



**Vallecitos Water District**  
**Annual Financial Report**  
**Fiscal Years Ended June 30, 2007 and 2006**



**Vallecitos Water District**  
**Annual Financial Report**  
**Fiscal Years Ended June 30, 2007 and 2006**

*Board of Directors as of June 30, 2007:*

Darrell Gentry – President  
Tim Shell – Vice-President  
Margaret E. Ferguson – Director  
Patricia Hannan – Director  
James W. Poltl – Director

William W. Rucker – General Manager

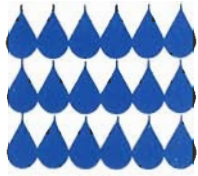
**Vallecitos Water District**  
**Annual Financial Report**  
**For the Years Ended June 30, 2007 and 2006**

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# **Financial Section**





Charles Z. Fedak, CPA, MBA  
Paul J. Kaymark, CPA

# Charles Z. Fedak & Company

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## Independent Auditor's Report

Board of Directors  
Vallecitos Water District  
San Marcos, California

We have audited the accompanying financial statements of the Vallecitos Water District (District) as of and for the years ended June 30, 2007 and 2006, which collectively comprise the District's basic financial statements as listed in the table of contents. These basic financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these basic financial statements based on our audit.

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

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the respective financial position of the Vallecitos Water District as of June 30, 2007 and 2006, and the respective changes in net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 18, 2007 on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

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

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

October 18, 2007  
Cypress, California

*Charles Z. Fedak*  
An Accountancy Corporation

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**Vallecitos Water District**  
***Management's Discussion and Analysis***  
**For the Years Ended June 30, 2007 and 2006**

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, 2007. Management's Discussion and Analysis (MD&A) presents financial highlights; an overview of the accompanying financial statements; an analysis of financial position and results of operations; a current-to-prior year analysis; a discussion on restrictions, commitments and limitations; a discussion on significant activity involving capital assets and long-term debt.

**FINANCIAL HIGHLIGHTS**

During the fiscal year ended June 30, 2007, increased regulations promulgated by State Water Resources Control Board and State Department of Health Services continued to impact the District's operations and fiscal planning. Although growth in the District's customer base has slowed, the District has nearly completed construction on significant projects that will help meet the ultimate demand within District boundaries. The following highlights for the year impacted, or have the potential to impact, the finances of the District.

- The District neared completion of construction on the Meadowlark Treatment Plant Expansion and the Twin Oaks 40 million gallon reservoir. During the fiscal year ended June 30, 2007, the District expended \$15.9 million and \$15.5 million, respectively, out of bond proceeds on the projects. The District expended \$19.2 million from reserves and restricted capacity funds on other capital projects during the year. Total capital spending amounted to \$50.6 million compared to \$31.8 million in the prior year, and \$12.7 million two years prior.
- During the fiscal year ended June 30, 2007, new development contributed \$8,547,531 in capital assets and cash to be used to fund planned capital facilities, compared to \$9,749,798 in the prior year, and \$20,282,965 two years prior.
- Debt service of \$1,769,483 included auction agent and broker fees and auction rate interest. The interest rate averaged 3.3% during 2006/07. The District made a principal payment of \$1,475,000 on July 5, 2007, before converting its remaining \$63.8 million in certificates of participation from variable rate to fixed rate debt at a total-all-in-cost of 4.736%, on July 12, 2007.
- Proposition 1A passed in November of 2004 and resulted in a loss of property tax revenue of \$947,173 in the 2004/05 fiscal year, and another \$947,173 in the 2005/06 fiscal year. Property tax revenue increased \$1,095,564 in 2006/07 from the prior year because of the full allocation received and an increase in the pass-through of Redevelopment Agency tax increment from the City of San Marcos.
- Interest earnings for 2006/07 totaled \$3,134,320 compared to \$3,485,275 in 2005/06. Increasing yields offset a declining investment portfolio balance. Remaining bond proceeds were completely expended during the year.
- Increased sewer rates, growth, and switching business customers from count-based formulas to flow basis attributed to an increase in sewer revenues of \$1.2 million, or 15.9%, and helped off set the fiscal burden of increase regulations.
- The District added 371 active meters during the fiscal year ended June 30, 2007 – a 1.9% increase, compared to 492 meters (a 2.6% increase) in the prior year, and 1,117 meters (a 6.2% increase) two years prior. The City of San Marcos issued building permits for 2,320 residential units in 2004, 1,344 in 2005, 447 in 2006, and 247 through September of 2007.
- On June 20, 2007, the District adopted two years of rate increases – effective July 1, 2007, 6% sewer and 7.2% ready-to-serve increase, effective January 1, 2008, 6.4% increase in water commodity (mostly the wholesale pass-through), effective July 1, 2008, 10% increase in sewer and 6.7% increase in ready-to-serve, and effective January 1, 2009, 6% increase in water commodity (mostly the wholesale pass-through). Increased revenues will offset wholesale rate increases, increased costs from complying with new regulations, and help maintain reserves above adopted floors.

**Vallecitos Water District**  
**Management's Discussion and Analysis**  
**For the Years Ended June 30, 2007 and 2006**

**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.

**Statements of Net Assets**

The Statements of Net Assets present the District's financial position (assets and liabilities) as of June 30, 2007, and 2006. Assets in excess of liabilities (Net Assets) were \$235,430,125 and \$227,738,839 as of June 30, 2007, and 2006, respectively. In accordance with generally accepted accounting principles, capital assets are recorded at historical cost.

**Statements of Revenues, Expenses, and Changes in Net Assets**

The Statements of Revenues, Expenses, and Changes in Net Assets present the District's results of operations for the years ended June 30, 2007, and 2006. Revenues are recognized (recorded) when water or services are provided, and expenses are recognized when incurred. Operating revenues and expenses are related to the District's core activities (providing water and related services, wastewater services, and processing and delivering recycled water). Non-operating revenues and expenses (e.g. interest income, interest expenses, etc.) are not directly related to the core activities of the District. The operating loss for the year ended June 30, 2007, of \$4,842,949 is combined with net non-operating revenues of \$3,986,704 and capital contributions of \$8,547,531 to arrive at the change in net assets of \$7,691,286. The increase in net assets is added to beginning net assets of \$227,738,839 to arrive at ending net assets of \$235,430,125 as of June 30, 2007.

Operating income / (loss)	\$ (4,842,949)
Nonoperating revenues / (expenses)	3,986,704
Capital contributions	<u>8,547,531</u>
Change in net assets	7,691,286
Beginning net assets	<u>227,738,839</u>
Ending net assets	<u>\$ 235,430,125</u>

**Statements of Cash Flows**

The Statements of Cash Flows presents the amounts of cash provided or used by the District's operating, financing, and investing activities. Every item comprising 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, 2007, represents the decrease in cash and cash equivalents of \$21,875,249, which is combined with beginning cash and cash equivalents of \$38,815,452, to arrive at ending cash and cash equivalents of \$16,940,203. Investments in the California Local Agency Investment Fund, San Diego County Investment Pool, open-ended money market mutual funds, commercial paper, and agency obligations with original maturities of 90 days or less are the only cash equivalents held by the District at June 30, 2007. As of June 30, 2007, the ending cash and cash equivalents are represented on the Statements of Net Assets as follows:

Beginning cash & cash equivalents	\$ 38,815,452
Decrease in cash & cash equivalents	<u>(21,875,249)</u>
Ending cash & cash equivalents	<u>\$ 16,940,203</u>

Unrestricted cash & cash equivalents	\$ 10,817,423
Cash & cash equivalents restricted - current	1,522,954
Cash & cash equivalents restricted - noncurrent	<u>4,599,826</u>
Total cash & cash equivalents	<u>\$ 16,940,203</u>

**Vallecitos Water District**  
**Management's Discussion and Analysis**  
**For the Years Ended June 30, 2007 and 2006**

**MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)**

**ANALYSIS OF FINANCIAL POSITION AND RESULTS OF OPERATIONS**

During the fiscal year ended June 30, 2007, the increase in total assets of \$9.6 million and the increase in total liabilities of \$1.9 million (from increased accounts payable) resulted in an increase in net assets of \$7.7 million.

Cash and investments decreased by \$40.1 million to fund construction of capital projects. The District expended, mostly out of bond proceeds, \$15.9 million for the Meadowlark Plant expansion, and \$15.5 million for the second Twin Oaks Reservoir. The District's cash funded \$6.7 million in progress payments for the Encina Wastewater Authority (EWA) expansion (EWA is a JPA of which the District is a member), \$2.5 million for North Twin Oaks reservoirs, \$2 million in Wulff pump station upgrade and tank replacement, \$1.1 million for the automated meter reading conversion, \$0.9 million for solar carports (net of a \$1.2 million grant from the San Diego Regional Energy Office), and \$6 million for the construction and acquisition of other capital assets. These cash funded projects provide for needed capacity, replacement, and operating efficiencies that will result in long-term cost savings to the District. The following table summarizes how these capital projects and debt service were financed during the year.

Sources (in millions)		Uses (in millions)	
Decrease in cash and investment balances	\$40.1	Capital construction and acquisition	\$50.6
Capital facility fees	4.6	Debt service	3.2
Investment earnings	3.3		
Operating activities	3.2		
Property taxes	2.4		
Annexation fees and other receipts	0.2		
	<u>\$53.8</u>		<u>\$53.8</u>

The operating loss of \$4,842,949 includes the depreciation expense of \$5,528,101. Depreciation is the systematic allocation of a capital asset's cost to expense over a specified period of time.

On June 30, 2005, the District issued \$66.7 million in COPs to fund the construction of a 40 million gallon buried pre-stressed concrete reservoir, fund expansion of the Meadowlark Reclamation Facility, and refund COPs of \$23.4 million issued in 1998. The 1998 COPs funded construction of a 33 million gallon reservoir and were retired on July 1, 2005. The District maintains an AA rating from Fitch Inc., an AA- from Standard & Poor's Rating Group, and purchased insurance to an AAA rating. The COPs were seven-day auction rate certificates offered initially at 2%. The rate varied between 3.0% and 3.7% (averaging 3.3%) during the 2006/07 fiscal year, while the District's rate of return on an average invested balance of \$60 million averaged 4.9% with a weighted average maturity of 107 days. Debt proceeds were expended by June 30, 2007, within two years of issuance, thereby avoiding federal arbitrage rebate rules. On July 12, 2007, the remaining \$63.8 million COPs were converted to fixed rate debt to avert interest rate risk since investment balances declined past the point of maintaining a hedge from interest on short term investments.

**CURRENT-TO-PRIOR YEAR ANALYSIS**

**Analysis of Net Assets**

As noted in the table on the following page, cash and investments have decreased by \$39.9 million, or 48.9% over the prior fiscal year. This decrease differs from the decrease in cash and investment noted above because it includes a mark-to-market adjustment of \$184,127 for the increased value in investments during the year (a non-cash adjustment). This spend-down along with funds provided by capital facility fees, operations, and property tax provided for the \$49.1 million, or 22.4%, increase in capital assets (see discussion above under "Analysis of Financial Position and Results of Operations"). Net assets increased by \$7.7 million, or 3.4%, from the prior year.

**Vallecitos Water District**  
**Management's Discussion and Analysis**  
**For the Years Ended June 30, 2007 and 2006**

**MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)**

**CURRENT-TO-PRIOR YEAR ANALYSIS (Continued)**

**Analysis of Net Assets (continued)**

Vallecitos Water District's Net Assets				
	2007	2006	Change	
			Amount	%
Cash and investments	\$ 41,638,522	\$ 81,547,184	\$ (39,908,662)	-48.9%
Capital assets	268,073,883	218,962,378	49,111,505	22.4%
Other assets	8,553,461	8,159,886	393,575	4.8%
Total Assets	<u>318,265,866</u>	<u>308,669,448</u>	<u>9,596,418</u>	3.1%
Current liabilities	18,943,375	15,929,214	3,014,161	18.9%
Noncurrent liabilities	63,892,366	65,001,395	(1,109,029)	-1.7%
Total Liabilities	<u>82,835,741</u>	<u>80,930,609</u>	<u>1,905,132</u>	2.4%
Net Assets				
Invested in capital assets, net of related debt	202,307,708	182,555,345	19,752,363	10.8%
Restricted	19,748,742	27,413,638	(7,664,896)	-28.0%
Unrestricted	13,373,675	17,769,856	(4,396,181)	-24.7%
Total Net Assets	<u>\$ 235,430,125</u>	<u>\$ 227,738,839</u>	<u>\$ 7,691,286</u>	3.4%

Vallecitos Water District Selected Financial Ratios		
	2007	2006
Current ratio	1.46	3.65
Quick ratio	1.41	3.58
Capital assets-to-Long-term liabilities	4.20 / 1	3.37 / 1
Debt-to-equity	1 / 2.84	1 / 2.81

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 1.46 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

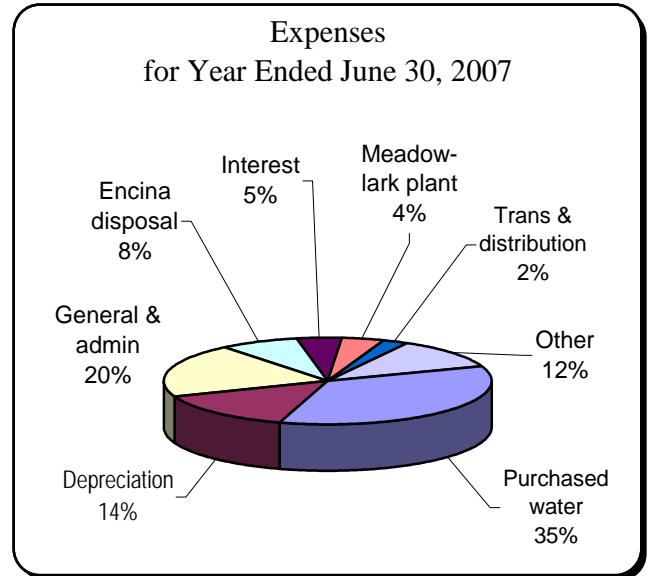
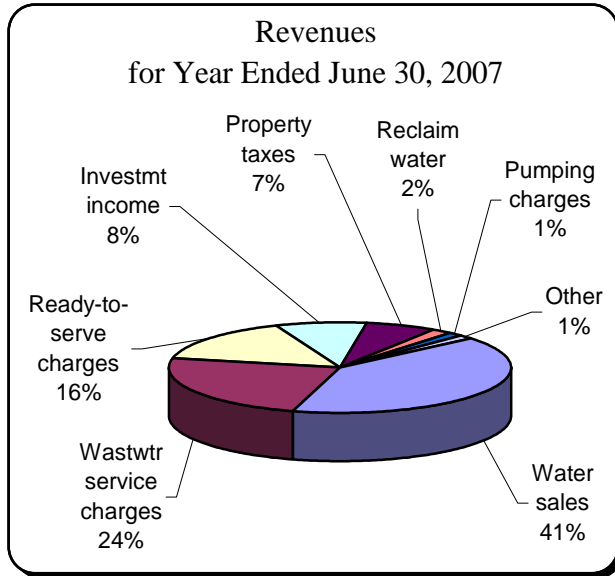
ratio, quick assets (cash, liquid investments, accounts receivable) divided by current liabilities, measures how effectively the District can meet current obligations with assets that are readily convertible to cash. The District can pay 1.41 times its current obligations with assets readily convertible to cash. The District's current and quick ratios indicate a trade-off of current position to fund construction of projects like the Meadowlark Treatment Plant Expansion, Twin Oaks Reservoir, and EWA Phase V Expansion that may satisfy flow demands for decades. The current position will improve as construction slows and customers add on to the system. The capital-assets-to-long-term-liabilities ratio indicates that for every dollar of debt the District has \$4.20 in capital assets (infrastructure, land, building, vehicles, equipment, furniture, etc.). The increase in this ratio is also testament to the trade-off in the current position to fund capital projects with limited debt. The debt-to-equity ratio indicates that for every dollar of debt the District has \$2.84 of net assets (equity).

**Vallecitos Water District**  
**Management's Discussion and Analysis**  
**For the Years Ended June 30, 2007 and 2006**

**MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)**

**CURRENT-TO-PRIOR YEAR ANALYSIS (Continued)**

**Analysis of Revenues and Expenses**



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

Vallecitos Water District's Revenues and Expenses				
	For Fiscal Year:		Change	
	2007	2006	Amount	%
Water sales	\$ 14,945,265	\$ 12,987,538	\$ 1,957,727	15.1%
Wastewater service charges	8,845,156	7,633,921	1,211,235	15.9%
Ready-to-serve charges	5,808,110	5,581,223	226,887	4.1%
Investment income	3,134,320	3,485,275	(350,955)	-10.1%
Property taxes	2,511,616	1,416,052	1,095,564	77.4%
Other revenues	1,694,511	1,579,221	115,290	7.3%
<b>Total Revenues</b>	<b>36,938,978</b>	<b>32,683,230</b>	<b>4,255,748</b>	<b>13.0%</b>
Purchased water	13,626,626	11,650,340	1,976,286	17.0%
General and administrative	7,674,817	7,097,306	577,511	8.1%
Depreciation expense	5,528,101	4,959,815	568,286	11.5%
Encina disposal	2,966,331	2,921,237	45,094	1.5%
Interest expense	1,769,483	2,000,800	(231,317)	-11.6%
Meadowlark plant	1,528,436	1,504,519	23,917	1.6%
Transmission and distribution	952,967	899,623	53,344	5.9%
Other expenses	3,748,462	3,170,797	577,665	18.2%
<b>Total Expenses</b>	<b>37,795,223</b>	<b>34,204,437</b>	<b>3,590,786</b>	<b>10.5%</b>
Income / (Loss) before contributions	(856,245)	(1,521,207)	664,962	-43.7%
Capital contributions	8,547,531	9,749,798	(1,202,267)	-12.3%
Change in Net Assets	7,691,286	8,228,591	(537,305)	-6.5%
Beginning Net Assets	227,738,839	219,510,248	8,228,591	3.7%
Ending Net Assets	<b>\$ 235,430,125</b>	<b>\$ 227,738,839</b>	7,691,286	3.4%

**Vallecitos Water District**  
*Management's Discussion and Analysis*  
**For the Years Ended June 30, 2007 and 2006**

**MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)**

**CURRENT-TO-PRIOR YEAR ANALYSIS (Continued)**

**Analysis of Revenues and Expenses (continued)**

The composition of revenues and expenses for the 2006/07 fiscal year is graphically illustrated on the preceding page. Water sales, ready-to-serve charges, and wastewater service charges continue to be the main sources of revenue funding District operations. Water sales are commodity charges assessed to cover the variable costs of purchasing and delivering water to customers. Ready-to-serve charges are intended to cover fixed costs in the wholesale water rate, and costs related to being able to provide water to customers.

- Water sales and purchased water increased due to a rate increase (ten-cent per unit increase effective January 1, 2007), growth, and unanticipated demand from drought conditions.
- The \$1.2 million increase in wastewater service charges was anticipated due to an increase in customers and rates (10% effective in January of 2007), and changing commercial customers from a fixed count-based formula (based on employees, seats, etc.) to more equitable flow based charges.
- The District received the full allocation of property taxes during 2006/07, whereas the two prior years were reduced by \$947,173 each year pursuant to Proposition 1A.
- Depreciation expense increased because of the number of capital projects completed and placed in service over the last three fiscal years.
- The increase in other costs is mainly attributable to an anticipated \$104,008 increase in engineering costs, a \$91,404 increase in information technology expenses from increased staffing and software applications, demands on resources and staffing from increased regulations, and anticipated inflationary increases in other areas.
- The 2006/07 decrease in capital contributions (capital facility fees and developer contributed assets and deposits) was caused by a continued slow-down in growth in the San Marcos area as discussed in the Financial Highlights.

**RESTRICTIONS, COMMITMENTS, AND LIMITATIONS**

**2005 Certificates of Participation**

On June 30, 2005, the District issued \$66,700,000 in Certificates of Participation (COPs) to refinance 1998 COPs, construct an additional 40 million gallon buried pre-stressed concrete reservoir at the Twin Oaks site, and expand and improve the Meadowlark Reclamation Facility. Any funds held with the fiscal agent were pledged as security. The only amounts held with the fiscal agent were the weekly interest payment (which averaged \$45,000 during 2006/07), any principle payments deposited for disbursement to bondholders, and any accrued interest. As of June 30, 2007, the fiscal agent held \$1,522,953 to pay the July 1, 2007 principle payment of \$1,475,000, to pay the weekly interest payment of \$45,005, and accrued interest of \$2,948. The 2005 COPs were auction rate certificates with the rate changing and interest payments due weekly. The net revenue requirement is 1.15 times debt service. The District's 2006/07 net revenue was 3.45 times debt service. On July 12, 2007, the remaining \$63.8 million COPs were converted to fixed rate debt with a total all-in interest cost of 4.736%. The District is required to pay principal each July 1 from 2008 through 2035 when the COPs mature. Interest is payable semi-annually. The COPs are payable from net combined water and sewer revenue of the District.

**Vallecitos Water District**  
**Management's Discussion and Analysis**  
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**MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)**

**RESTRICTIONS, COMMITMENTS, AND LIMITATIONS (Continued)**

**Capital Facility Fees**

The District collects capital facility fees from new development and increased demands from existing customers, maintains the collected fees in separate funds (one for water and one for wastewater), and uses the funds exclusively to provide capacity to serve new development and fund future construction of facilities identified in the District's Master Plan. As of June 30, 2007, the balances of cash and investments held in the capacity funds were \$13,645,962 for water and \$6,583,660 for wastewater. (The District maintains separate funds for specific purposes. Funds are combined for financial statement presentation.)

**Capital Projects**

The following budgeted projects have been contracted for at least the design phase before the 2007 fiscal year end:

Project Description	2007/08 Budget	Spent	Remaining
Meadowlark treatment plant expansion	\$ 31,585,000	\$ 28,551,828	\$ 3,033,172
Twin Oaks Reservoir #2	21,100,000	18,078,307	3,021,693
Encina Wastewater Authority Phase V expansion	18,227,000	8,490,025	9,736,975
San Marcos interceptor sewer line	16,400,000	3,317,754	13,082,246
North Twin Oaks Tank 2	5,600,000	3,087,902	2,512,098
Automated meter reading conversion	3,775,500	3,563,301	212,199
Meadowlark Tank #3	3,600,000	244,671	3,355,329
Mountain Belle pump station and pipeline	2,500,000	45,701	2,454,299
Wulff hydro-pneumatic pump station	2,300,000	959,936	1,340,064
Encina Wastewater Authority building program	2,205,500	451,290	1,754,210
Discovery Street sewer	1,850,000	121,592	1,728,408

The budget amounts above indicate the amount anticipated for completion of the projects. For some of these projects the District has only committed to the design phase through contractual obligations, and the construction has not yet been through the bidding process. Details are provided in the District's 2007-08 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 development:

Sewer mains	\$4,173,548
Water transmission and distribution mains	3,814,179
Pump stations and pumping equipment	2,676,390
Water service lines	1,560,363
Solar car ports	1,016,652

The \$66.7 million in COPs issued to refinance 1998 COPs, construct a 40 million gallon reservoir, and expand the Meadowlark Reclamation Facility is the only long-term debt owed by the District.

**Vallecitos Water District**  
*Management's Discussion and Analysis*  
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**MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)**

**ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES**

The District considered the following economic factors in establishing 2007/08 budget amounts and rates:

- Slowed but continued growth - the District anticipates adding 428 meters and four additional employment positions in the 2008 fiscal year,
- The need for improved and expanded facilities,
- Increases to wholesale water rates,
- Increased requirements related to regulatory compliance, and
- The need to stay technologically current.

As a result of these factors, the 2007/08 budget includes:

- Increased water sales and water purchases from growth and rate increases offset by decreased water demand per customer due to higher projected (average) rainfall,
- Increased wastewater service charges from an adopted 6% increase in rates effective July 1, 2007, to cover costs incurred to comply with increasing regulations,
- A 10.5% increase in salaries and benefits due to additional hires, cost of living adjustments, step increases, and anticipated increases in group insurance costs, and
- \$55.4 million in budgeted capital expenditures, including \$41.6 million in expansion costs.

**CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT**

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

# **Basic Financial Statements**

**Vallecitos Water District**  
**Statements of Net Assets**  
**June 30, 2007 and 2006**

<i>Assets</i>	<b>2007</b>	<b>2006</b>
<b>Current Assets:</b>		
Cash and cash equivalents (note 2)	\$ 10,817,423	\$ 15,209,250
Restricted cash and cash equivalents (note 2)	1,522,954	3,746,063
Investments (note 2)	8,886,323	33,362,817
Accounts receivable:		
Water and wastewater sales and services, net (note 3)	4,059,358	3,349,221
Taxes and assessments	932,826	831,638
From other governmental entities	334,618	29,801
Other	130,755	452,521
Accrued interest receivable	276,891	440,708
Current portion of note receivable (note 6)	82,632	78,324
Inventories	555,525	507,094
Prepaid expenses	118,570	182,135
<b>Total current assets</b>	<u>27,717,875</u>	<u>58,189,572</u>
<b>Non-current assets:</b>		
Restricted cash and cash equivalents (note 2)	4,599,826	19,860,139
Restricted investments (note 2)	15,811,996	9,368,915
Restricted accrued interest receivable	157,030	307,761
Restricted capital facility fees receivable	34,062	-
Note receivable from City of San Marcos, net of current portion (note 6)	1,122,422	1,205,052
Debt issuance costs, net (note 7)	520,852	538,214
Deferred charges from debt retirement, net (note 8)	227,920	237,417
Investment in Encina Wastewater Authority capital assets (Note 5)	24,180,604	16,049,383
Capital assets not being depreciated (note 4)	78,818,207	48,107,247
Net capital assets being depreciated (note 4)	165,075,072	154,805,748
<b>Total non-current assets</b>	<u>290,547,991</u>	<u>250,479,876</u>
<b>Total assets</b>	<u>318,265,866</u>	<u>308,669,448</u>
<b><i>Liabilities</i></b>		
<b>Current liabilities:</b>		
Accounts payable	11,625,792	8,203,380
Accounts payable from restricted assets	854,172	2,123,177
Accrued compensation	1,229,064	1,124,809
Construction & service deposits	3,711,395	3,000,328
Accrued interest payable from restricted assets	47,952	52,520
Current portion of long term debt (note 9)	1,475,000	1,425,000
<b>Total current liabilities</b>	<u>18,943,375</u>	<u>15,929,214</u>
<b>Non-current liabilities:</b>		
Deposit from San Marcos Unified School District	189,400	189,400
Other post employment benefits obligation, net (note 13)	351,575	-
Certificates of participation, net of amortized discount & current portion (note 9)	63,351,391	64,811,995
<b>Total non-current liabilities</b>	<u>63,892,366</u>	<u>65,001,395</u>
<b>Total liabilities</b>	<u>82,835,741</u>	<u>80,930,609</u>
<b><i>Net Assets</i></b>		
Invested in capital assets, net of related debt (note 10)	202,307,708	182,555,345
Restricted for future capital facilities	19,748,742	27,413,638
Unrestricted	13,373,675	17,769,856
<b>Total Net Assets</b>	<u>\$ 235,430,125</u>	<u>\$ 227,738,839</u>

See accompanying notes to the financial statements

**Vallecitos Water District**  
**Statements of Revenues, Expenses and Changes in Net Assets**  
**For the Years Ended June 30, 2007 and 2006**

	<b>2007</b>	<b>2006</b>
<b>Operating revenues:</b>		
Water sales	\$ 14,945,265	\$ 12,987,538
Wastewater service charges	8,845,156	7,633,921
Ready-to-serve charges	5,808,110	5,581,223
Reclaimed water sales	648,566	615,158
Pumping charges	524,043	505,073
Other services and abatements	375,579	377,372
<b>Total operating revenues</b>	<b>31,146,719</b>	<b>27,700,285</b>
<b>Operating expenses:</b>		
Purchased water	13,626,626	11,650,340
General and administrative	7,674,817	7,097,306
Encina disposal	2,966,331	2,921,237
Meadowlark wastewater treatment plant	1,528,436	1,504,519
Transmission and distribution	952,967	899,623
Engineering	735,694	631,686
Customer accounts	566,390	510,861
Pumping	456,767	460,047
Collection and conveyance	722,966	669,281
Buildings and grounds	401,096	332,546
Equipment and vehicles	297,076	282,503
Meter reading and repairs	157,125	139,806
Tanks and reservoirs	228,569	196,737
Water quality and treatment	185,836	143,327
Information technology	138,791	47,387
Other wastewater operating expenses	239,876	192,248
Other water operating expenses	262,862	177,411
<b>Total operating expenses</b>	<b>31,142,225</b>	<b>27,856,865</b>
Operating income before overhead absorption	4,494	(156,580)
Overhead absorption	680,658	613,043
Operating Income before depreciation and amortization	685,152	456,463
Depreciation and amortization	(5,528,101)	(4,959,815)
<b>Operating loss</b>	<b>(4,842,949)</b>	<b>(4,503,352)</b>
<b>Non-operating revenues (exepnses):</b>		
Property taxes	2,511,616	1,416,052
Investment income	3,134,320	3,485,275
Annexation fees	146,323	71,266
Interest expense	(1,769,483)	(2,000,800)
Other, net	(36,072)	10,352
<b>Total non-operating revenues and expenses</b>	<b>3,986,704</b>	<b>2,982,145</b>
<b>Loss before contributions</b>	<b>(856,245)</b>	<b>(1,521,207)</b>
Capital contributions	8,547,531	9,749,798
<b>Change in net assets</b>	<b>7,691,286</b>	<b>8,228,591</b>
<b>Net assets, beginning of year (Restated for prior year adjustment)</b>	<b>227,738,839</b>	<b>219,510,248</b>
<b>Net assets, end of year</b>	<b>\$ 235,430,125</b>	<b>\$ 227,738,839</b>

See accompanying notes to the financial statements

**Vallecitos Water District**  
**Statements of Cash Flows**  
**For the Years Ended June 30, 2007 and 2006**

	<u>2007</u>	<u>2006</u>
Cash flows from operating activities:		
Receipts from water and wastewater customers	\$ 31,164,598	\$ 26,832,881
Payments for water	(13,237,750)	(11,763,238)
Payments for services and supplies	(3,199,567)	(2,692,014)
Payments for employee wages, benefits and related costs	<u>(11,515,619)</u>	<u>(10,137,117)</u>
Net cash provided by operating activities	<u>3,211,662</u>	<u>2,240,512</u>
Cash Flows from non-capital financing activities:		
Receipts from taxes and assessments	<u>2,405,059</u>	<u>1,362,776</u>
Net cash provided by non-capital financing activities	<u>2,405,059</u>	<u>1,362,776</u>
Cash flows from capital and related financing activities:		
Receipts from annexation fees	146,323	71,266
Acquisition and construction of utility plant	(43,852,778)	(26,742,468)
Proceeds from Disposal of Capital assets	-	2,346
Principal paid on long term debt	(1,425,000)	(23,400,000)
Payments for costs of debt issuance	-	(44,875)
Deferred charges from debt retirement	-	(237,417)
Interest payments on long-term debt	(1,745,641)	(1,993,229)
Investment in Encina Wastewater Authority	(6,746,476)	(2,936,042)
Capacity fees received	<u>4,570,909</u>	<u>7,253,851</u>
Net cash used in capital and related financing activities	<u>(49,052,663)</u>	<u>(48,026,568)</u>
Cash flows from investing activities:		
Purchase of investments	(81,853,508)	(216,097,113)
Proceeds from sale, call and maturity of investments	100,078,224	195,789,593
Interest received	3,257,655	3,075,819
Collections on Note receivable from City of San Marcos	<u>78,322</u>	<u>74,240</u>
Net Cash provided (used) by Investing Activities	<u>21,560,693</u>	<u>(17,157,461)</u>
Net decrease in cash and cash equivalents	(21,875,249)	(61,580,741)
Cash and cash equivalents, beginning of year	<u>38,815,452</u>	<u>100,396,193</u>
Cash and cash equivalents, end of year	<u>\$ 16,940,203</u>	<u>\$ 38,815,452</u>
Reconciliation of cash and cash equivalents to statement of net assets:		
Cash and cash equivalents	\$ 10,817,423	\$ 15,209,250
Restricted cash and cash equivalents - current	1,522,954	3,746,063
Restricted cash and cash equivalents - non-current	<u>4,599,826</u>	<u>19,860,139</u>
Total cash and cash equivalents	<u>\$ 16,940,203</u>	<u>\$ 38,815,452</u>
Reconciliation of operating loss to net cash provided by operating activities:		
Net cash provided by operating activities:		
Operating loss	\$ (4,842,949)	\$ (4,503,352)
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation & amortization expense	5,528,101	4,959,815
Changes in operating assets and liabilities:		
Accounts receivable from water and wastewater sales and services	(710,137)	(363,933)
Accounts receivable from other governmental entities	(304,817)	403,006
Accounts receivable - other	321,766	(418,869)
Inventories	(48,431)	20,064
Prepaid expenses	63,565	(35,903)
Investment in Encina Wastewater Authority	943,954	807,419
Accounts payable	1,093,713	3,750,532
Accrued compensation	104,255	223,242
Other post employment benefits obligation, net	351,575	-
Construction and service deposits	<u>711,067</u>	<u>(487,608)</u>
Net cash provided by operating activities	<u>\$ 3,211,662</u>	<u>\$ 4,354,413</u>
Noncash investing capital and financing activities:		
Contributions of assets by developers	<u>\$ 3,661,706</u>	<u>\$ 4,019,555</u>
Amortization related to long-term debt	<u>\$ 14,396</u>	<u>\$ 14,936</u>
Unrealized appreciation (depreciation) of investments	<u>\$ 244,478</u>	<u>\$ 60,351</u>

See accompanying notes to the financial statements

**Vallecitos Water District**  
**Notes to the Basic Financial Statements**  
**For the Years Ended June 30, 2007 and 2006**

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

**A. Organization and Operations of the Reporting Entity**

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

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

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

**B. Basis of Accounting and Measurement Focus**

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

Operating revenues, such as water and wastewater sales and services, 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. Non-operating revenues, such as investment income, result from non-exchange transactions, in which, the District gives or receives value without directly receiving or giving value in exchange.

**C. Financial Reporting**

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

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

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

**C. Financial Reporting, continued**

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

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

**D. Implementation of New Governmental Accounting Standards Board Statements**

***Governmental Accounting Standards Board Statement No. 45***

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

**E. Assets, Liabilities, and Net Assets**

**1. Use of Estimates**

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

**2. Cash and Cash Equivalents**

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

**3. Investments and Investment Policy**

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

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

**4. Accounts Receivable and Allowance for Uncollectible Accounts**

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

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

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

**E. Assets, Liabilities, and Net Assets, continued**

**5. Federal and State Capital and Operating Grants**

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

**6. Property Taxes and Assessments**

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

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

Taxes and assessments receivable of \$932,826 and \$831,638 have been reduced by an allowance for estimated uncollectible taxes of \$14,167 and \$11,329 at June 30, 2007 and 2006, respectively.

**7. Water-In-Storage Inventory**

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

**8. Materials and Supplies Inventory**

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

**9. Prepaid Expenses**

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

**10. Restricted Assets**

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

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

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

**E. Assets, Liabilities, and Net Assets, continued**

**11. Capital Assets**

Capital assets acquired and/or constructed are capitalized at historical cost. District policy has set the capitalization threshold for reporting capital assets at \$2,500. Donated assets are recorded at estimated fair market value at the date of donation. Upon retirement or other disposition of capital assets, the cost and related accumulated depreciation are removed from the respective balances and any gains or losses are recognized. Depreciation is recorded on a straight-line basis over the estimated useful lives of the assets as follows:

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

**12. Encina Wastewater Authority**

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

**13. Deferred Charges**

The deferred charges are from bond issuance costs that will be amortized using the straight-line method over the remaining life of the respective debt service.

**14. Compensated Absences**

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

**15. Construction Advances and Deposits**

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

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

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

**E. Assets, Liabilities, and Net Assets, continued**

**16. Net Assets**

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

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

**F. Water and Wastewater Sales and Services**

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

**G. Capital Contributions**

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

**H. Economic Dependency**

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

**I. Budgetary Policies**

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

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(2) Cash and Investments**

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

	<u>2007</u>	<u>2006</u>
Cash and cash equivalents	\$ 10,817,423	15,209,250
Restricted cash and cash equivalents – current portion	1,522,954	3,746,063
Investments – current portion	8,886,323	33,362,817
Restricted cash and cash equivalents – noncurrent portion	4,599,826	19,860,139
Restricted investments	<u>15,811,996</u>	<u>9,368,915</u>
Total Cash and Investments	<u>\$ 41,638,522</u>	<u>81,547,184</u>

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

	<u>2007</u>	<u>2006</u>
Cash on hand	\$ 1,700	1,700
Deposits with financial institutions	102,307	190,228
Investments	<u>41,534,515</u>	<u>81,355,256</u>
Total cash and investments	<u>\$ 41,638,522</u>	<u>81,547,184</u>

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

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

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

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(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 debt agreement for the 1998 Twin Oaks Certificates of Participation authorizes the bond trustee to invest in money market funds. 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 \$346,203 and \$642,188 as of June 30, 2007 and 2006, respectively. Of the bank balances, up to \$100,000 is federally insured and the remaining balance is collateralized in accordance with the Code; however, the collateralized securities are not held in the District's name.

***Investment in State Investment Pool***

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

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(2) Cash and Investments, continued**

***San Diego County Pooled Investment Fund***

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

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

***Interest Rate Risk***

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

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

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

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(2) Cash and Investments, continued**

Maturities of investments at June 30, 2006, are as follows:

Investment Type	Total	Remaining Maturity (in Months)		
		12 Months Or Less	13 to 24 Months	25-60 Months
U.S. Treasury bills	\$ 4,974,834	4,974,834	-	-
Federal Home Loan Bank	17,876,015	15,908,515	1,967,500	-
Federal Farm Credit Bank	1,472,345	494,845	977,500	-
Federal Home Loan Mortgage Corporation	3,951,340	3,951,340	-	-
Federal National Mortgage Association	7,899,810	6,928,250	-	971,560
Certificates of Deposit	1,095,097	998,051	97,046	-
Commercial paper	7,980,160	7,980,160	-	-
Local Agency Investment Fund (LAIF)	33,233,355	33,233,355	-	-
San Diego County Investment Pool	1,394,775	1,394,775	-	-
Held by bond trustee:				
Money market funds	1,477,525	1,477,525	-	-
<b>Total</b>	<b>\$ 81,355,256</b>	<b>77,341,650</b>	<b>3,042,046</b>	<b>971,560</b>

***Credit Risk***

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

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

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

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(2) Cash and Investments, continued**

Credit ratings of investments as of June 30, 2006 were as follows:

Investment Types	Total	Minimum Legal Rating	Exempt From Disclosure	Rated as of Year End		
				AAA	AA+	Not Rated
U.S. Treasury bills	\$ 4,974,834	N/A	4,974,834	-	-	-
Federal Home Loan Bank	17,876,015	AA+	-	17,876,015	-	-
Federal Farm Credit Bank	1,472,345	AA+	-	1,472,345	-	-
Federal Home Loan Mortgage Corporation	3,951,340	AA+	-	3,951,340	-	-
Federal National Mortgage Association	7,899,810	AA+	-	7,899,810	-	-
Certificates of Deposit	1,095,097	N/A	-	1,095,097	-	-
Commercial paper	7,980,160	AA+	-	-	7,980,160	-
Local Agency Investment Fund (LAIF)	33,233,355	N/A	-	-	-	33,233,355
San Diego County Investment Pool	1,394,775	N/A	-	1,394,775	-	-
Held by bond trustee:						
Money market funds	1,477,525	N/A	1,477,525	-	-	-
	<u>\$ 81,355,256</u>		<u>6,452,359</u>	<u>33,689,382</u>	<u>7,980,160</u>	<u>33,233,355</u>

**Concentration of Credit Risk**

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

Issuer	2007		2006	
	Reported Amount	Portfolio Percentage	Reported Amount	Portfolio Percentage
Federal Home Loan Bank	\$ 7,912,933	19%	\$ 17,876,015	22%

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

The balance at June 30, consists of the following:

	2007	2006
Accounts receivable – water and wastewater sales and services	\$ 4,074,118	3,357,926
Allowance for uncollectible accounts	(14,760)	(8,705)
Accounts receivable – water sales, net	<u>\$ 4,059,358</u>	<u>3,349,221</u>

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(4) Capital Assets**

Changes in capital assets for 2007 were as follows:

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

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

***Prior Period Adjustment***

The District has historically capitalized sewer laterals that connect each property served by the District to the sewer system either, placed by the District or by developers, as assets and depreciated them accordingly. Upon a review of District assets, it was determined that the laterals are not owned by the District, but rather by each property served. As a result, the District has recorded a prior period adjustment to remove the capitalized laterals, related depreciation and contributed capital previously recorded. The effect of the adjustment has been reflected as a restatement of 2006 balances for each area affected as presented below. Please refer to note 18 to the basic financial statements for further discussion.

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(4) Capital Assets, continued**

Changes in capital assets for 2006 were as follows:

	<u>Balance 2005</u>	<u>Additions/ Transfers</u>	<u>Deletions/ Transfers</u>	<u>Restated Balance 2006</u>
Non-depreciable assets:				
Land	\$ 4,674,034	-	-	4,674,034
Construction-in-process	<u>23,133,763</u>	<u>37,081,281</u>	<u>(16,781,831)</u>	<u>43,433,213</u>
Total non-depreciable assets	<u>27,807,797</u>	<u>37,081,281</u>	<u>(16,781,831)</u>	<u>48,107,247</u>
Depreciable assets:				
Water transmission and distribution system	120,985,099	6,310,383	(14,363)	127,281,119
Wastewater system	72,228,428	4,435,739	(15,545,266)	61,118,901
Buildings	13,770,844	61,735	-	13,832,579
Transportation equipment	2,281,791	274,661	(131,458)	2,424,994
Field and shop equipment	5,840,943	1,032,991	-	6,873,934
Office equipment	<u>1,017,447</u>	<u>48,055</u>	<u>(22,910)</u>	<u>1,042,592</u>
Total depreciable assets	<u>216,124,552</u>	<u>12,163,564</u>	<u>(15,713,997)</u>	<u>212,574,119</u>
Accumulated depreciation and amortization:				
Water transmission and distribution system	(25,740,471)	(2,504,700)	12,793	(28,232,378)
Wastewater system	(21,494,096)	(1,708,710)	2,995,370	(20,207,436)
Buildings	(2,181,941)	(288,989)	-	(2,470,930)
Transportation equipment	(1,043,888)	(249,474)	102,504	(1,190,858)
Field and shop equipment	(4,509,614)	(415,695)	-	(4,925,309)
Office equipment	<u>(680,494)</u>	<u>(81,374)</u>	<u>20,408</u>	<u>(741,460)</u>
Total accum depr. and amort.	<u>(55,650,504)</u>	<u>(5,248,942)</u>	<u>3,131,075</u>	<u>(57,768,371)</u>
Total depreciable assets, net	<u>160,474,048</u>	<u>6,914,622</u>	<u>(12,582,922)</u>	<u>154,805,748</u>
Total capital assets, net	<u>\$ 188,281,845</u>	<u>43,995,903</u>	<u>(29,364,753)</u>	<u>202,912,995</u>

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(4) Capital Assets, continued**

***Construction-In-Process***

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

<u>Project Name</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>
<i>District Financed</i>			
Meadowlark Plant Expansion	\$ -	13,067,765	28,551,828
Twin Oaks Reservoir	-	868,874	14,580,065
Twin Oaks Reservoir #2	-	2,086,649	3,455,664
SM interceptor - SM Blvd/Discovery	1,869,431	1,013,633	3,317,754
North Twin Oaks reservoir 2 & 3 San Marcos Mtn / Merriam Mtn	228,366	1,602,679	3,087,902
Land outfall replacement 24" & 54" Laurels to Carillo Ranch	1,250,083	775,855	2,596,117
Facility/Maintenance data management system	303,753	1,602,679	2,236,337
Automated Meter Reading Conversion	-	1,168,433	1,944,232
Wulff Pump Station - Upgrade	261,555	262,978	1,897,260
Lift Station #3	-	220,570	1,854,380
North Twin Oaks Pump Station Upgrade	-	1,112,420	1,588,819
Wulff Reservoir	-	-	959,936
San Elijo Road Facilities	-	-	641,204
Finance & Customer Information Systems	-	-	303,323
Miscellaneous Road Improvements	-	280,847	280,847
Meadowlark Tank #3	-	196,519	244,671
Meadowlark Plant expansion design	1,765,027	3,270,011	-
Deer Springs pump station replacement	1,474,017	1,569,387	-
Radio read meters	1,317,582	900,669	-
South Lake Pump Station improvement project	900,536	-	-
Slip lining for outfall under I-5	849,480	-	-
Water wastewater reclamation FY 2000-2001 master plan update	690,899	335,650	-
Sewer flow monitoring stations	277,187	1,600,260	-
City of San Marcos water/sewer plan check - Rancho Santa Fe Rd	276,562	-	-
Sewer main replacement- Linda Vista/Pacific	234,702	2,520,785	-
Gravity portion of Montiel Lift Station	216,777	-	-
Los Posas Road Improvements	-	570,642	-
Rancho Santa Fe Rd Phase I	-	254,973	-
Solar Carport Covers	-	829,156	-
Emergency Replacement 24" RPM	-	295,795	-
Subtotal - District Financed	<u>\$ 11,915,957</u>	<u>36,407,229</u>	<u>67,540,339</u>
<i>Developer Financed</i>			
La Costa Ridge 2.3 / 2.5 & Street Improvements	\$ -	-	425,252
Oceanside-Escondido rail project-railroad right of way & CSUSM loop	210,048	310,216	323,472
Las Posas widening - Las Posas drainage Grand to Mission	213,633	213,633	221,781
San Elijo Hills 1530 Zone Reservoir	-	-	145,020
Altman Subdivision	-	-	106,127
Merriam Mtn / Stonegate WS Study	-	-	105,038
Univ. Commons, San Elijo Hills Rd. improvement water/sewer plan check	1,259,517	1,198,823	-
Euston Homes water/sewer grading plan check	1,195,082	-	-
Rancho Coronado Village B-4 water/sewer plan check Twin Oaks Valley Rd	525,626	217,761	-
TSM 430 water/sewer plan check	363,800	-	-
San Marcos track 432 water/sewer plan check, Mission Rd	254,786	-	-
University Commons, TSM 421 unit 11, Shadetree DR	213,650	-	-
University Commons, Unit 3, San Elijo Rd, water/sewer plan check	212,451	212,451	-
University Commons TSM 421, Unit 1 water/sewer plan check	206,607	304,005	-
University Commons Unit 5	-	115,465	-
Subtotal - Developer Financed	<u>\$ 4,655,200</u>	<u>2,572,354</u>	<u>1,326,690</u>
Various Other Projects	<u>\$ 6,562,606</u>	<u>4,453,630</u>	<u>5,277,144</u>
Total	<u>\$ 23,133,763</u>	<u>43,433,213</u>	<u>74,144,173</u>

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(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, 2007, the Member Agencies have the following approximate ownership interest:

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

The latest available financial statements of EWA, dated June 30, 2007 and 2006, are available directly from EWA (6200 Avenida Encinas, Carlsbad, California 92009), and show the following:

	<u>2007</u>	<u>2006</u>
Total assets	\$ 75,229,524	66,487,445
Total liabilities	<u>2,945,630</u>	<u>3,649,739</u>
Total net assets	\$ <u>72,283,894</u>	<u>62,837,706</u>
Increase(decrease) in net assets	\$ <u>9,446,188</u>	<u>10,772,317</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, 2007, the following amounts are due to the District:

<u>Fiscal Year</u>	<u>Principal Amount</u>
2008	\$ 82,632
2009	87,176
2010	91,971
2011	97,029
2012	102,365
2013-2017	602,734
2018	<u>141,147</u>
Total	1,205,054
Current portion	<u>(82,632)</u>
Non-current portion	\$ <u>1,122,422</u>

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(7) Debt Issuance Costs**

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

The balance at June 30, consists of the following:	<u>2007</u>	<u>2006</u>
Debt issuance costs	\$ 538,214	555,576
Accumulated amortization	<u>(17,362)</u>	<u>(17,362)</u>
Debt issuance costs, net	<u>\$ 520,852</u>	<u>538,214</u>

**(8) Deferred Charges from Debt Retirement**

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

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

The balance at June 30, consists of the following:	<u>2007</u>	<u>2006</u>
Deferred charges from debt retirement	\$ 237,417	246,914
Accumulated amortization	<u>(9,497)</u>	<u>(9,497)</u>
Deferred charges from debt retirement, net	<u>\$ 227,920</u>	<u>237,417</u>

**(9) Long-term Debt**

***2005 Certificates of Participation***

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

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

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

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(9) Long-term Debt, continued**

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

	<u>2006</u>	<u>Additions</u>	<u>Principal Pmts Amortization</u>	<u>2007</u>
2005 Auction Rate Certificates	\$ 66,700,000	-	(1,425,000)	65,275,000
Less: Unamortized Discount	<u>(463,005)</u>	-	<u>14,396</u>	<u>(448,609)</u>
Total	<u>66,236,995</u>	-	<u>(1,410,604)</u>	<u>64,826,391</u>
Less: current portion	(1,425,000)			(1,475,000)
Long-term portion	<u>\$ 64,811,995</u>			<u>63,351,391</u>

Annual debt service payments are as follows:

<u>Fiscal Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2008	\$ 1,475,000	2,259,119	3,734,119
2009	1,500,000	2,206,341	3,706,341
2010	1,550,000	2,151,664	3,701,664
2011	1,625,000	2,134,614	3,759,614
2012	1,675,000	2,034,139	3,709,139
2013-2017	9,375,000	9,236,010	18,611,010
2018-2022	11,225,000	7,376,729	18,601,729
2023-2026	13,425,000	5,138,865	18,563,865
2027-2032	14,675,000	2,549,199	17,224,199
2033-2036	<u>8,750,000</u>	<u>487,696</u>	<u>9,237,696</u>
Total	<u>\$ 65,275,000</u>	<u>35,574,376</u>	<u>100,849,376</u>
Less: current portion	<u>(1,475,000)</u>		
Non-current portion	<u>\$ 63,800,000</u>		

***Subsequent Conversion***

Subsequent to June 30, 2007, the District converted \$63,800,000 of Series 2005 A COPs that were originally executed as Auction Rate Certificates with variable interest rates, to a fixed rate structure respective to the maturities of the Certificates. Interest rates range from 4.00% to 5.25% with payments scheduled on January 1 and July 1 of each year commencing January 1, 2008 and maturing July 1, 2035.

**(10) Net Investment in Capital Assets**

	<u>2007</u>	<u>Restated 2006</u>
The balance at June 30, consists of the following:		
Investment in Encina Wastewater Authority capital assets	\$ 24,180,604	16,049,383
Capital assets not being depreciated	78,818,207	48,107,247
Net capital assets being depreciated	165,075,072	154,805,748
Debt issuance costs net of amortization	520,852	538,214
Deferred charges from debt retirement	227,920	237,417
Certificates of participation – current portion	(1,475,000)	(1,425,000)
Deposit from San Marcos Unified School District	(189,400)	(189,400)
Portion of COPs attributable to spent proceeds	<u>(64,850,547)</u>	<u>(35,568,264)</u>
Net investment in capital assets	<u>\$ 202,307,708</u>	<u>182,555,345</u>

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(11) Deferred Compensation Savings Plan**

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

Federal law requires deferred compensation assets to be held in trust for the exclusive benefit of the participants. Accordingly, the District is in compliance with this legislation. Therefore, these assets are not the legal property of the District, and are not subject to claims of the District's general creditors. Market value of all plan assets held in trust by the District's two deferred compensation plans at June 30, 2007 and 2006 amounted to \$1,347,001 and \$1,140,062, respectively.

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

**(12) Defined Benefit Pension Plan**

***Plan Description***

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

***Funding Policy***

The contribution rate for plan members in the CalPERS 3.0% at 60 Risk Pool Retirement Plan is 8% of their annual covered salary. The Agency makes these contributions required of Agency employees on their behalf and for their account. Also, the Agency is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The required employer contribution rate for fiscal years 2007, 2006 and 2005 were 19.688%, 19.182% and 14.260%, respectively. The contribution requirements of the plan members are established by State statute, and the employer contribution rate is established and may be amended by CalPERS. For fiscal years 2007, 2006 and 2005, the Agencies annual contribution was \$1,159,400, \$1,072,497 and \$633,679, respectively, for CalPERS and was equal to the Agencies required and actual contribution for each year.

**(13) Post Employment Benefits**

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

The total expense incurred for these benefits for retired employees for the year ended June 30, 2007 and 2006 was \$106,722 and \$98,500, respectively.

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(13) Post Employment Benefits, continued**

***Other Post-Employment Benefits Obligation***

***Plan Description***

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

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

***Funding Policy***

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

***Annual OPEB Cost***

For the year ended June 30, 2007, the annual OPEB cost is \$470,948, and \$119,373, or 25.3%, in contributions were made. Because the District implemented GASB 45 for the first time this year, the difference, or net OPEB obligation of \$351,575, is both the increase and net OPEB obligation at the end of the year, and is comprised only of the Annual Required Contribution with no interest or adjustments.

***Funded Status of the Plan***

The most recent valuation (dated July 1, 2006) includes an Actuarial Accrued Liability and Unfunded Actuarial Accrued Liability of \$3,084,165. There are no plan assets because the District funds on a pay-as-you-go basis and maintains reserves equal to the remaining net OPEB obligation. No trend information is reported because the year ended June 30, 2007, is the first year the District implemented GASB 45. The covered payroll (annual payroll of active employees covered by the plan) for the year ended June 30, 2007 is \$6,543,659. The ratio of the unfunded actuarial liability to annual covered is 47.1%.

***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.

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(13) Post Employment Benefits, continued**

*Other Post-Employment Benefits Obligation, continued*

*Actuarial Methods and Assumptions, continued*

The District's valuation uses the Projected Unit Credit actuarial cost method to project the Annual Required Contribution and a 4% investment return assumption. The high rate of annual health care cost increases experienced in recent years is assumed to gradually decrease – 10% in 2006/07, 9% in 2007/08, 8% in 2008/09, 7% in 2009/10, 6% in 2010/11, and 5.5% in 2011/12. A level dollar amortization of the Unfunded Actuarial Accrued Liability is used over a closed 30-year period.

**(14) Risk Management**

The District is exposed to various risks of loss related to torts, theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District is a member of the Association of California Water Agencies/Joint Powers Insurance Authority (ACWA/JPIA), an intergovernmental risk sharing joint powers authority created to provide self-insurance programs for California water agencies. The purpose of the ACWA/JPIA is to arrange and administer programs of self-insured losses and to purchase excess insurance coverage. At June 30, 2007, the District participated in the liability and property programs of the ACWA/JPIA as follows:

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

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

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

Settled claims have not exceeded any of the coverage amounts in any of the last three fiscal years and there were no reductions in the District's insurance coverage during the years ending June 30, 2007 and 2006. 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, 2007 and 2006.

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(15) Segment Information**

**Condensed Statement of Net Assets**

	<b>2007</b>			<b>2006</b>
	<b>Water</b>	<b>Sewer</b>	<b>Total</b>	<b>Total</b>
<b>Assets:</b>				
Current assets	19,053,674	8,664,201	27,717,875	58,189,572
Non-current assets	14,969,701	7,504,407	22,474,108	31,517,498
Capital assets, net	156,762,311	111,311,572	268,073,883	218,962,378
<b>Total assets</b>	<b>190,785,686</b>	<b>127,480,180</b>	<b>318,265,866</b>	<b>308,669,448</b>
<b>Liabilities:</b>				
Current liabilities	12,880,055	6,063,320	18,943,375	15,929,214
Non-current liabilities	41,603,946	22,288,420	63,892,366	65,001,395
<b>Total liabilities</b>	<b>54,484,001</b>	<b>28,351,740</b>	<b>82,835,741</b>	<b>80,930,609</b>
<b>Net assets:</b>				
Invested in capital assets, net of related debt	114,085,570	88,222,138	202,307,708	182,555,345
Restricted for future capital facilities	13,391,395	6,357,347	19,748,742	27,413,638
Unrestricted	8,824,720	4,548,955	13,373,675	17,769,856
<b>Total net assets</b>	<b>136,301,685</b>	<b>99,128,440</b>	<b>235,430,125</b>	<b>227,738,839</b>

**Condensed Statement of Revenues, Expenses and Changes in Net Assets**

	<b>2007</b>			<b>2006</b>
	<b>Water</b>	<b>Sewer</b>	<b>Total</b>	<b>Total</b>
<b>Revenues:</b>				
Operating revenues	21,627,739	9,518,980	31,146,719	27,700,285
Non-operating revenues	3,347,073	2,409,114	5,756,187	4,982,945
<b>Total revenues</b>	<b>24,974,812</b>	<b>11,928,094</b>	<b>36,902,906</b>	<b>32,683,230</b>
<b>Expenses:</b>				
Operating expenses	21,265,696	9,195,871	30,461,567	27,243,822
Depreciation and amortization	3,620,341	1,907,760	5,528,101	4,959,815
Non-operating expenses	1,150,164	619,319	1,769,483	2,000,800
<b>Total expenses</b>	<b>26,036,201</b>	<b>11,722,950</b>	<b>37,759,151</b>	<b>34,204,437</b>
<b>Net income/(loss) before capital contributions</b>	<b>(1,061,389)</b>	<b>205,144</b>	<b>(856,245)</b>	<b>(1,521,207)</b>
Capital contributions	6,192,839	2,354,692	8,547,531	9,749,798
<b>Change in net assets</b>	<b>5,131,450</b>	<b>2,559,836</b>	<b>7,691,286</b>	<b>8,228,591</b>
Net assets, beginning of year (Restated)	131,170,235	96,568,604	227,738,839	219,510,248
Net assets, end of year	136,301,685	99,128,440	235,430,125	227,738,839

**Condensed Statement of Cash Flows**

	<b>2007</b>			<b>2006</b>
	<b>Water</b>	<b>Sewer</b>	<b>Total</b>	<b>Total</b>
<b>Net cash provided (used) by:</b>				
Operating activities	1,122,368	2,089,294	3,211,662	2,240,512
Non-capital financing activities	1,295,188	1,109,871	2,405,059	1,362,776
Capital and related financing activities	(28,975,260)	(20,077,403)	(49,052,663)	(48,026,568)
Investing activities	7,198,726	14,361,967	21,560,693	(17,157,461)
<b>Net cash provided</b>	<b>(19,358,978)</b>	<b>(2,516,271)</b>	<b>(21,875,249)</b>	<b>(61,580,741)</b>
Cash and cash equivalents, beginning of year	28,946,324	9,869,128	38,815,452	100,396,193
Cash and cash equivalents, end of year	9,587,346	7,352,857	16,940,203	38,815,452

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(16) Governmental Accounting Standards Board Statements Issued, Not Yet Effective**

The Governmental Accounting Standards Board (GASB) has issued several pronouncements prior to June 30, 2007, that has effective dates that may impact future financial presentations.

***Governmental Accounting Standards Board Statement No. 48***

In September 2006, the GASB issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*. This statement establishes criteria that governments will use to ascertain whether certain transactions should be regarded as sales or as collateralized borrowings. This statement also includes disclosure requirements for future revenues that are pledged or sold. This statement is not effective for this District until the fiscal year ended June 30, 2008. This statement is not expected to have a significant impact on the presentation of the District's financial statements.

***Governmental Accounting Standards Board Statement No. 49***

In November 2006, the GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. This statement provides guidance on how to calculate and report the costs and obligations associated with pollution cleanup efforts. This statement is not effective for this District until the fiscal year ended June 30, 2009. This statement is not expected to have a significant impact on the presentation of the District's financial statements.

***Governmental Accounting Standards Board Statement No. 50***

In May 2007, the GASB issued Statement No. 50, *Pension Disclosures, an amendment of GASB Statements No. 25 and 27*. This statement more closely aligns the financial reporting requirements for pensions with those for other post-employment benefits (OPEB) and, in doing so, enhances information disclosed in the notes to financial statements or presented as required supplementary information (RSI) by pension plans and by employers that provide pension benefits. The reporting changes required by this Statement amend applicable note disclosure and RSI requirements of GASB Statements No. 25 and 27, to conform with requirements of GASB Statements No. 43 and 45. This statement is not effective for this District until the fiscal year ended June 30, 2009. This statement is not expected to have a significant impact on the presentation of the District's financial statements.

***Governmental Accounting Standards Board Statement No. 51***

In June 2007, the GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. This statement requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets. This statement is not effective for this District until the fiscal year ended June 30, 2010. This statement is not expected to have a significant impact on the presentation of the District's financial statements.

**Vallecitos Water District**  
**Notes to the Basic Financial Statements, continued**  
**For the Years Ended June 30, 2007 and 2006**

**(17) 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 \$8,197,843 in open construction contracts as of June 30, 2007. These include the following:

<u>Project Name</u>	<u>Contract[s]</u>	<u>To Date</u>	<u>Balance</u>
Meadowlark Reclamation Facility Expansion	\$ 26,548,949	22,996,454	3,552,495
Twin Oaks No. 2 Reservoir	16,708,677	14,572,847	2,135,830
Twin Oaks Reservoir Mass Grading	5,268,512	2,758,994	2,509,518
	<u>\$ 48,526,138</u>	<u>40,328,295</u>	<u>8,197,843</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.

**(18) Prior Period Adjustment**

The District has historically capitalized sewer laterals that connect each property served by the District to the sewer system either, placed by the District or by developers, as assets and depreciated them accordingly. Upon a review of District assets, it was determined that the laterals are not owned by the District but, rather by each property owner served. As a result, the District has recorded a prior period adjustment to remove the capitalized laterals, related depreciation and contributed capital previously recorded. The effect of the adjustment has been reflected as a restatement of 2006 balances for each area affected as presented below.

	<u>June 30, 2006</u> <u>As Previously</u> <u>Reported</u>	<u>Adjustment</u>	<u>June 30, 2006</u> <u>As Restated</u>
Statements of Net Assets:			
Assets:			
Capital assets not being depreciated-Work-in-process	49,020,447	(913,200)	48,107,247
Net capital assets being depreciated - Laterals	167,355,644	(12,549,896)	154,805,748
Net Assets:			
Invested in capital assets, net of related debt	196,018,439	(13,463,094)	182,555,345
Statements of Revenues, Expenses and Changes in Net Assets			
Expenses:			
Depreciation and amortization	5,248,942	(289,127)	4,959,815
Contributions			
Capital contributions	11,748,807	(1,999,009)	9,749,798
Net assets, beginning of year	231,263,462	(11,753,214)	219,510,248

## **Required Supplementary Information**



**Vallecitos Water District**  
**Schedule of Funding Progress – Other Post-employment Benefits Plan**  
**For the Years Ended June 30, 2007 and 2006**

**Other Post-employment Benefits Plan**

***Funding Status***

The District funds Other Post-employment Benefits (OPEB) on a pay-as-you-go basis, and does not prefund the Actuarial Accrued Liability. Instead, the District maintains reserves equal to the end of year Net OPEB Obligation. The covered payroll (annual payroll of active employees covered by the plan) for the year ended June 30, 2007 is \$6,543,659. The ratio of the unfunded actuarial liability to annual covered is 47.1%.

***Trend Information***

No trend information is provided because this is the first year GASB 45 was implemented.

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# **Supplementary Information Section**



**Vallecitos Water District**  
**Combining Schedule of Revenue, Expenses, and Changes in Net Assets**  
**For the Year Ended June 30, 2007 with Comparative Totals for the Year Ended June 30, 2006**

	<b>2007</b>			<b>2006 Total</b>
	<b>Water</b>	<b>Wastewater</b>	<b>Total</b>	
Operating revenue	\$ 21,627,739	9,518,980	31,146,719	27,700,285
Operating expenses:				
Water division	21,265,696	-	21,265,696	18,404,370
Wastewater division	-	9,195,871	9,195,871	8,839,452
Depreciation	3,620,341	1,907,760	5,528,101	4,959,815
Total operating expenses	24,886,037	11,103,631	35,989,668	32,203,637
Operating loss	(3,258,298)	(1,584,651)	(4,842,949)	(4,503,352)
Non-operating revenue(expense)				
Property taxes	1,341,712	1,169,904	2,511,616	1,416,052
Interest and investment earnings	2,030,589	1,103,731	3,134,320	3,485,275
Annexation fees	-	146,323	146,323	71,266
Interest expense – long-term debt	(1,150,164)	(619,319)	(1,769,483)	(2,000,800)
Other non-operating revenues/(expenses), net	(25,228)	(10,844)	(36,072)	10,352
Total nonoperating revenues and expenses	2,196,909	1,789,795	3,986,704	2,982,145
Net loss before capital contributions	(1,061,389)	205,144	(856,245)	(1,521,207)
Capital contributions	6,192,839	2,354,692	8,547,531	9,749,798
Change in net assets	5,131,450	2,559,836	7,691,286	8,228,591
Net assets, beginning of year	131,100,127	96,638,712	227,738,839	219,510,248
Net assets, end of year	\$ 136,231,577	99,198,548	235,430,125	227,738,839

**Vallecitos Water District**  
**Schedule of Operating Expenses – Water Division**  
**For the Years Ended June 30, 2007 and 2006**

	<u>2007</u>	<u>2006</u>
Purchased Water	\$ 13,626,626	\$ 11,650,340
Pumping:		
Labor	72,608	76,317
Materials and supplies	16,434	26,051
Outside repair	6,387	7,459
Power	361,338	350,220
Total Pumping	<u>456,767</u>	<u>460,047</u>
Water Quality and Treatment:		
Labor	85,715	85,807
Materials and supplies	25,119	15,768
Outside Repair	44,793	34,316
Power	30,209	7,436
Total Water Treatment	<u>185,836</u>	<u>143,327</u>
Tanks and Reservoirs:		
Labor	159,668	135,284
Materials and supplies	27,863	32,396
Outside repair	38,367	26,802
Telemetry and power	2,671	2,254
Total Tanks and Reservoirs	<u>228,569</u>	<u>196,737</u>
Transmission and Distribution:		
Labor	597,205	579,623
Materials and supplies	157,939	158,124
Outside repair	122,842	121,593
Telemetry and power	74,981	40,283
Total Transmission and Distribution	<u>952,967</u>	<u>899,623</u>
Services:		
Labor	79,596	53,047
Materials and supplies	44,409	30,366
Outside repair	60,652	33,313
Total Services	<u>184,657</u>	<u>116,726</u>
Meters:		
Labor	56,603	37,900
Materials and supplies	19,703	23,979
Outside repair	6,668	3,660
Total Meters	<u>\$ 82,974</u>	<u>\$ 65,539</u>

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**Vallecitos Water District**  
**Schedule of Operating Expenses – Water Division, continued**  
**For the Years Ended June 30, 2007 and 2006**

	<u>2007</u>	<u>2006</u>
Backflow Prevention:		
Labor	\$ 28,337	\$ 25,439
Materials and supplies	-	80
Total Backflow Prevention	<u>28,337</u>	<u>25,519</u>
Meter Reading:		
Labor	<u>74,151</u>	<u>74,267</u>
Customer Accounts:		
Labor	327,428	313,655
Materials and supplies	75,364	63,779
Uncollectible accounts	30,125	16,979
Total Customer Accounts	<u>432,917</u>	<u>394,413</u>
Equipment and Vehicles:		
Labor, fuel and repairs	138,753	93,391
Materials and supplies	116,017	160,149
Allocated to wastewater division	(101,358)	(96,833)
Total Equipment and Vehicles	<u>153,412</u>	<u>156,707</u>
Building and Grounds:		
Labor	156,824	120,713
Materials and supplies	37,493	33,522
Outside Repair	129,441	79,364
Power	77,338	98,948
Allocated to wastewater division	(162,030)	(129,838)
Total Building and Grounds	<u>239,066</u>	<u>202,709</u>
Engineering:		
Labor	654,638	579,581
Materials and supplies	7,404	10,717
Outside Repair	73,652	41,388
Allocated to wastewater division	(294,208)	(243,069)
Total Engineering	<u>441,486</u>	<u>388,617</u>
Safety:		
Labor	49,397	39,440
Materials and supplies	18,962	11,132
Safety support	15,281	6,304
Allocated to wastewater division	(33,775)	(21,714)
Total Safety	<u>\$ 49,865</u>	<u>\$ 35,163</u>

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**Vallecitos Water District**  
**Schedule of Operating Expenses – Water Division, continued**  
**For the Years Ended June 30, 2007 and 2006**

	<u>2007</u>	<u>2006</u>
Information Technology		
Labor	\$ 88,192	\$ -
Materials and supplies	4,869	4,800
Outside Repair	45,730	42,587
Allocated to wastewater division	(41,498)	-
Total Information Technology	<u>97,293</u>	<u>47,387</u>
 General and Administration:		
Salaries	1,956,077	2,052,713
Other taxes/benefits	40,521	32,237
Social security	866,634	826,777
Group insurance	1,189,304	1,070,617
Public employees' retirement	1,742,498	1,327,389
Workers' compensation insurance	111,243	138,412
District insurance	252,747	219,085
Director's expense	67,949	81,523
Director's fees	52,500	61,650
Public awareness	95,224	85,797
Travel	20,459	8,308
Postage	20,039	10,319
Telephone	40,013	41,396
Office supplies	48,257	63,691
Dues and subscriptions	59,269	63,884
Meetings and seminars	70,997	53,625
Office equipment repair	28,148	11,846
Legal	146,064	123,120
Auditing	21,236	25,694
Outside services	58,368	124,455
Election and annexations	2,632	4,692
Other	38,153	34,643
Administrative credits transferred	(466,671)	(466,238)
Allocated to wastewater division	(2,430,888)	(2,448,386)
Total General and Administration	<u>4,030,773</u>	<u>3,547,249</u>
 Total Water Division Expenses	<u>\$ 21,265,696</u>	<u>\$ 18,404,370</u>

**Vallecitos Water District**  
**Schedule of Operating Expenses – Wastewater Division**  
**For the Years Ended June 30, 2007 and 2006**

	<u>2007</u>	<u>2006</u>
Collection System:		
Labor	\$ 436,511	\$ 373,845
Materials and supplies	199,808	225,778
Outside repair	85,167	68,469
Power	1,480	1,190
Total Collection System	<u>722,966</u>	<u>669,282</u>
Lift Stations:		
Labor	57,563	32,787
Materials and supplies	21,243	6,797
Outside repair	3,548	4,000
Power	36,326	30,167
Telemetry	-	(81)
Total Lift Stations	<u>118,680</u>	<u>73,670</u>
Peroxide Station:		
Labor	8,630	8,939
Materials and supplies	1,238	1,476
Outside repair	197	850
Power	203	192
Telemetry	207	571
Total Peroxide Station	<u>10,475</u>	<u>12,028</u>
Industrial Waste:		
Labor	8,238	6,844
Materials and supplies	38,900	38,099
Total Industrial Waste	<u>47,138</u>	<u>44,943</u>
Encina Disposal	<u>2,966,331</u>	<u>2,921,237</u>
Meadowlark Lift Station:		
Labor	27,041	21,638
Materials and supplies	2,293	2,988
Outside repair	2,726	1,856
Power	43,141	33,934
Telemetry	-	-
Total Meadowlark Lift Station	<u>\$ 75,201</u>	<u>\$ 60,416</u>

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**Vallecitos Water District**  
**Schedule of Operating Expenses – Wastewater Division, continued**  
**For the Years Ended June 30, 2007 and 2006**

	<u>2007</u>	<u>2006</u>
Meadowlark Plant:		
Labor	\$ 300,450	\$ 323,948
Materials and supplies	806,822	795,024
Outside repair	61,106	89,112
Power	250,314	196,728
Telephone	2,852	1,939
Total Meadowlark Plant	<u>1,421,544</u>	<u>1,406,751</u>
Mahr Reservoir:		
Labor	18,732	16,073
Materials and supplies	10,984	11,778
Outside repairs	1,975	9,501
Total Mahr Reservoir	<u>31,691</u>	<u>37,352</u>
Customer Accounts:		
Labor	84,676	79,293
Materials and supplies	25,865	21,689
Uncollectible accounts	22,932	15,465
Total Customer Accounts	<u>133,473</u>	<u>116,447</u>
Equipment and Vehicles:		
Labor, fuel and repairs	42,306	28,963
Allocated from water division	101,358	96,833
Total Equipment and Vehicles	<u>143,664</u>	<u>125,796</u>
Buildings and Grounds:		
Allocated from water division	<u>162,030</u>	<u>129,838</u>
Engineering:		
Allocated from water division	<u>294,208</u>	<u>243,069</u>
Safety:		
Labor	29,808	39,893
Allocated from water division	33,775	21,714
Total Safety	<u>\$ 63,583</u>	<u>\$ 61,607</u>

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**Vallecitos Water District**  
**Schedule of Operating Expenses – Wastewater Division, continued**  
**For the Years Ended June 30, 2007 and 2006**

	<u>2007</u>	<u>2006</u>
Information Technology		
Allocated from water division	\$ 41,498	\$ -
General and Administration:		
Salaries	119,317	127,353
Other taxes/benefits	3,357	2,598
Social security	142,381	128,207
Group insurance	181,832	138,323
Public employees' retirement	251,842	178,820
Workers' compensation insurance	25,005	30,505
Travel	737	759
Dues and subscriptions	2,629	2,283
Meetings and seminars	4,979	10,618
Outside services	169	163
Miscellaneous	14,240	15,806
Transfer from water division	2,430,888	2,448,386
Administrative credits transferred	(213,987)	(146,805)
Total General and Administration	<u>2,963,389</u>	<u>2,937,016</u>
Total Wastewater Division Expenses	<u>\$ 9,195,871</u>	<u>\$ 8,839,452</u>

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# **Report on Internal Controls and Compliance**





Charles Z. Fedak, CPA, MBA  
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# Charles Z. Fedak & Company

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**Independent Auditor's Report on Internal Control Over Financial Reporting  
And on Compliance and Other Matters Based on an Audit of Financial Statements  
Performed in Accordance with *Government Auditing Standards***

Board of Directors  
Vallecitos Water District  
San Marcos, California

We have audited the basic financial statements of the Vallecitos Water District (District) as of and for the year ended June 30, 2007 and 2006, and have issued our report thereon dated October 18, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

***Internal Control Over Financial Reporting***

In planning and performing our audit, we considered the District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the District's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the District's financial statements that is more than inconsequential will not be prevented or detected by the District's internal control. A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the District's internal control. Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

***Compliance and Other Matters***

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Directors and management and is not intended to be and should not be used by anyone other than these specified parties.

October 18, 2007  
Cypress, California

*Charles Z. Fedak & Company, CPAs  
An Accountancy Corporation*