumstances that may constitute failure of consideration, destruction of or damage to the Projects or the Enterprise; commercial frustration of purpose; any change in the tax or other laws of the United States of America or of the State or any political subdivision of either of them; any failure of the Trustee to observe or perform any agreement, condition, covenant or term contained in the Indenture required to be observed and performed by it, whether express or implied, or any duty, liability or obligation arising out of or connected herewith; the insolvency, or deemed insolvency, or bankruptcy or liquidation of the Corporation or the Trustee; any force majeure, including acts of God, tempest, storm, earthquake, war, rebellion, riot, civil disorder, acts of public enemies, blockade or embargo, strikes, industrial disputes, lockouts, lack of transportation facilities, fire, explosion; or any acts or regulations of governmental authorities.

Payment of Taxes and Compliance with Governmental Regulations. The District will pay and discharge all taxes, assessments and other governmental charges which may hereafter be lawfully imposed upon the Enterprise or any part thereof when the same will become due. The District will duly observe and conform with all valid regulations and requirements of any governmental authority relative to the operation of the Enterprise or any part thereof, but the District will not be required to comply with any regulations or requirements so long as the validity or application thereof will be contested in good faith.

Default and Limitations of Liability

Events of Default. If any Event of Default (as that term is defined in the Master Contract) will happen, then such Event of Default will constitute a default under the Indenture, then in each and every such case during the continuance of such Event of Default the Trustee may, and will at the direction of the Owners of not less than a majority in aggregate principal amount of Outstanding Bonds, upon notice in writing to the District, declare an Event of Default under the Indenture; provided, that if at any time after an Event of Default has been declared and before any judgment or decree for the payment of the money due will have been obtained or entered the District will deposit with the Trustee a sum sufficient to pay the unpaid principal amount of the Payments due and payable prior to such declaration and the accrued interest thereon, with interest on such overdue Payments at the rate or rates applicable to such unpaid principal amounts of the Payments if paid in accordance with their terms, and the reasonable expenses of the Trustee, and any and all other defaults known to the Trustee will have been made good or cured to the satisfaction of the Trustee or provision deemed by the Trustee to be adequate will have been made therefore, then and in every such case the Trustee, by written notice to the District, may rescind and annul such declaration of an Event of Default and its consequences; but no such rescission and annulment will extend to or will affect any subsequent default or will impair or exhaust any right or power consequent thereon; provided, that nothing contained in the Indenture will affect or impair the right of action of any Owner to institute suit directly against the District to enforce payment of the obligation evidenced and represented by such Owner's Certificate.

The payment of principal and interest on the Payments will not be accelerated upon the declaration of an Event of Default under the Indenture.

Other Remedies of the Trustee. The Trustee will have the right:

(a) if an Event of Default will have been declared and if requested so to do by the Owners of not less than a majority in aggregate principal amount of Outstanding Bonds and indemnified as provided in the Indenture, the Trustee will be obligated to exercise such one or more of the rights and powers conferred in the Indenture, as the Trustee, being advised by counsel, will deem most expedient in the interests of the Owners;

(b) by mandamus or other action or proceeding or suit at law or in equity, institute action to enforce its rights against the District or any member of the Board of Directors or officer or employee of the District, and to compel the District or any member of the Board of Directors or officer or employee of the District to observe or perform its or his or her duties under applicable law and the agreements, conditions, covenants and terms contained in the Indenture required to be observed or performed by it or him or her;

(c) by suit in equity, institute action to enjoin any acts or things which are unlawful or violate the rights of the Trustee; or

(d) by suit in equity, upon the happening of an Event of Default under the Indenture, to require the District or any member of the Board of Directors or officer or employee of the District to account as the trustee of an express trust.

Non-Waiver. A waiver by the Trustee of any default or breach of any obligation by the District under the Indenture will not affect any subsequent default or any subsequent breach of an obligation by the District under the Indenture or impair any rights or remedies on any such subsequent default under the Indenture or on any such subsequent breach of an obligation by the District under the Indenture. No delay or omission by the Trustee to exercise any right or remedy accruing upon any default will impair any such right or remedy or will be construed to be a waiver of any such default or an acquiescence, and every right or remedy conferred upon the Trustee by applicable law or by this article may be enforced and exercised from time to time and as often as will be deemed expedient by the Trustee.

If any action, proceeding or suit to enforce any right or to exercise any remedy is abandoned or determined adversely to the District or the Trustee, the District and the Trustee will be restored to their former positions, rights and remedies as if such action, proceeding or suit had not been brought or taken.

Remedies Not Exclusive. No remedy conferred upon or reserved in the Indenture to the Trustee is intended to be exclusive and all remedies will be cumulative, and each remedy will be in addition to every other remedy given under the Indenture or now or hereafter existing under applicable law or equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by any other applicable law.

No Liability by the District to the Owners. Except for the payment when due of the Debt Service on the Bonds and the observance and performance of the other agreements, conditions, covenants and terms contained in the Master Contract or in the Indenture required to be observed or performed by it, the District will not have any obligation or liability to the Owners with respect to the Indenture of Trust or the execution, delivery, transfer, exchange or cancellation of the Bonds or the receipt, deposit or disbursement of the Payments by the Trustee, or with respect to the performance by the Trustee of any obligation contained in the Indenture required to be performed by the Trustee.

If the Trustee, upon the happening of an Event of Default, will have taken any action, by judicial proceedings or otherwise, pursuant to its duties in the Indenture, whether upon its own discretion or upon the request of the Owners of at least a majority in aggregate principal amount of the Bonds then Outstanding, it will have full power, in the exercise of its discretion for the best interests of the Owners of the Bonds, with respect to the continuance, discontinuance, withdrawal, compromise, settlement or other disposal of such action; provided, however, that the Trustee will not, unless there no longer continues an Event of Default, discontinue, withdraw, compromise or settle, or otherwise dispose of any litigation pending at law or in equity, if at the time there has been filed with it a written request signed by the Owners of a majority in aggregate principal amount of the Outstanding Bonds under the Indenture opposing such discontinuance, withdrawal, compromise, settlement or other disposal of such litigation and if the Trustee is indemnified as provided in the Indenture. Any suit, action or proceeding which any Owner of Bonds will have the right to bring to enforce any right or remedy in the Indenture may be brought by the Trustee for the equal benefit and protection of all Owners of Bonds similarly situated and the Trustee is appointed (and the successive respective Owners of the Bonds issued under the Indenture by taking and holding the same, will be conclusively deemed so to have appointed it) the true and lawful attorney-in-fact of the respective Owners of the Bonds for the purpose of bringing any such suit, action or proceeding and to do and perform any and all acts and things for and on behalf of the respective Owners of the Bonds as a class or classes, as may be necessary or advisable in the opinion of the Trustee as such attorney-in-fact.

No Owner of any Bond issued under the Indenture will have the right to institute any suit, action or proceeding at law or in equity, for any remedy under or upon the Indenture, unless (a) such Owner will have previously given to the Trustee written notice of the occurrence of an Event of Default; (b) the Owners of a majority in aggregate principal amount of all the Bonds then Outstanding will have made written request upon the Trustee to exercise the powers under the Indenture granted or to institute such action, suit or proceeding in its own name; (c) said Owners will have tendered to the Trustee indemnity reasonably acceptable to the Trustee against the costs, expenses and liabilities to be incurred in compliance with such request; and (d) the Trustee will have refused or omitted to comply with such request for a period of 60 days after such written request will have been received by, and said tender of indemnity will have been made to, the Trustee.

Such notification, request, tender of indemnity and refusal or omission are declared, in every case, to be conditions precedent to the exercise by any Owner of Bonds of any remedy under the Indenture; it being understood and intended that no one or more Owners of Bonds will have any right in any manner whatever by his or their action to enforce any right under the Indenture, except in the manner provided in the Indenture, and that all proceedings at law or in equity to enforce any provision of the Indenture will be instituted, had and

maintained in the manner provided under the Indenture and for the equal benefit of all Owners of the Outstanding Bonds.

The Trustee

Appointment; Duties and Immunities of Trustee.

(a) MUFG Union Bank, N.A. is appointed as Trustee under the Indenture and accepts the trust imposed upon it as Trustee and to perform all the functions and duties of the Trustee under the Indenture, subject to the terms and conditions set forth in the Indenture. The Trustee will, prior to an Event of Default, and after the curing or waiver of all Events of Default which may have occurred, perform such duties and only such duties as are specifically set forth in the Indenture and no implied covenants will be read into the Indenture against the Trustee. The Trustee will, during the existence of any Event of Default (which has not been cured or waived), exercise such of the rights and powers vested in it by the Indenture and use the same degree of care and skill in their exercise as a prudent person would exercise or use under the circumstances in the conduct of his or her own affairs.

(b) The District may remove the Trustee at any time unless an Event of Default will have occurred and then be continuing, and will remove the Trustee if at any time requested to do so by an instrument or concurrent instruments in writing signed by the Owners of not less than a majority in aggregate amount of Bond Obligation of the Bonds then Outstanding (or their attorneys duly authorized in writing) or if at any time the Trustee will cease to be eligible in accordance with subsection (e) of this section, or will become incapable of acting, or will be adjudged a bankrupt or insolvent, or a receiver of the Trustee or its property will be appointed, or any public officer will take control or charge of the Trustee or of its property or affairs for the purpose of rehabilitation, conservation or liquidation, in each case by giving written notice of such removal to the Trustee, and thereupon will appoint a successor Trustee by an instrument in writing.

(c) The Trustee may at any time resign by giving written notice of such resignation to the District and any Credit Provider and by giving the Bondholders notice of such resignation by mail at the addresses shown on the registration books maintained by the Trustee. Upon receiving such notice of resignation, the District will promptly appoint a successor Trustee by an instrument in writing.

(d) Any removal or resignation of the Trustee and appointment of a successor Trustee will become effective upon acceptance of appointment by the successor Trustee. If no successor Trustee will have been appointed and have accepted appointment within forty-five (45) days of giving notice of removal or notice of resignation as aforesaid, the resigning Trustee or any Bondholder (on behalf of himself and all other Bondholders) may petition any court of competent jurisdiction for the appointment of a successor Trustee, and such court may thereupon, after such notice (if any) as it may deem proper, appoint such successor Trustee. Any successor Trustee appointed under the Indenture, will signify its acceptance of such appointment by executing and delivering to the District and to its predecessor Trustee a written acceptance thereof, and thereupon such successor Trustee, without any further act, deed or conveyance, will become vested with all the moneys, estates, properties, rights, powers, trusts, duties and obligations of such predecessor Trustee, with like effect as if originally named Trustee in the Indenture; but, nevertheless at the Request of the District or the request of the successor Trustee, such predecessor Trustee will execute and deliver any and all instruments of conveyance or further assurance and do such other things as may reasonably be required for more fully and certainly vesting in and confirming to such successor Trustee all the right, title and interest of such predecessor Trustee in and to any property held by it under the Indenture and will pay over, transfer, assign and deliver to the successor Trustee any money or other property subject to the trusts and conditions set forth in the Indenture. Upon request of the successor Trustee, the District will execute and deliver any and all instruments as may be reasonably required for more fully and certainly vesting in and confirming to such successor Trustee all such moneys, estates, properties, rights, powers, trusts, duties and obligations. Upon acceptance of appointment by a successor Trustee as provided in this subsection, the District will give notice of the succession of such Trustee to the trusts under the Indenture by mail to the Bondholders at the addresses shown

on the registration books maintained by the Trustee. If the District fails to mail such notice within fifteen (15) days after acceptance of appointment by the successor Trustee, the successor Trustee will cause such notice to be mailed at the expense of the District.

(e) Any Trustee appointed under the provisions of the Indenture in succession to the Trustee will be reasonably acceptable to each Credit Provider and will be a trust company, corporation or bank having the powers of a trust company having a corporate trust office in the State, having a combined capital and surplus of at least fifty million dollars (\$50,000,000) and subject to supervision or examination by federal or state authority. If such bank, corporation or trust company publishes a report of condition at least annually, pursuant to law or to the requirements of any supervising or examining authority above referred to, then for the purpose of this subsection the combined capital and surplus of such bank or trust company will be deemed to be its combined capital and surplus as set forth in its most recent report of condition so published. In case at any time the Trustee will cease to be eligible in accordance with the provisions of this subsection (e), the Trustee will resign immediately in the manner and with the effect specified in this section.

(f) If, by reason of the judgment of any court, the Trustee or any successor Trustee is rendered unable to perform its duties under the Indenture, and if no successor Trustee be then appointed, all such duties and all of the rights and powers of the Trustee under the Indenture will be assumed by and vest in the District in trust for the benefit of the Bondowners.

Liability of Trustee.

(a) The recitals of facts in the Indenture and in the Bonds contained will be taken as statements of the District, and the Trustee assumes no responsibility for the correctness of the same (other than the certificate of authentication of the Trustee on each Bond), and makes no representations as to the validity or sufficiency of the Indenture or of the Bonds or of any Investment Security, as to the sufficiency of the Net Revenues, or the priority of the lien of the Indenture thereon, or as to the financial or technical feasibility of the Water System and will not incur any responsibility in respect of any such matter, other than in connection with the duties or obligations expressly in the Indenture or in the Bonds assigned to or imposed upon it. The Trustee will, however, be responsible for its representations contained in its certificate of authentication on the Bonds. The Trustee will not be liable in connection with the performance of its duties under the Indenture, except for its own negligence or willful misconduct. The Trustee and its directors, officers, employees or agents may in good faith buy, sell, own, hold and deal in any of the Bonds and may join in any action which any Owner of a Bond may be entitled to take, with like effect as if the Trustee was not the Trustee under the Indenture. The Trustee may in good faith hold any other form of indebtedness of the District, own, accept or negotiate any drafts, bills of exchange, acceptances or obligations of the District and make disbursements for the District and enter into any commercial or business arrangement therewith, without limitation.

(b) The Trustee will not be liable for any error of judgment made in good faith by a responsible officer unless it will be proved that the Trustee was negligent in ascertaining the pertinent facts. The Trustee may execute any of the trusts or powers hereof and perform the duties required of it under the Indenture by or through attorneys, agents, or receivers, and will be entitled to advice of counsel concerning all matters of trust and its duty under the Indenture. The Trustee will not be responsible for the negligence or misconduct of such persons selected by it with reasonable care.

(c) The Trustee will not be liable with respect to any action taken or omitted to be taken by it in good faith in accordance with the direction of the Owners of not less than twenty-five percent (25%) in aggregate amount of Bond Obligation of the Bonds at the time Outstanding relating to the time, method and place of conducting any proceeding for any remedy available to the Trustee or exercising any trust or power conferred upon the Trustee under the Indenture.

(d) The Trustee will be under no obligation to exercise any of the rights or powers vested in it by the Indenture at the request, order or direction of any of the Bondholders or insurer pursuant to the provisions

of the Indenture, unless such Bondholders or insurer will have offered to the Trustee security or indemnity satisfactory to it against the costs, expenses and liabilities which may be incurred.

(e) No provision of the Indenture will require the Trustee to expend or risk its own funds or otherwise incur any financial liability in the performance or exercise of any of its duties under the Indenture.

(f) The Trustee will not be deemed to have knowledge of and will not be required to take any action with respect to, any Event of Default (other than an Event of Default described in the Master Contract) or event which would, with the giving of notice, the passage of time or both, constitute an Event of Default, unless the Trustee will have actual knowledge of such event or will have been notified of such event by the District or the Owners of twenty-five percent (25%) in aggregate amount of Bond Obligation of the Bonds at the time Outstanding. Without limiting the generality of the foregoing, the Trustee will not be required to ascertain, monitor or inquire as to the performance or observance by the District of the terms, conditions, covenants or agreements set forth in Article VI hereof (including, without limitation, the covenants of the District set forth in the Indenture), other than the covenants of the District to make payments with respect to the Bonds when due as set forth in the Indenture and to file with the Trustee when due, such reports and certifications as the District is required to file with the Trustee.

(g) No permissive power, right or remedy conferred upon the Trustee under the Indenture will be construed to impose a duty to exercise such power, right or remedy.

(h) The Trustee will not be bound to make any investigation into the facts or matters stated in any resolution, certificate, statement, instrument, opinion, report, notice, request, direction, consent, order, bond, debenture, coupon or other paper or document but the Trustee, in its discretion, may make such further inquiry or investigation into such facts or matters as it may see fit, and, if the Trustee will determine to make such further inquiry or investigation, it will be entitled to examine the books, records and premises of the District, personally or by agent or attorney.

(i) The Trustee will not be responsible for:

(1) the application or handling by the District of any Gross Aggregate Revenues or other moneys transferred to or pursuant to any Requisition or Request of the District in accordance with the terms and conditions hereof;

(2) the application and handling by the District of any other fund or account designated to be held by the District under the Indenture;

(3) any error or omission by the District in making any computation or giving any instruction pursuant to the Indenture and may rely conclusively on any computations or instructions furnished to it by the District in connection with the requirements of the Indenture and the Tax Certificate and will have no liability or responsibility to enforce compliance by the District with the terms of the Indenture or of the Tax Certificate; or

(4) the construction, operation or maintenance of the Enterprise.

(j) Whether or not expressly provided, every provision of the Indenture relating to the conduct or affecting the liability of or affording protection to the Trustee will be subject to the provisions of the Indenture titled "Trustee."

(k) The Trustee will have no responsibility with respect to any information, statement or recital in any official statement, offering memorandum or any other disclosure material prepared or distributed with respect to the Bonds.

(l) The Trustee agrees to accept and act upon notices, requests, instructions or directions pursuant to the Indenture sent by unsecured e-mail, facsimile transmission or other similar unsecured electronic methods; and provided further that the Trustee will have received an incumbency certificate listing persons designated to give such instructions or directions and containing specimen signatures of such designated persons, which such incumbency certificate will be amended and replaced whenever a person is to be added or deleted from the listing. The Trustee will not be liable for any losses, costs or expenses arising directly or indirectly from the Trustee's reliance upon and compliance with such instructions notwithstanding that such instructions conflict or are inconsistent with a subsequent written instruction. The District agrees to assume all risks arising out of the use of such electronic methods to submit instructions and directions to the Trustee, including without limitation the risk of the Trustee acting on unauthorized instructions, and the risk of interception and misuse by third parties.

(m) The Trustee's rights to immunities and protection from liability under the Indenture and its rights to payment of its fees and expenses will survive its resignation or removal and final payment or defeasance of the Bonds. All indemnifications and releases from liability granted in the Indenture to the Trustee will extend to the directors, officers, employees and agents of the Trustee.

Modification of Indenture of Trust and Supplemental Indentures of Trust

(a) The Indenture and the rights and obligations of the District, the Owners of the Bonds and the Trustee may be modified or amended from time to time and at any time by a Supplemental Indenture, which the District and the Trustee may enter into if there will be filed with the Trustee the written consent of the Owners of a majority in aggregate amount of Bond Obligation of the Bonds (or, if such Supplemental Indenture is only applicable to a Series of Bonds, such Series of Bonds) then Outstanding; provided that if such modification or amendment will, by its terms, not take effect so long as any Bonds of any particular maturity remain Outstanding or until any Bonds of a Series have been tendered by the Owners thereof, the consent of the Owners of such Bonds will not be required and such Bonds will not be deemed to be Outstanding for the purpose of any calculation of Bonds Outstanding under this section. Notwithstanding the foregoing, no such modification or amendment will (a) extend the fixed maturity of any Bond, or reduce the amount of principal thereof, or extend the time of payment or reduce the amount of any mandatory sinking fund payment provided for the payment of any Bond, or reduce the rate of interest thereon, or extend the time of payment of interest thereon, or reduce any premium payable upon the redemption thereof exclusively, without the consent of the Owner of each Bond so affected, or (b) reduce the aforesaid percentage of Bond Obligation, the consent of the Owners of which is required to effect any such modification or amendment, or permit the creation of any lien on the Net Revenues and other assets pledged under the Indenture prior to or on a parity with the lien created by the Indenture, or deprive the Owners of the Bonds of the lien created by the Indenture on such Net Revenues and other assets (in each case, except as expressly provided in the Indenture), without the consent of the Owners of all of the Bonds then Outstanding unless permitted pursuant to the terms of any Obligations. It will not be necessary for the consent of the Bondholders to approve the particular form of any Supplemental Indenture, but it will be sufficient if such consent will approve the substance thereof. Promptly after the execution and delivery by the Trustee and the District of any Supplemental Indenture, the Trustee will mail a notice, setting forth in general terms the substance of such Supplemental Indenture to the Owners of the Bonds at the addresses shown on the registration books of the Trustee. Any failure to give such notice, or any defect in the notice, will not, however, in any way impair or affect the validity of any such Supplemental Indenture.

(b) The Indenture and the rights and obligations of the District, of the Trustee and of the Owners of the Bonds may also be modified or amended from time to time and at any time by a Supplemental Indenture, which the District may adopt without the consent of any Bondholders but only to the extent permitted by law and only for any one or more of the following purposes:

(1) to add to the covenants and agreements of the District in the Indenture contained other covenants and agreements thereafter to be observed, to pledge or assign

additional security for the Bonds (or any portion thereof), or to surrender any right or power in the Indenture reserved to or conferred upon the District;

(2) to make such provisions for the purpose of curing any ambiguity, inconsistency or omission, or of curing or correcting any defective provision, contained in the Indenture, or in regard to matters or questions arising under the Indenture, as the District may deem necessary or desirable, and which will not materially and adversely affect the interests of the Owners of the Bonds;

(3) to modify, amend or supplement the Indenture in such manner as to permit the qualification hereof under the Trust Indenture Act of 1939, as amended, or any similar federal statute hereafter in effect, and to add such other terms, conditions and provisions as may be permitted by said Act or similar federal statute, and which will not materially and adversely affect the interests of the Owners of the Bonds;

(4) to make modifications or adjustments necessary, appropriate or desirable to provide for the issuance of Parity Obligations with such interest rate, payment, maturity and other terms as the District may deem desirable; subject to the provisions of the Indenture relating to the issuance of additional Bonds;

(5) to provide for the issuance of Bonds in book-entry form or bearer form, provided that no such provision will materially and adversely affect the interests of the Owners of the Bonds;

(6) if the District agrees in a Supplemental Indenture to maintain the exclusion of interest on a Series of Bonds from gross income for purposes of federal income taxation, to make such provisions as are necessary or appropriate to ensure such exclusion;

(7) to provide for the issuance of an additional Series of Bonds; and

(8) for any other purpose that does not materially and adversely affect the interests of the Owners of the Bonds.

The Trustee may in its discretion, but will not be obligated to, enter into any such Supplemental Indenture authorized by the Indenture which adversely affects the Trustee's own rights, duties or immunities under the Indenture or otherwise.

Amendments to Master Contract.

The District and the Corporation will not supplement, amend, modify or terminate any of the terms of the Master Contract, or consent to any such supplement, amendment, modification or termination, without the prior written consent of the Trustee, which such consent will be given only if (a) such supplement, amendment, modification or termination will not materially adversely affect the interests of the Owners of the Bonds or result in any material impairment of the security given for the payment of the Bonds, or (b) the Trustee first obtains the written consent of the Owners of a majority in aggregate principal amount of the Parity Obligations then outstanding and the written consent of any credit enhancers of such Parity Obligations if required by the terms of such Parity Obligations to such supplement, amendment, modification or termination, and, if the supplement, amendment, modification or termination affects certain provisions of the Master Contract relating to the pledge of Net Revenues, the conditions for the issuance of Parity Obligations, the sale or other disposition of the Property or the amounts of fees, rates and charges, the Trustee will also first obtain the written consent of a majority in aggregate principal amount of Subordinate Obligations then outstanding; provided, that any supplement that complies with the provisions of the Master Contract relating to the

execution of, and procedure for execution of, Parity Obligations and Subordinate Obligations, will not require the consent of the credit enhancers of any Obligations and will not be deemed to materially adversely affect the interests of the Owners of the Bonds or result in any material impairment of the security given for the payment of the Bonds; and provided further, that no such supplement, amendment, modification or termination reduces the amount of Payments to be made to the Trustee by the District, or extend the time for making such Payments, or permit the creation of any lien prior to or on a parity with the lien created by the Master Contract on the Payments without the written consent of all of the holders of all Obligations then outstanding.

Defeasance

Discharge of Indenture. Bonds of any Series or a portion thereof may be paid by the District in any of the following ways:

- (a) by paying or causing to be paid the Bond Obligation of and interest on such Outstanding Bonds, as and when the same become due and payable;
- (b) by depositing with the Trustee, an escrow agent or other fiduciary, in trust, at or before maturity, money or securities in the necessary amount to pay or redeem such Outstanding Bonds; or
- (c) by delivering to the Trustee, for cancellation by it, such Outstanding Bonds.

If the District will pay all Series for which any Bonds are Outstanding and also pay or cause to be paid all other sums payable under the Indenture by the District, including the Trustee's fees and expenses, or to any Credit Provider, then and in that case, at the election of the District (evidenced by a Certificate of the District filed with the Trustee signifying the intention of the District to discharge all such indebtedness and the Indenture), and notwithstanding that any Bonds will not have been surrendered for payment, the Indenture and the pledge of Net Revenues and other assets made under the Indenture and all covenants, agreements and other obligations of the District under the Indenture will cease, terminate, become void and be completely discharged and satisfied. In such event, upon Request of the District, the Trustee will cause an accounting for such period or periods as may be requested by the District to be prepared and filed with the District and will execute and deliver to the District all such instruments as may be necessary or desirable to evidence such discharge and satisfaction, and the Trustee will pay over, transfer, assign or deliver to the District all moneys or securities or other property held by it pursuant to the Indenture which, as evidenced by a verification report, upon which the Trustee may conclusively rely, from a firm of certified public accountants, are not required for the payment or redemption of Bonds not theretofore surrendered for such payment or redemption

Discharge of Liability on Bonds. Upon the deposit with the Trustee, escrow agent or other fiduciary, in trust, at or before maturity, of money or securities in the necessary amount to pay or redeem any Outstanding Bond (whether upon or prior to its maturity or the redemption date of such Bond), provided that, if such Bond is to be redeemed prior to maturity, notice of such redemption will have been given as in Article IV provided or provision satisfactory to the Trustee will have been made for the giving of such notice, then all liability of the District in respect of such Bond will cease, terminate and be completely discharged, provided that the Owner thereof will thereafter be entitled to the payment of the principal of and premium, if any, and interest on the Bonds, and the District will remain liable for such payment, but only out of such money or securities deposited with the Trustee as aforesaid for their payment, subject, however, to the provisions of the Indenture and the continuing duties of the Trustee.

The District may at any time surrender to the Trustee for cancellation by it any Bonds previously issued and delivered, which the District may have acquired in any manner whatsoever, and such Bonds, upon such surrender and cancellation, will be deemed to be paid and retired.

Deposit of Money or Securities with Trustee. Whenever in the Indenture it is provided or permitted that there be deposited with or held in trust by the Trustee money or securities in the necessary amount to pay

or redeem any Bonds, the money or securities so to be deposited or held may include money or securities held by the Trustee in the funds and accounts established pursuant to the Indenture and will be:

(a) lawful money of the United States of America in an amount equal to the principal amount of such Bonds and all unpaid interest thereon to maturity, except that, in the case of Bonds which are to be redeemed prior to maturity and in respect of which notice of such redemption will have been given as in Article IV provided or provision satisfactory to the Trustee will have been made for the giving of such notice, the amount to be deposited or held will be the principal amount or Redemption Price of such Bonds and all unpaid interest thereon to the redemption date; or

(b) Government obligations, the principal of and interest on which when due will, in the opinion of an independent certified public accountant delivered to the Trustee (upon which opinion the Trustee may conclusively rely), provide money sufficient to pay the principal or Redemption Price of and all unpaid interest to maturity, or to the redemption date, as the case may be, on the Bonds to be paid or redeemed, as such principal or Redemption Price and interest become due, provided that, in the case of Bonds which are to be redeemed prior to the maturity thereof, notice of such redemption will have been given as in Article IV provided or provision satisfactory to the Trustee will have been made for the giving of such notice;

provided, in each case, that the Trustee will have been irrevocably instructed (by the terms of the Indenture or by Request of the District) to apply such money to the payment of such principal or Redemption Price and interest with respect to such Bonds.

Payment of Bonds After Discharge of Indenture. Any moneys held by the Trustee in trust for the payment of the principal or Redemption Price of, or interest on, any Bonds and remaining unclaimed for two years after the principal of all of the Bonds has become due and payable (whether at maturity or upon call for redemption as provided in the Indenture), if such moneys were so held at such date, or two (2) years after the date of deposit of such moneys if deposited after said date when all of the Bonds became due and payable, will be repaid to the District free from the trust created by the Indenture, and all liability of the Trustee with respect to such moneys will thereupon cease; provided, however, that before the repayment of such moneys to the District as aforesaid, the Trustee may (at the cost of the District) first mail to the Owners of any Bonds remaining unpaid at the addresses shown on the registration books maintained by the Trustee a notice, in such form as may be deemed appropriate by the Trustee, with respect to the Bonds so payable and not presented and with respect to the provisions relating to the repayment to the District of the moneys held for the payment thereof. All moneys held by or on behalf of the Trustee for the payment of principal or interest or premium on Bonds, whether at redemption or maturity, will be held in trust for the account of the Owners thereof and the Trustee will not be required to pay Owners any interest on, or be liable to the Owners or any other person (other than the District) for any interest earned on, moneys so held. Any interest earned thereon will belong to the District and will be transferred monthly by the Trustee to the District for deposit into the Revenue Fund.

APPENDIX C

FORM OF OPINION OF BOND COUNSEL

[Closing Date]

Vallecitos Water District
San Marcos, California

\$45,315,000
VALLECITOS WATER DISTRICT
Water and Wastewater Enterprise 2015
Refunding Revenue Bonds

Ladies and Gentlemen:

We have acted as bond counsel to the Vallecitos Water District (the “District”), and in such capacity have examined a record of proceedings related to the issuance of \$45,315,000 Vallecitos Water District, Water and Wastewater Enterprise, 2015 Refunding Revenue Bonds (the “2015 Bonds”). The 2015 Bonds are issued under and pursuant to (i) The California County Water District Law (commencing at California Water Code Section 30,000) and all laws amendatory thereof or supplemental thereto, including Articles 10 and 11 of Chapter 3 of Part 1 of Division 2 of Title 5 of the California Government Code (together, the “Law”) (ii) the Master Installment Purchase Contract, dated as of June 15, 2005, as amended (the “Master Contract”), by and between the District and the Vallecitos Water District Financing Corporation, and (iii) an Indenture of Trust, dated as of June 1, 2015 (the “Master Indenture”), by and between the District and MUFG Union Bank, N.A., as Trustee, and a First Supplement to Indenture of Trust, dated June 1, 2015, by and between the same parties (the “First Supplement”, and collectively, the “Indenture”).

In our capacity as bond counsel, we have reviewed relevant laws of the State of California; executed copies of the Indenture, the Master Contract, originals or copies certified or otherwise identified to our satisfaction of such documents, certificates, opinions and other matters as we deemed necessary or appropriate to render the opinions set forth herein. In rendering the opinions set forth below, we have relied upon certifications and representations of the District with respect to certain material facts solely within the knowledge of the District, without undertaking to verify the same by independent investigation. Further, we have assumed, but have not independently verified, that the signatures on all documents, certificates and opinions that we reviewed are genuine. We have also assumed compliance with all covenants and agreements contained in the Indenture and the Master Contract, including (without limitation) covenants and agreements compliance with which is necessary to assure that future actions, omissions or events will not cause interest on the 2015 Bonds to be included in gross income for federal income tax purposes. Capitalized terms not otherwise defined herein shall have the meanings ascribed thereto in the Indenture.

Certain requirements and procedures contained or referred to in the Indenture or in other documents pertaining to the 2015 Bonds may be changed, and certain actions may be taken or not taken, under the circumstances and subject to the terms and conditions set forth in such documents, upon the advice or with the approving opinion of counsel nationally recognized in the area of tax-exempt obligations. We express no opinion as to the effect of any change to any document pertaining to the 2015 Bonds or of any action taken or not taken where such change is made or action is taken or not taken without our approval or in reliance upon the advice of counsel other than ourselves with respect to the exclusion from gross income of the interest on the 2015 Bonds for federal income tax purposes.

With respect to the opinions expressed herein, the enforceability of the Indenture is subject to the limitations on the imposition of certain fees and charges by the District related to the Enterprise under Articles

XIII C and XIII D of the California Constitution. In addition, the rights and obligations under the Bonds, and the Indenture and the Master Contract are subject to bankruptcy, insolvency, reorganization, arrangement, moratorium and other similar laws affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases, and to the limitations on legal remedies against public agencies in the State of California.

Based upon the foregoing and subject to the limitations and qualifications herein specified, as of the date hereof, we are of the following opinions:

1. The 2015 Bonds have been duly authorized, executed and delivered by, and constitute the valid and binding limited obligations of the District, and are payable exclusively from and are secured by a pledge of the Net Revenues of the Enterprise and certain amounts held under the Indenture. The general fund of the District is not liable and the credit or taxing power of the District is not pledged for the payment of the Bonds or the interest thereon. The 2015 Bonds are not secured by a legal or equitable pledge of, or charge, lien or encumbrance upon, any of the property of the District or any of its income or receipts, except the Net Revenues.

2. The Indenture has been duly authorized, executed and delivered by, and constitutes the valid and binding obligation of the District. The Indenture creates a valid pledge of the Net Revenues of the Enterprise (as defined in the Indenture) and certain other amounts held by the Trustee under the Indenture to secure the payment of the principal of and interest on the 2015 Bonds, as and to the extent set forth in the Indenture and subject to the provisions of the Indenture permitting the application thereof for the purposes and on the terms and conditions set forth therein.

3. Assuming continuing compliance by the District with certain covenants in the Indenture, the Master Contract and other documents pertaining to the 2015 Bonds and requirements of the Internal Revenue Code of 1986, as amended, regarding the use, expenditure and investment of proceeds of the 2015 Bonds and the timely payment of certain investment earnings to the United States, interest on the 2015 Bonds is not includable in the gross income of the owners of the 2015 Bonds for purposes of federal income taxation. Interest on the 2015 Bonds is not treated as an item of tax preference in calculating the federal alternative minimum taxable income of individuals or corporations. Interest on the 2015 Bonds, however, is included as an adjustment in the calculation of federal corporate alternative minimum taxable income and may therefore affect a corporation's alternative minimum tax liability. We express no opinion as to any other federal income tax consequences caused by the ownership of, or receipt or accrual of interest on, the 2015 Bonds.

4. Interest on the 2015 Bonds is exempt from personal income tax imposed by the State of California.

The opinions expressed and the statements made herein are based on an analysis of existing laws, regulations, rulings and court decisions. Such opinions and statements may be adversely affected by actions taken or events occurring, including a change in law, regulation or ruling (or in the application or official interpretation of any law, regulation or ruling) after the date hereof. We have not undertaken to determine, or to inform any person, whether such actions are taken or such events occur, and we have no obligation to update this letter in light of such actions or events or for any other reason.

No opinion is expressed herein on the accuracy, completeness or sufficiency of the Official Statement or other offering material relating to the 2015 Bonds.

This opinion is limited to the laws of the State of California and the federal laws of the United States. The opinions in this letter are expressed solely as of the date hereof for your benefit and may not be relied upon in any manner for any purposes by any other person.

Respectfully submitted,

APPENDIX D

INFORMATION CONCERNING DTC

The information in this section concerning DTC and DTC's book-entry only system has been obtained from sources that the District believes to be reliable, but the District takes no responsibility for the completeness or accuracy thereof. The following description of the procedures and record keeping with respect to beneficial ownership interests in the 2015 Bonds, payment of principal, premium, if any, accreted value, if any, and interest on the 2015 Bonds to DTC Participants or Beneficial Owners, confirmation and transfers of beneficial ownership interests in the 2015 Bonds and other related transactions by and between DTC, the DTC Participants and the Beneficial Owners is based solely on information provided by DTC.

The Depository Trust Company ("DTC"), New York, NY, will act as securities depository for the 2015 Bonds. The 2015 Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered 2015 Bond will be issued for each annual maturity of the 2015 Bonds, each in the aggregate principal amount of such annual maturity, and will be deposited with DTC.

DTC, the world's largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC is rated AA+ by Standard & Poor's. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Purchases of 2015 Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the 2015 Bonds on DTC's records. The ownership interest of each actual purchaser of each 2015 Bond ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the 2015 Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive bonds representing their ownership interests in 2015 Bonds, except in the event that use of the book-entry system for the 2015 Bonds is discontinued.

To facilitate subsequent transfers, all 2015 Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of 2015 Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the 2015 Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such 2015 Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of 2015 Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the 2015 Bonds, such as redemptions, tenders, defaults, and proposed amendments to the 2015 Bonds documents. For example, Beneficial Owners of 2015 Bonds may wish to ascertain that the nominee holding the 2015 Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the 2015 Bonds within a maturity are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such maturity to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to 2015 Bonds unless authorized by a Direct Participant in accordance with DTC's MMI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the District as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts 2015 Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Redemption proceeds, distributions, and dividend payments on the 2015 Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the District or the Trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Trustee, or the District, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the District or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

A 2015 Bondowner shall give notice to elect to have its 2015 Bonds purchased or tendered, through its Participant, to the Trustee, and shall effect delivery of such 2015 Bond by causing the Direct Participant to transfer the Participant's interest in the 2015 Bonds, on DTC's records, to the Trustee. The requirement for physical delivery of 2015 Bond in connection with an optional tender or a mandatory purchase will be deemed satisfied when the ownership rights in the 2015 Bond are transferred by Direct Participants on DTC's records and followed by a book-entry credit of tendered 2015 Bond to the Trustee's DTC account.

DTC may discontinue providing its services as depository with respect to the 2015 Bonds at any time by giving reasonable notice to the District or the Trustee. Under such circumstances, in the event that a successor depository is not obtained, physical certificates are required to be printed and delivered.

The District may decide to discontinue use of the system of book-entry only transfers through DTC (or a successor securities depository). In that event, 2015 Bonds will be printed and delivered to DTC.

THE TRUSTEE, AS LONG AS A BOOK-ENTRY ONLY SYSTEM IS USED FOR THE 2015 Bonds, WILL SEND ANY NOTICE OF REDEMPTION OR OTHER NOTICES TO OWNERS ONLY TO DTC. ANY FAILURE OF DTC TO ADVISE ANY DTC PARTICIPANT, OR OF ANY DTC PARTICIPANT TO NOTIFY ANY BENEFICIAL OWNER, OF ANY NOTICE AND ITS CONTENT OR EFFECT WILL NOT AFFECT THE VALIDITY OF SUFFICIENCY OF THE PROCEEDINGS RELATING TO THE REDEMPTION OF THE 2015 Bonds CALLED FOR REDEMPTION OR OF ANY OTHER ACTION PREMISED ON SUCH NOTICE.

APPENDIX E

FORM OF CONTINUING DISCLOSURE CERTIFICATE

Upon issuance of the 2015 Bonds, the District proposes to enter into a Continuing Disclosure Certificate in substantially the following form:

THIS CONTINUING DISCLOSURE AGREEMENT (this “Disclosure Agreement”), dated as of June 1, 2015, is made and entered into by the Vallecitos Water District (the “District”) and Applied Best Practices, (the “Dissemination Agent”), in connection with the issuance of the Vallecitos Water District Revenue Refunding Bonds, Series 2015A (the “Bonds”). The Bonds are being issued pursuant to an Indenture of Trust, dated as of June 1, 2015, by and between the District and MUFG Union Bank, N.A. as Trustee (the “Trustee”), as supplemented by the First Supplemental Indenture of Trust, dated as of June 1, 2015, by and between the District and the Trustee (collectively, the “Indenture”).

The District and the Dissemination Agent hereby agree as follows:

SECTION 1. Purpose of the Disclosure Agreement. This Disclosure Agreement is being executed and delivered for the benefit of the Owners and Beneficial Owners of the Bonds and in order to assist the Participating Underwriter in complying with the Rule.

SECTION 2. Definitions. In addition to the definitions set forth in the Indenture which apply to any capitalized term used in this Disclosure Agreement unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

“Annual Report” shall mean any Annual Report provided by the District pursuant to, and as described in, Sections 3 and 4 of this Disclosure Agreement.

“Beneficial Owner” shall mean any person who (a) has the power, directly or indirectly, to vote or consent with respect to, or to dispose of ownership of, any Bond (including a person holding a Bond through a nominee, depository or other intermediary), or (b) is treated as the owner of any Bond for federal income tax purposes.

“Disclosure Representative” shall mean the General Manager, the Assistant General Manager, the Director of Finance or such other officer or employee as the District shall designate in writing to the Dissemination Agent from time to time.

“Dissemination Agent” shall mean, initially, Applied Best Practices, a subsidiary of Fieldman Rolapp & Associates, acting in its capacity as Dissemination Agent hereunder, or any successor Dissemination Agent designated in writing by the District and which has been filed with the then current Dissemination Agent a written acceptance of such designation.

“EMMA” means the Municipal Securities Rulemaking Board’s Electronic Municipal Market Access System for municipal securities disclosures, maintained on the Internet at <http://emma.msrb.org/>.

“Fiscal Year” means the one-year period ending on the last day of June each year.

“Listed Events” shall mean any of the events listed in Section 5(a) of this Disclosure Agreement.

“Official Statement” shall mean the District’s official statement dated June 11, 2015, with respect to the Bonds.

“Participating Underwriter” shall mean Citigroup Global Markets Inc.

“Rule” shall mean Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time.

SECTION 3. Provision of Annual Reports.

(a) Not later than nine months after the end of the District’s fiscal year (which currently ends on June 30), commencing with the fiscal year ending June 30, 2015, the District shall, or shall cause the Dissemination Agent to, provide to EMMA an Annual Report which is consistent with the requirements of Section 4 of this Disclosure Agreement. Not later than 15 business days prior to the date referred to in the prior sentence hereof, the District shall provide the Annual Report to the Dissemination Agent. The Annual Report may be submitted as a single document or as separate documents comprising a package and may include by reference other information as provided in Section 4 of this Disclosure Agreement; provided that the audited financial statements of the District may be submitted separately from and later than the balance of the Annual Report if they are not available by the date required above for the filing of the Annual Report.

The District shall provide a written certification with each Annual Report furnished to the Dissemination Agent to the effect that such Annual Report constitutes the Annual Report required to be furnished by it hereunder. The Dissemination Agent may conclusively rely upon such certification of the District and shall have no duty or obligation to review such Annual Report.

(b) If by the date required in subsection (a) the Dissemination Agent has not received a copy of the Annual Report, the Dissemination Agent shall contact the District to determine if the District will be filing the Annual Report in compliance with subsection (a).

(c) If the Dissemination Agent is unable to verify that an Annual Report has been provided to EMMA and the Participating Underwriter by the date required in subsection (a), the Dissemination Agent shall send a notice in substantially the form attached as Exhibit A to the Municipal Securities Rulemaking Board (“MSRB”).

(d) The Dissemination Agent shall:

(i) determine each year prior to the date for providing the Annual Report and the procedure for filing with EMMA;

(ii) provide any Annual Report received by it to EMMA and the Participating Underwriter, as provided herein; and

(iii) if it has provided the Annual Report pursuant to (ii) above, file a report with the District certifying that the Annual Report has been provided to EMMA and the Participating Underwriter pursuant to this Disclosure Agreement and stating the date it was provided.

SECTION 4. Content of Annual Reports. The District’s Annual Report shall contain or include by reference:

(a) Financial Statements. The audited financial statements of the District for the most recent fiscal year of the District then ended prepared in accordance with generally accepted accounting principles as promulgated to apply to governmental entities from time-to-time by the Governmental Accounting Standards Board. If the audited financial statements are not available by the time the Annual Report is required to be filed, the Annual Report shall contain any unaudited financial statements of the District in a format similar to the audited financial statements, and the audited financial statements shall be filed in the same manner as the Annual Report when they become available.

(b) Financial and Operating Data. The Annual Report shall contain or incorporate by reference the following information:

(i) the principal amount of Bonds outstanding as of the July 2 preceding the filing of the Annual Report;

(ii) the balance in the Reserve Fund and the Reserve Requirement as of the July 2 preceding the filing of the Annual Report; and

(iii) updates of the following tables set forth under the caption entitled "THE ENTERPRISE" in the Official Statement:

1. Table No. 2, "VALLECITOS WATER DISTRICT WATER SYSTEM - SCHEDULE OF WATER UNITS AND RATES";

2. Table No. 5, "VALLECITOS WATER DISTRICT - HISTORIC METER CONNECTIONS";

3. Table No. 7, "VALLECITOS WATER DISTRICT - WATER PURCHASES AND DELIVERIES";

4. Table No. 14 "VALLECITOS WATER DISTRICT WATER SYSTEM - MONTHLY WASTEWATER SERVICE CHARGES";

5. Table No. 15, "VALLECITOS WATER DISTRICT - HISTORIC WASTEWATER CONNECTIONS"; and

6. Table No. 23, "VALLECITOS WATER DISTRICT - HISTORIC ENTERPRISE OPERATING RESULTS."

(c) Any or all of the items listed in (a) or (b) above may be included by specific reference to other documents, including official statements of debt issues of the District or related public entities, which have been submitted to EMMA or the Securities and Exchange Commission. If the document included by reference is a final official statement, it must be available from the MSRB. The District shall clearly identify each such other document so included by reference.

SECTION 5. Reporting of Significant Events.

(a) Pursuant to the provisions of this Section 5(a), the District shall give, or cause the Dissemination Agent to give, notice of the occurrence of any of the following events with respect to the Bonds in a timely manner not more than ten (10) Business Days after the event:

(i) principal and interest payment delinquencies;

(ii) unscheduled draws on debt service reserves reflecting financial difficulties;

(iii) unscheduled draws on credit enhancements reflecting financial difficulties;

(iv) substitution of credit or liquidity providers, or their failure to perform;

(v) adverse tax opinions or the issuance by the Internal Revenue Service of proposed or final determinations of taxability or of a Notice of Proposed Issue (IRS Form 5701-TEB);

- (vi) tender offers;
- (vii) defeasances;
- (viii) ratings changes; and
- (ix) bankruptcy, insolvency, receivership or similar proceedings.

Note: for the purposes of the event identified in subparagraph (9), the event is considered to occur when any of the following occur: the appointment of a receiver, fiscal agent or similar officer for an obligated person in a proceeding under the U.S. Bankruptcy Code or in any other proceeding under state or federal law in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the obligated person, or if such jurisdiction has been assumed by leaving the existing governmental body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan of reorganization, arrangement or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets or business of the obligated person.

(b) Pursuant to the provisions of Section 5(c), the District shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Bonds, if material:

1. unless described in paragraph 5(a)(5) above, notices or determinations by the Internal Revenue Service with respect to the tax status of the Bonds or other material events affecting the tax status of the Bonds;
2. the consummation of a merger, consolidation or acquisition involving an obligated person or the sale of all or substantially all of the assets of the obligated person, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms;
3. appointment of a successor or additional trustee or the change of the name of a trustee;
4. nonpayment related defaults;
5. modifications to the rights of Owners of the Bonds;
6. notices of redemption; and
7. release, substitution or sale of property securing repayment of the Bonds.

(c) If the District determines that knowledge of the occurrence of a Listed Event under Section 5(b) would be material under applicable federal securities laws, the District shall file a notice of such occurrence with EMMA in a timely manner not more than 10 Business Days after the event.

(d) While the failure to file a notice of the occurrence of a Listed Event under Section 5(a)(8) shall constitute non-compliance with the terms hereof and may be required to be disclosed by the District in accordance with the Rule, failure shall not constitute an event of default hereunder if (i) the District did not receive written notice of such rating change from the respective rating agency, (ii) the rating change was a result of a change in the rating of a liquidity or credit enhancement and the market was generally aware of the

change in the rating of such liquidity or credit enhancer or (iii) the rating agency filed a notice of such rating change with EMMA.

(e) The District hereby agrees that the undertaking set forth in this Disclosure Agreement is the responsibility of the District and that the Dissemination Agent, if other than the District, shall not be responsible for determining whether the District's instructions to the Dissemination Agent under this Section 5 comply with the requirements of the Rule.

SECTION 6. Termination of Reporting Obligation. The District's obligations under this Disclosure Agreement shall terminate upon the legal defeasance, prior redemption or payment in full of all of the Bonds. If such termination occurs prior to the final maturity of the Bonds, the District shall give notice of such termination in the same manner as for a Listed Event under Section 5(f).

SECTION 7. Dissemination Agent. The District may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out its obligations under this Disclosure Agreement, and may discharge any such Dissemination Agent, with or without appointing a successor Dissemination Agent. The Dissemination Agent shall not be responsible in any manner for the content of any notice or report prepared by the District pursuant to this Disclosure Agreement. If at any time there is not any other designated Dissemination Agent, the Trustee shall be the Dissemination Agent. The initial Dissemination Agent shall be MUFG Union Bank, N.A. The Dissemination Agent may resign by providing thirty (30) days written notice to the District and the Trustee.

SECTION 8. Amendment.

Notwithstanding any other provision of this Disclosure Agreement, the District may amend this Disclosure Agreement, and any provision of this Disclosure Agreement may be waived, provided that the following conditions are satisfied:

(a) If the amendment or waiver related to the provisions of Sections 3(a), 4, or 5, it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature or status of an obligated person with respect to the Bonds, or the type of business conducted;

(b) The undertaking hereunder, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) The amendment or waiver either (i) is approved by the Owners of the Bonds in the same manner as provided in the Indenture for amendments to the Indenture with the consent of Owners, or (ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the Owners of the Bonds.

In the event of any amendment or waiver of a provision of this Disclosure Agreement, the District shall describe such amendment in the next Annual Report, and shall include, as applicable, a narrative explanation of the reason for the amendment or waiver and its impact on the type (or, in the case of a change of accounting principles, on the presentation) of financial information or operating data being presented by the District. In addition, if the amendment relates to the accounting principles to be followed in preparing financial statements, (i) notice of such change shall be given in the same manner as for a Listed Event under Section 5(f), and (ii) the Annual Report for the year in which the change is made shall present a comparison (in narrative form and also, if feasible, in quantitative form) between the financial statements as prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles.

SECTION 9. Additional Information. . Nothing in this Disclosure Agreement shall be deemed to prevent the District from disseminating any other information, using the means of dissemination set forth in this Disclosure Agreement or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Agreement. If the District chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Agreement, the District shall have no obligation under this Agreement to update such information or include it in any future Annual Report or notice of occurrence of a Listed Event.

SECTION 10. Default. In the event of a failure of the District to comply with any provision of this Disclosure Agreement, the Trustee at the written direction of the Participating Underwriter or the Beneficial Owners of at least 25% aggregate principal amount of Outstanding Bonds, shall, or any Beneficial Owner of the Bonds may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the District to comply with its obligations under this Disclosure Agreement, but only to the extent funds have been provided to it or it has been otherwise indemnified to its satisfaction from any cost, liability, expense or additional charges of the Trustee whatsoever, including, without limitation, fees and expenses of its attorney. A default under this Disclosure Agreement shall not be deemed an Event of Default under the Indenture, and the sole remedy under this Disclosure Agreement shall be an action to compel performance.

SECTION 11. Duties, Immunities and Liabilities of Dissemination Agent. The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Agreement, and the District agrees to indemnify and save the Dissemination Agent and its officers, directors, employees and agents, harmless against any loss, expense and liabilities which it may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the costs and expenses (including attorneys' fees) of defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's negligence or willful misconduct. The obligations of the District under this Section shall survive resignation or removal of the Dissemination Agent and payment of the Bonds.

SECTION 12. Beneficiaries. This Disclosure Agreement shall inure solely to the benefit of the District, the Dissemination Agent, the Participating Underwriter and Owners and Beneficial Owners from time to time of the Bonds; and it shall create no rights in any other person or entity.

SECTION 13. Merger. Any person succeeding to all or substantially all of the Dissemination Agent's corporate trust business shall be the successor Dissemination Agent without the filing of any paper or any further act.

SECTION 14. Severability. In case any one or more of the provisions contained herein shall for any reason be held to be invalid, illegal or unenforceable in any respect, such invalidity, illegality or unenforceability shall not affect any other provision hereof.

SECTION 15. Governing Law. The validity, interpretation and performance of this Disclosure Agreement shall be governed by the laws of the State of California.

SECTION 16. Counterparts. This Disclosure Agreement may be executed in several counterparts, each of which shall be an original and all of which shall constitute but one and the same instrument.

VALLECITOS WATER DISTRICT

By: _____
General Manager of the
Vallecitos Water District

APPLIED BEST PRACTICES., as Dissemination Agent

By: _____
Its: Authorized Officer

EXHIBIT A

NOTICE OF FAILURE TO FILE ANNUAL REPORT

Name of Issuer: Vallecitos Water District

Name of Issue: Vallecitos Water District Water and Wastewater Enterprise 2015 Refunding Revenue Bonds

Date of Issuance: _____, 2015

NOTICE IS HEREBY GIVEN that the Vallecitos Water District (the "District") has not provided an Annual Report with respect to the above-named Bonds as required by Section 3 of the District Continuing Disclosure Agreement, dated as of June 1, 2015. [The District anticipates that the Annual Report will be filed by _____.]

Dated:

APPLIED BEST PRACTICES, as Dissemination Agent

By: _____

cc: District

