

CITRUS HEIGHTS WATER DISTRICT

BASIC FINANCIAL STATEMENTS

DECEMBER 31, 2004

CITRUS HEIGHTS WATER DISTRICT

TABLE OF CONTENTS

	<u>Page</u>
Independent Auditor’s Report	1
Management’s Discussion and Analysis	2
Basic Financial Statements:	
Statement of Net Assets	8
Statement of Revenues, Expenses, and Change in Net Assets	10
Statement of Cash Flows.....	11
Notes to Basic Financial Statements	13
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 <i>Government Auditing Standards</i>	25

MOSS, LEVY & HARTZHEIM

Certified Public Accountants

4740 NORTHGATE BLVD., SUITE 160
SACRAMENTO, CALIFORNIA 95834

TELEPHONE (916) 925-5141
FAX (916) 925-7632

ROBERT M. MOSS, C.P.A.*
RONALD A. LEVY, C.P.A.*
CRAIG A. HARTZHEIM, C.P.A.*
BRETT I. MILLER, C.P.A.

PAUL NIEDERMULLER, C.P.A.
HADLEY HUI, C.P.A.
KARAN C. POHL, C.P.A.

*DENOTES PROFESSIONAL CORPORATION

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Citrus Heights Water District
Citrus Heights, California

We have audited the accompanying basic financial statements of Citrus Heights Water District (District) as of and for the year ended December 31, 2004, 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall 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 financial position of the Citrus Heights Water District as of December 31, 2004, and the respective changes in financial position and cash flows, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 2 through 8 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 principally of inquiries of management regarding the methods of measurement and presentation of this information, but we did not audit this information and we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 21, 2005 on our consideration of the Citrus Heights Water District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and 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 not to provide an opinion on the internal control over financial reporting or on compliance. This 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.

MOSS, LEVY & HARTZHEIM, C.P.A.s

January 21, 2005

CITRUS HEIGHTS WATER DISTRICT

2004 FINANCIAL AUDIT

MANAGEMENT'S DISCUSSION AND ANALYSIS

The management of the Citrus Heights Water District (District) presents this Management Discussion and Analysis to achieve two goals:

1. To comply with the requirements of Governmental Accounting Standards Board Statement 34 (GASB 34) that are designed to provide more and easier-to-understand information about the finances of local government agencies such as the District; and
2. To provide readers with narrative information that may help in understanding and interpreting the information presented in the District's financial statements for the year ended December 31, 2004 (CY2004).

Questions or comments regarding this Management's Discussion and Analysis may be directed to the District Treasurer via the following methods:

Mailing address: Citrus Heights Water District, P.O. Box 286, Citrus Heights, CA, 95611
Telephone: (916) 725-6873
Facsimile: (916) 725-0345
E-mail: dkane@chwd.org

Financial Highlights

The following items are, in the opinion of District management, among the most significant in assessing the District's overall financial activities during 2004 and its financial position at the close of CY2004:

- ❖ The District's assets exceeded its liabilities at the end of CY2004 by \$30,468,916. Roughly three-quarters of the District's net assets, \$24,772,158, are composed of the capital assets of the District – water transmission and distribution system, land, buildings, and equipment belonging to the District. Unrestricted net assets totaled \$4,800,242. Of this unrestricted amount, the District has designated \$800,000 for rate stabilization and/or catastrophic losses, and also designated \$588,195 for current District operations, leaving \$3,412,047 for future operations and projects.
- ❖ The District's revenues for CY2004 were \$6,884,799. The great majority of revenues, \$6,499,350, came from water sales to customers. The District adopted a 10.0 percent increase in water rates that went into effect at the beginning of 2004. The second-largest source of revenue for 2004 was \$209,796 in capacity fees. Capacity fees are collected on each new connection to the District's water distribution system to reflect the cost already paid by existing users to provide capacity in the water system to serve additional users, a method of calculating fees known as the "system buy-in" method.
- ❖ The District's total net long-term debt at the end of CY2004, including the 2003 Certificates of Participation, the 2000 Certificates of Participation, leases of fleet equipment and information technology systems and compensated absences, less the current portion of long-term debt, is \$10,414,958.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of two parts: (1) management's discussion and analysis; and (2) the basic financial statements, including the notes to basic financial statements.

The financial statements provide both long-term and short-term information about the District's overall financial status. The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data.

The District's financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units on an accrual basis. Under this basis, revenues are recognized in the period in which they are earned, expenses are recognized in the period in which they are incurred, and depreciation of assets is recognized in the Statement of Revenues, Expenses and Change in Net Assets. All assets and liabilities associated with the operation of the District are included in the Statement of Net Assets.

The Statement of Net Assets presents the financial position of the District on a full accrual historical cost basis and provides information about the nature and amount of resources and obligations at year-end.

Statement of Net Assets

As of December 31, 2004, the total net assets of the District were \$30,468,916. The following table summarizes assets, liabilities and net assets at December 31, 2004:

	<u>2004</u>	<u>2003</u>
Current assets	\$ 6,341,360	\$ 2,998,221
Restricted cash and cash equivalents	863,595	4,093,271
Capital assets, net	35,263,864	28,790,691
Other assets	<u>250,350</u>	<u>5,303,383</u>
Total assets	<u>42,719,169</u>	<u>41,185,566</u>
Current liabilities	1,835,295	1,468,493
Long-term liabilities	<u>10,414,958</u>	<u>10,807,056</u>
Total liabilities	<u>12,250,253</u>	<u>12,275,549</u>
Net Assets		
Invested in capital assets, net of related debt	24,772,158	25,119,216
Restricted	896,516	1,530,818
Unrestricted	<u>4,800,242</u>	<u>2,259,983</u>
Total net assets	<u>\$ 30,468,916</u>	<u>\$ 28,910,017</u>

The District's net assets reflect restrictions imposed as a condition of its Certificates of Participation debt. Funds that the District has collected through Capacity Fees are restricted to use for evaluating and constructing capital facilities to benefit District customers. The remaining net assets are unrestricted.

Change in Net Assets

The following table summarizes the change in net assets for the year ended December 31, 2004:

	<u>2004</u>	<u>2003</u>
Operating revenues	<u>\$ 6,884,799</u>	<u>\$ 6,532,210</u>
Operating expenses:		
Water purchases	1,472,399	1,353,408
Pumping and well maintenance	131,148	66,801
Transmission and distribution	1,506,929	1,614,221
Customer service, administrative and general	1,354,424	1,106,021
Depreciation and amortization	<u>1,650,438</u>	<u>1,283,492</u>
Total operating expenses	<u>6,115,338</u>	<u>5,423,943</u>
Operating income	769,461	1,108,267
Net nonoperating revenues (expenses)	<u>(438,833)</u>	<u>(244,673)</u>
Net Income Before Capital Contributions	330,628	863,594
Capital Contributions		
Donated Assets	<u>1,286,034</u>	<u>297,542</u>
Change in Net Assets	<u>\$ 1,616,662</u>	<u>\$ 1,161,136</u>

Total net assets increased approximately \$1.62 million or 5.6 percent from the prior year. The receipt of \$1,286,034 in donated assets from private developer additions to the District's water distribution system accounted for about 75 percent of the increase in net assets.

Total operating revenues increased \$0.35 million or 5.3 percent from the prior year, primarily as a result of an increase in water charges. Operating expenses increased approximately \$0.69 million or 12.7 percent from the prior year, resulting mostly from the increased costs of water purchases and the increased costs of operating and maintaining new technology systems designed to help increase the efficiency and effectiveness of District services.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

As of December 31, 2004, the District's investment in capital assets was \$35.3 million, including: water transmission and distribution system (underground pipelines, water services, water meters, fire hydrants, and other components); water production facilities (groundwater wells); land; buildings, and mobile and fixed equipment.

Significant additions to the District's capital assets include the installation of over 1,500 new water meters throughout the District's system as part of the ongoing Water Meter Retrofit Program. The project to install over 2,000 lineal feet of 24-inch water transmission main to serve the Stock Ranch area of Citrus Heights was accepted as complete in early 2004. A number of large private development projects resulted in the addition of about \$1.29 million in donated capital assets.

The District completed the first and biggest phase of a major information technology investment with the acquisition and installation of new computer hardware and software for managing the District's customer information and billing, financial accounting, engineering, mapping, maintenance scheduling, and other District operations and services. Future phases to build upon the technology systems now in place are planned, but not yet scheduled.

Debt Administration

The District issued no new debt in 2004. The District's total Certificates of Participation (COP) debt from its issuances in 2000 and 2003 now stands at approximately \$10.0 million.

The District also had short- and long-term lease obligations totaling about \$0.73 million as of December 31, 2004. Most of this amount is for a five-year lease for technology improvements (computer hardware and software and related equipment) that was initiated in 2002. About \$37,900 remains on a five-year lease for two major field equipment items that was also initiated in 2002.

Compensated absences, composed of leave hours earned by employees that are payable upon termination or retirement, are valued at \$266,779.

The current portion of long-term debt is \$593,877.

Additional information on debt activity can be found in Note 5, Long-Term Debt, of the audited basic financial statements.

ECONOMIC FACTORS AND FUTURE BUDGET CONSIDERATIONS

The cost of District operations is expected to continue to rise in 2005 due to a number of factors, including an 8 percent increase in the cost of water purchased from the District's treated water wholesaler, the San Juan Water District. Major increases are also expected in the cost of various forms of insurance, especially worker's compensation insurance and employee health insurance for employees. Due to weak performance of investments by the California Public Employee Retirement System (CalPERS) earlier this decade, the District's CalPERS contribution cost for employees has risen by more than \$150,000 annually since 2002, an increase of 160 percent. As the District continues to move in the direction of becoming a fully-metered water system, its costs for reading water meters, billing customers based on metered consumption, and servicing and repairing water meters, will also continue to rise. A 2005 Operating Budget Summary is included at the conclusion of this Management's Discussion and Analysis to provide an overview of the District's operating budget.

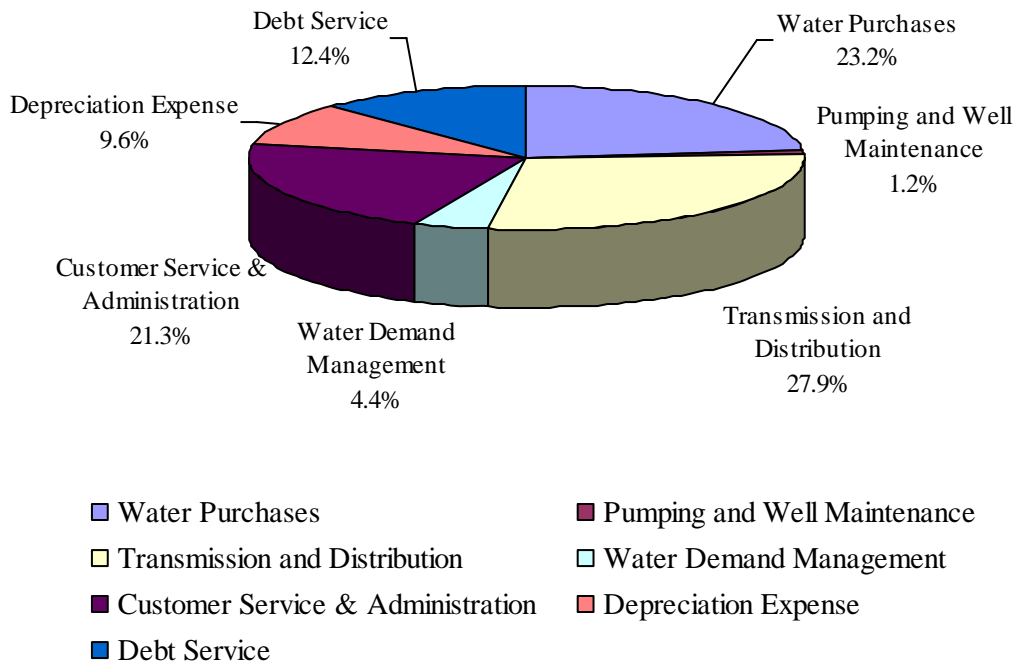
Along with rising operating costs, the District will continue to incur significant costs for capital improvements. Most significant among these is the cost of retrofitting all existing customer water services with water meters. The District has made great progress on water meter installations over the past few years, and now has meters installed on about 15,400 of its water services, almost 80 percent of the District's total of 19,200 services. However, about 3,900 meters remain to be installed, with 1,850 planned for installation in 2005. The District also plans to install two new groundwater wells over the next two years at a cost of about \$1 million each. A California Department of Water Resources Proposition 13 Grant is expected to pay approximately 50 percent of the cost of these two wells. Paying for these and other necessary capital improvements has required the District to issue long-term debt in the form of Certificates of Participation. The District's debt service cost, which was \$0 in 2000, now stands at almost \$832,000 for 2005. A 2005 Capital Improvement Budget Summary is included at the conclusion of this Management's Discussion and Analysis to provide an overview of the District's capital improvement budget.

In order to keep pace with these rising costs, the District's Board of Directors adopted a water rate increase of 8 percent for 2005, following a rate increase of 10 percent for 2004. Even with these water rate increases, the District's water rates are still about 17 percent below the average water rate in the Sacramento region. The District's Long-Range Financial Planning Model, which was updated in 2004, forecasts a need for annual water rate increases in the range of 3 to 10 percent annually through the Year 2010. These increases will be needed to meet the anticipated operating and capital improvement costs of the District while maintaining financial reserves to comply with debt covenants and to provide funds for emergencies or catastrophic losses.

2005 Operating Budget Summary

<u>Expense Category</u>	<u>2003 Actual</u>	<u>2004 Adopted</u>	<u>2005 Proposed</u>	<u>% Change 2005 vs. 2004</u>
Water Purchases	\$ 1,376,619	\$ 1,554,350	\$ 1,610,291	3.5%
Pumping and Well Maintenance	67,231	55,000	77,500	40.9%
Transmission and Distribution	1,715,809	1,689,855	1,867,653	10.5%
Water Demand Management	230,956	272,784	294,864	8.0%
Customer Service & Administration	942,425	1,195,555	1,421,452	18.8%
Depreciation Expense	0	637,123	641,726	0.7%
Debt Service	633,586	817,300	831,708	1.7%
Total	<u>\$ 4,966,626</u>	<u>\$ 6,221,967</u>	<u>\$ 6,745,194</u>	<u>8.4%</u>

CHWD 2005 Operating Budget By Category

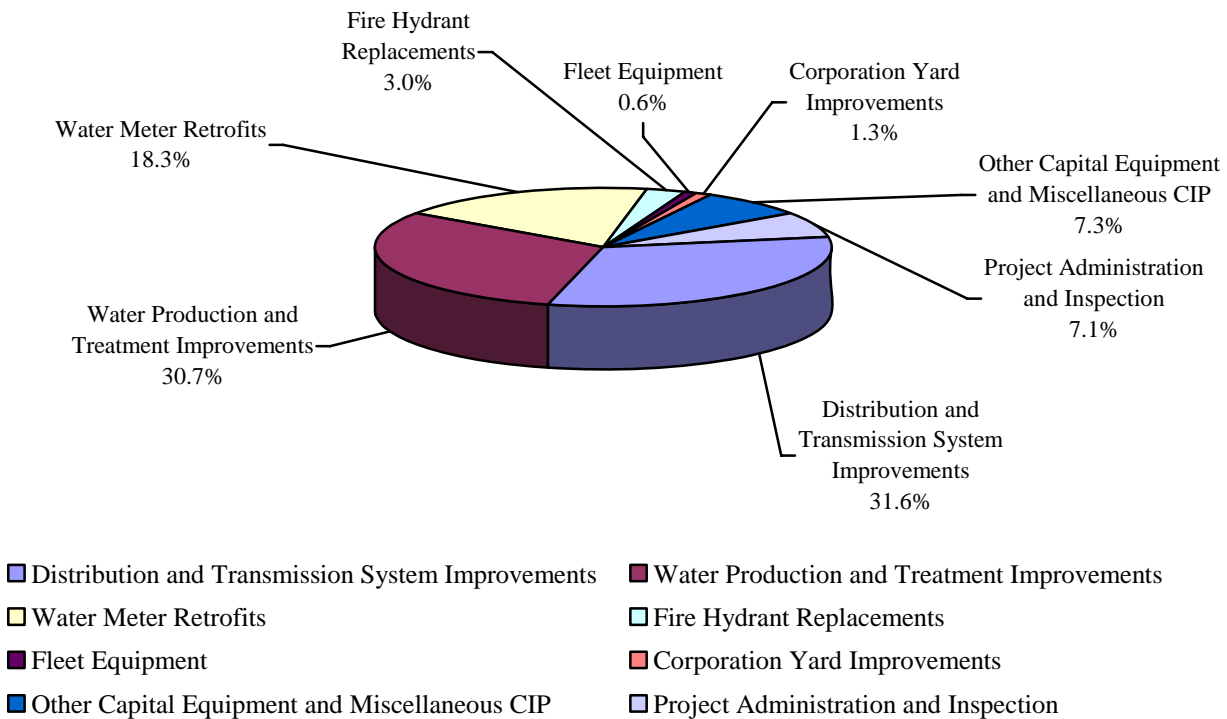


2005 Capital Improvement Budget Summary

<u>Capital Improvement Expense Categories*</u>	<u>2005 Proposed</u>
Distribution and Transmission System Improvements	\$ 1,003,250
Water Production and Treatment Improvements	975,000
Water Meter Retrofits	581,650
Fire Hydrant Replacements	96,500
Fleet Equipment	18,930
Corporation Yard Improvements	40,000
Other Capital Equipment and Miscellaneous CIP	232,437
Project Administration and Inspection	224,453
Total	<u>\$ 3,172,220</u>

*Expenses shown do not include District force account labor included in Operating Budget

CHWD 2005 Capital Improvement Budget By Category



CITRUS HEIGHTS WATER DISTRICT

Statement of Net Assets

December 31, 2004

ASSETS

Current Assets:

Cash and investments	\$ 4,440,331
Investments - trading securities	435,875
Accounts receivable - net	331,086
Interest receivable	23,449
Inventory	658,541
Prepaid expenses	<u>452,078</u>

Total Current Assets 6,341,360

Restricted Assets:

Cash and investments	<u>863,595</u>
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Total Restricted Assets 863,595

Capital Assets:

Nondepreciable:

Land	171,884
Right of ways	26,080
Construction in progress	7,789

Depreciable:

Capacity entitlements	5,615,262
Improvements	55,847
Pipelines and infrastructure	28,488,483
Office equipment	1,457,459
Machinery and equipment	970,176
Buildings	1,083,462
Well improvements	1,104,171
Donated pipelines	12,376,469
Accumulated depreciation	<u>(16,093,218)</u>

Net Capital Assets 35,263,864

Other Assets:

Issuance costs, net of accumulated amortization	<u>250,350</u>
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Total Other Assets 250,350

Total Assets \$ 42,719,169

The accompanying notes are an integral part of these financial statements.

CITRUS HEIGHTS WATER DISTRICT

Statement of Net Assets (Continued)

December 31, 2004

LIABILITIES

Current Liabilities:

Accrued interest payable	\$ 55,792
Accounts payable	51,460
Deferred revenue	1,094,312
Deposits payable	39,854
Current portion of long-term debt	<u>593,877</u>

Total Current Liabilities 1,835,295

Long-term Debt:

Capital leases payable	730,301
Certificates of participation payable	10,011,755
Compensated absences	266,779
Less: current portion of long-term debt	<u>(593,877)</u>

Net Long-Term Debt 10,414,958

Total Liabilities 12,250,253

NET ASSETS

Net Assets:

Invested in capital assets, net of related debt	24,772,158
Restricted for:	
Connection fees	88,713
Debt service	807,803
Unrestricted	<u>4,800,242</u>

Total Net Assets \$ 30,468,916

The accompanying notes are an integral part of these financial statements.

CITRUS HEIGHTS WATER DISTRICT

Statement of Revenues, Expenses, and Change in Net Assets For the Year Ended December 31, 2004

Operating Revenues:	
Water sales - annual	\$ 5,102,718
Water sales - apartments, trailers, cabins, and meters	1,396,632
Penalties and bank charges	89,944
Service charges and repairs	26,911
Tap fees (water services installation)	44,075
Water wheeling	10,194
Inclusion fees	4,529
Capacity fees	209,796
	<hr/>
Total Operating Revenues	6,884,799
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Operating Expenses:	
Water purchases	1,472,399
Pumping and well maintenance	131,148
Transmission and distribution	1,506,929
Customer service, administrative, and general	1,354,424
Amortization	12,141
Depreciation	1,638,297
	<hr/>
Total Operating Expenses	6,115,338
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Operating Income	769,461
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Nonoperating Revenues (Expenses):	
Investment earnings	99,375
Gain (loss) on disposal of capital assets	(7,599)
Other income	53,071
Interest expense	(583,680)
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Total Nonoperating Revenues (Expenses)	(438,833)
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Net Income before Capital Contributions	330,628
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Capital Contributions:	
Donated capital assets	1,286,034
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Change in Net Assets	1,616,662
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Net Assets, January 1, 2004	28,910,017
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Prior year adjustment	(57,763)
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Net Assets, January 1, 2004, restated	28,852,254
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Net Assets, December 31, 2004	\$ 30,468,916
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The accompanying notes are an integral part of these financial statements.

CITRUS HEIGHTS WATER DISTRICT

Statement of Cash Flows For the Year Ended December 31, 2004

Cash Flows from Operating Activities:	
Cash received from customers	\$ 8,016,253
Cash payments to employees	(1,840,321)
Cash payments to suppliers for goods and services	<u>(3,186,893)</u>
Net Cash Provided (Used) by Operating Activities	<u>2,989,039</u>
Cash Flows from Noncapital Financing Activities:	
Other income	<u>53,071</u>
Net Cash Provided (Used) by Noncapital Financing	<u>53,071</u>
Cash Flows from Capital and Related Financing Activities:	
Interest paid on long-term debt	(583,306)
Retirement of long-term debt	(631,587)
Purchase of capital assets	<u>(2,199,964)</u>
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>(3,414,857)</u>
Cash Flows from Investing Activities:	
Net sale (purchase) of investments	(30,399)
Investment earnings received	<u>93,146</u>
Net Cash Provided (Used) by Investing Activities	<u>62,747</u>
Net Change in Cash and Cash Equivalents	(310,000)
Cash and Cash Equivalents, January 1, 2004	<u>5,613,926</u>
Cash and Cash Equivalents, December 31, 2004	<u>\$ 5,303,926</u>
Reconciliation of Cash and Cash Equivalents to Statement of Net Assets:	
Cash and investments	\$ 4,440,331
Restricted cash and investments	<u>863,595</u>
Total Cash and Cash Equivalents	<u>\$ 5,303,926</u>

The accompanying notes are an integral part of these financial statements.

CITRUS HEIGHTS WATER DISTRICT

Statement of Cash Flows (Continued) For the Year Ended December 31, 2004

Reconciliation of Operating Income to Net	
Cash Provided by Operating Activities:	
Operating income	\$ 769,461
Adjustments to reconcile operating income to	
net cash provided by operating activities:	
Depreciation	1,638,297
Amortization	12,141
Changes in assets and liabilities:	
Decrease (increase) in accounts receivable	29,434
Decrease (increase) in inventory	26,561
Decrease (increase) in prepaid expenses	(37,354)
Increase (decrease) in accounts payable	(568,298)
Increase (decrease) in deferred revenue	1,062,166
Increase (decrease) in deposits payable	39,854
Increase (decrease) in compensated absences	<u>16,777</u>
Net Cash Provided by Operating Activities	<u><u>\$ 2,989,039</u></u>

The accompanying notes are an integral part of these financial statements.

CITRUS HEIGHTS WATER DISTRICT

Notes to Basic Financial Statements December 31, 2004

Note 1: Summary of Significant Accounting Policies

A. **Reporting Entity**

The Citrus Heights Water District (District) is an irrigation district formed on October 25, 1920, under Division 11 of the Act of Legislature of the State of California titled, "Act to Provide for Organization and Government of Irrigation Districts." The District constructs and maintains waterworks and supplies domestic and irrigation water in an area of approximately 7,900 acres to 19,200 connections in Sacramento and Placer counties with an estimated population of 66,000.

The District's basic financial statements include the operations of all organizations for which the District Board of Directors exercises oversight responsibility. Oversight responsibility is demonstrated by financial interdependency, selection of governing authority, designation of management, ability to significantly influence operations, and accountability for fiscal matters.

The Board of Directors serves in a separate session as the governing body of the Citrus Heights Water District Financing Corporation (Corporation), although the Corporation is a legal entity apart from the District.

The Corporation is included as a blended component unit in the accompanying financial statements. The financial activities of the foregoing entities have been aggregated and merged (termed "blending") with those of the District in the accompanying financial statements, as they meet the criteria for inclusion as set forth in the Governmental Accounting Standards Board (GASB) Statement No. 14 as amended by GASB Statement No. 39.

The Corporation was established by the Board of Directors for the purpose of providing assistance to the District in financing public improvements.

B. **Basis of Presentation**

Fund Financial Statements: The fund financial statements provide information about the District's funds. Separate statements for each proprietary fund are presented. The emphasis of fund financial statements is on major individual funds, each of which is displayed in a separate column.

C. **Basis of Accounting**

The government-wide financial statements are reported using the *economic resources measurement focus* and the full *accrual basis* of accounting. Revenues are recorded when *earned* and expenses are recorded at the time liabilities are *incurred*, regardless of when the related cash flows take place.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in the financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The government has elected not to follow subsequent private-sector guidance.

CITRUS HEIGHTS WATER DISTRICT

Notes to Basic Financial Statements December 31, 2004

Note 1: Summary of Significant Accounting Policies (Continued)

D. Budget and Budgeting

Budget integration is employed as a management control device. Budgets are formally adopted by the Board of Directors and take effect the following January 1. The budgets are used as a management tool and are not a legal requirement.

E. Restricted Assets

Restricted assets are financial resources generated for a specific purpose such as construction of improvements and financing of debt obligations. These assets are for the benefit of a distinct group and as such are legally or contractually restricted.

F. Inventory

Inventories of supplies and expendable equipment are stated at the lower of cost or market. Cost is determined on a first-in, first-out basis.

G. Capital Assets

Purchased capital assets are stated at historical cost or estimated historical cost when original cost is not available. Donated capital assets are recorded at their estimated fair value at the date of donation. The District's policy is to capitalize all capital assets with costs exceeding a minimum threshold of \$5,000. Depreciation is recorded using the straight-line method over the estimated useful lives of the capital assets which range from three to forty years for the plant and pipelines, and three to five years for other equipment.

H. Cash Equivalents

For purposes of the statement of cash flows, the District considers all highly liquid investment instruments purchased with a maturity of three months or less to be cash equivalents.

I. Compensated Absences

All earned annual leave and administrative leave hours, holiday, and compensatory time-off (CTO) hours are payable upon termination or retirement and are accrued as compensated absences. Upon death while employed by the District or retirement from the District, employees are paid one-third of their accumulated sick leave time. The compensated absences liability is calculated in accordance with GASB Statement No. 16. As of December 31, 2004, the total estimated liability for all compensated absences is \$266,779.

J. Deferred Charges

Costs and underwriters' discounts related to long-term debt issuance costs are deferred and amortized over the term of the bond redemption.

CITRUS HEIGHTS WATER DISTRICT

**Notes to Basic Financial Statements
December 31, 2004**

Note 1: Summary of Significant Accounting Policies (Continued)

K. Use of Estimates

The preparation of basic financial statements in conformity with accounting principles generally accepted in the United States of America, as prescribed by the GASB and the American Institute of Certified Public Accountants (AICPA), requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

L. Net Assets

GASB Statement No. 34 requires that the difference between assets and liabilities be reported as net assets. Net assets are classified as either invested in capital assets, net of related debt, restricted, or unrestricted.

Net assets that are invested in capital assets, net of related debt, consist of capital assets, net of accumulated depreciation, and reduced by the outstanding principal of related debt. Restricted net assets are those net assets that have external constraints placed on them by creditors, grantors, contributors, laws, or regulations of other governments, or through constitutional provisions or enabling legislation. Unrestricted net assets consist of net assets that do not meet the definition of invested in capital assets, net of related debt, or restricted net assets.

Note 2: Cash and Investments

The cash and investments shown on the statement of net assets are as follows:

Cash and investments	\$ 4,440,331
Investments - trading securities	435,875
Restricted cash and investments	<u>863,595</u>
Total	<u>\$ 5,739,801</u>

Deposits

All deposits are entirely insured or collateralized. The California Government Code requires California's banks and savings and loan associations to secure a district's deposits by pledging government securities as collateral. The fair value of pledged securities must equal at least 110% of a district's deposits. California's law also allows financial institutions to secure a district's deposits by pledging first trust deed mortgage notes having a value of 150% of a district's total deposits.

The District may waive collateral requirements for deposits, which are fully insured up to \$100,000 by the Federal Depository Insurance Corporation (FDIC).

CITRUS HEIGHTS WATER DISTRICT

**Notes to Basic Financial Statements
December 31, 2004**

Note 2: Cash and Investments (Continued)

Credit Risk, Carrying Amount, and Fair Value

Cash is classified in three categories of credit risk as follows:

- Category 1 - Insured or collateralized with securities held by the District or by its agent in the District's name;
- Category 2 - Collateralized with securities held by the pledging financial institution's trust department or agent in the District's name; and
- Category 3 - Uncollateralized.

At December 31, 2004, the carrying amount of the District's deposits was \$496,079. The bank's balance was \$996,980. This difference is due to the normal deposits in transit and outstanding checks. The District's cash deposits by category as of December 31, 2004, are as follows:

	Category			Bank Balance	Carrying Amount
	1	2	3		
Bank Accounts	\$ 100,000	\$ 896,980	\$ -	\$ 996,980	\$ 496,079
Total	\$ 100,000	\$ 896,980	\$ -	\$ 996,980	\$ 496,079

The District also maintains a \$375 imprest cash balance.

Investments are also classified in three categories of credit risk as follows:

- Category 1 - Insured or registered, with securities held by the District or its agent in the District 's name;
- Category 2 - Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the District 's name; and
- Category 3 - Uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent, but not in the District's name.

Investments in pools managed by other governments, investment agreements, and mutual funds are not required to be categorized.

Statutes authorize the District to invest in obligations of the U.S. Treasury, agencies, and instrumentalities within the State, State Treasury, bankers' acceptances, and commercial paper of the highest ranking provided by Moody's Investors Service, Inc., or Standard and Poor's Corporation, repurchase or reverse repurchase agreements, and the State Treasurer's Investment Pool.

CITRUS HEIGHTS WATER DISTRICT

**Notes to Basic Financial Statements
December 31, 2004**

Note 2: Cash and Investments (Continued)

Credit Risk, Carrying Amount, and Fair Value (Continued)

The District's investment policy allows the District's Treasurer to invest in the following investments: United States Treasury bills; Treasury notes or bonds maturing within one (1) year; insured or fully collateralized certificates of deposit of banks and savings and loan associations maturing within one (1) year; repurchase agreements collateralized by United States Treasury Securities; the State Treasurer's investment pool; and money market mutual funds whose portfolios consist entirely of United States government securities.

The composition of investments at December 31, 2004, is as follows:

	Category			Carrying Amount/ Fair Value
	1	2	3	
Money Market	\$ N/A	\$ N/A	\$ N/A	\$ 863,595
U.S. Government Securities	435,875			435,875
Local Agency Investment Fund (LAIF)	N/A	N/A	N/A	3,943,877
Total investments	\$ 435,875	\$ -	\$ -	\$ 5,243,347

Implementation of GASB Statement No. 31

Investments are accounted for in accordance with the provisions of GASB Statement No. 31, which requires governmental entities to report certain investments at fair value in the statement of net assets and recognize the corresponding change in fair value of investments in the year in which the change occurred. The District reports its investments at fair value based on quoted market information obtained from fiscal agents or other sources.

Note 3: Restricted Cash and Investments

Funds Held by Fiscal Agents

The District had \$863,595 in cash and investments as of December 31, 2004, held by fiscal agents pledged for the payment or security of certain certificates of participation. The California Government Code provides that these monies, in the absence of specific statutory provisions governing the issuance of bonds, certificates, or leases, may be invested in accordance with the ordinance, resolutions, or indentures specifying the types of investments its fiscal agents may make.

CITRUS HEIGHTS WATER DISTRICT

**Notes to Basic Financial Statements
December 31, 2004**

Note 4: Capital Assets

Capital assets at December 31, 2004, consisted of the following:

	Balance <u>January 1, 2004</u>	<u>Additions</u>	<u>Deletions</u>	<u>Transfers</u>	Balance <u>December 31, 2004</u>
Nondepreciable capital assets:					
Land	\$ 101,184	\$ 70,700	\$ -	\$ -	\$ 171,884
Right of ways	26,080				26,080
Construction in progress	<u>144,402</u>	<u>40,270</u>		<u>(176,883)</u>	<u>7,789</u>
Total nondepreciable capital assets	<u>271,666</u>	<u>110,970</u>		<u>(176,883)</u>	<u>205,753</u>
Depreciable capital assets:					
Capacity entitlements	5,615,262				5,615,262
Improvements	55,847				55,847
Pipelines and infrastructure	26,842,070	1,687,055	(40,642)		28,488,483
Office equipment	933,479	366,567	(2,126)	159,539	1,457,459
Machinery and equipment	966,287	17,417	(13,528)		970,176
Buildings	1,083,462				1,083,462
Well improvements	1,068,872	17,955		17,344	1,104,171
Donated pipelines	<u>11,090,435</u>	<u>1,286,034</u>			<u>12,376,469</u>
Subtotals	47,655,714	3,375,028	(56,296)	176,883	51,151,329
Less accumulated depreciation	<u>(14,503,618)</u>	<u>(1,638,297)</u>	<u>48,697</u>		<u>(16,093,218)</u>
Net depreciable capital assets	<u>33,152,096</u>	<u>1,736,731</u>	<u>(7,599)</u>	<u>176,883</u>	<u>35,058,111</u>
Net capital assets	<u>\$ 33,423,762</u>	<u>\$ 1,847,701</u>	<u>\$ (7,599)</u>	<u>\$ -</u>	<u>\$ 35,263,864</u>

From 1993 through 1998, the District participated with four other water agencies in a cooperative transmission pipeline project for the construction of additional transmission pipeline facilities. The District's share of these pipeline costs totaled \$5,615,262. The Capacity Entitlements asset represents the capacity rights the District has purchased in the cooperative transmission pipeline project owned by San Juan Water District. The asset will be amortized over the pipeline estimated useful life of forty years.

Note 5: Long-Term Debt

A. Compensated Absences

District employees accumulate earned but unused annual leave benefits which can be converted to cash at termination of employment. Since no means exists to reasonably estimate the amount that might be liquidated with expendable currently available financial resources, if any, they are reported as long-term debt on the Statement of Net Assets. The non-current portion of these vested benefits, at December 31, 2004, is \$266,779.

CITRUS HEIGHTS WATER DISTRICT

Notes to Basic Financial Statements December 31, 2004

Note 5: Long-Term Debt (Continued)

B. Capital Lease Obligation

In 2002, the District entered into a lease/purchase agreement with LaSalle Bank totaling \$1,150,000 to acquire certain equipment. The total capital lease balance at December 31, 2004 is \$694,777. The lease arrangement bears interest at a yield of 3.45% and is payable in monthly installments and matures November 15, 2007. Future minimum lease payments at December 31, 2004, were:

<u>Year Ending December 31</u>	<u>Amount</u>
2005	\$ 250,737
2006	250,737
2007	<u>229,842</u>
Total minimum lease payments	731,316
Less amounts representing interest	<u>(36,539)</u>
Present value of net minimum lease payments	<u>\$ 694,777</u>

In 2002, the District entered into a lease/purchase agreement with WestAmerica Bank totaling \$87,077 to acquire certain equipment. The total capital lease balance at December 31, 2004 is \$694,777. The lease arrangement bears interest at a yield of 4.35% and is payable in annual installments and matures May, 2006. Future minimum lease payments at December 31, 2004, were:

<u>Year Ending December 31</u>	<u>Amount</u>
2005	\$ 18,929
2006	<u>18,929</u>
Total minimum lease payments	37,858
Less amounts representing interest	<u>(2,334)</u>
Present value of net minimum lease payments	<u>\$ 35,524</u>

CITRUS HEIGHTS WATER DISTRICT

Notes to Basic Financial Statements December 31, 2004

Note 5: Long-Term Debt (Continued)

C. Certificates of Participation Payable

The District entered into an agreement in October 2000, concerning the sale and delivery of Certificates of Participation in the aggregate principal amount of \$7,900,000 with interest ranging from 4.00% to 5.25%. These 2000 Certificates of Participation were issued to finance the cost of certain capital improvements to the District's water system. The obligation of the District to make the debt service payments is a special obligation of the District payable solely from net revenues and certain debt reserve accounts. The 2000 Certificates of Participation mature through 2020 as follows:

Year Ending December 31,	Principal	Interest	Total
2005	\$ 300,000	\$ 334,751	\$ 634,751
2006	310,000	322,151	632,151
2007	325,000	308,976	633,976
2008	340,000	294,839	634,839
2009	355,000	279,878	634,878
2010-2014	2,020,000	1,140,818	3,160,818
2015-2019	2,580,000	577,501	3,157,501
2020	600,000	31,500	631,500
	\$ 6,830,000	\$ 3,290,414	\$ 10,120,414

The District entered into an agreement with San Juan Water District in December 2003, concerning the sale and delivery of Certificates of Participation in the aggregate principal amount of \$27,215,000 with interest ranging from 2.00% to 4.25%. The District's portion of the principal amount is \$3,220,000. These 2003 Certificates of Participation were issued to finance the cost of certain capital improvements to the District's water system. The obligation of the District to make the debt service payments is a special obligation of the District payable solely from net revenues and certain debt reserve accounts. The 2003 Certificates of Participation mature through 2033 as follows:

Year Ending December 31,	Principal	Interest	Total
2005	\$ 65,000	\$ 131,956	\$ 196,956
2006	65,000	130,656	195,656
2007	65,000	129,356	194,356
2008	70,000	127,406	197,406
2009	70,000	124,606	194,606
2010-2014	395,000	589,730	984,730
2015-2019	465,000	510,680	975,680
2020-2024	575,000	409,049	984,049
2025-2029	710,000	270,513	980,513
2030-2033	635,000	84,789	719,789
	3,115,000	2,508,741	5,623,741
Plus: Unamortized Premium	66,755		66,755
	\$ 3,181,755	\$ 2,508,741	\$ 5,690,496

CITRUS HEIGHTS WATER DISTRICT

**Notes to Basic Financial Statements
December 31, 2004**

Note 5: Long-Term Debt (Continued)

D. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2004, was as follows:

	January 1, 2004	Additions	Reductions	December 31, 2004	Due Within One Year
	<u>Balance</u>			<u>Balance</u>	<u>One Year</u>
Business-type activities:					
Capital leases payable	\$ 969,546	\$ -	\$ 239,245	\$ 730,301	\$ 228,877
Certificates of Participation payable	10,404,097		392,342	10,011,755	365,000
Compensated absences	<u>250,002</u>	<u>16,777</u>		<u>266,779</u>	
Business-type activity long-term liabilities	<u>\$ 11,623,645</u>	<u>\$ 16,777</u>	<u>\$ 631,587</u>	<u>\$ 11,008,835</u>	<u>\$ 593,877</u>

Note 6: Deferred Charges

The long-term debt issuance costs, and discounts are capitalized and amortized over the terms of the respective debt using the life of the underlying debt.

Note 7: Employees' Retirement Plan

Plan Description

The District's defined benefit pension plan, Public Employees' Retirement System (PERS), provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. PERS is part of the Public Agency portion of the California Public Employees' Retirement System, (CalPERS), an agent multiple-employer plan administered by CalPERS, which acts as a common investment and administrative agent for participating public employers within the State of California. A menu of benefit provisions as well as other requirements are established by State statutes with the Public Employees' Retirement Law. The District selects optional benefit provisions from the benefit menu by contract with CalPERS and adopts those benefits through local ordinance (other local methods). CalPERS issues a separate comprehensive annual financial report. Copies of the CalPERS' annual financial report may be obtained from the CalPERS Executive Office – 400 P Street – Sacramento, CA 95814.

Funding Policy

The District contributes the employee and employer shares for the Miscellaneous Plan. The District is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the CalPERS Board of Administration. The required employer contribution rate for the year 2004 was Citrus Heights Water District's employer contribution rate for 2003/04 was 4.784% and for 2004/05 was 10.663% for miscellaneous employees. The contribution requirements of the plan members are established by the State statute and the employer contribution rate is established and may be amended by CalPERS.

CITRUS HEIGHTS WATER DISTRICT

**Notes to Basic Financial Statements
December 31, 2004**

Note 7: Employees' Retirement Plan (Continued)

Annual Pension Cost

For year 2004, the District's annual pension cost was \$108,198 and was equal to the District's required and actual contributions. The required contribution for year 2004 was determined as part of the June 30, 2001 actuarial valuation using the entry age normal actuarial cost method with the contributions determined as a percent of pay. The actuarial assumptions included (a) 8.5% investment rate of return (net of administrative expenses); (b) projected salary increases that vary by duration of service, and (c) no cost-of-living adjustment. Both (a) and (b) include an inflation component of 3.5%. The actuarial value of the District's assets was determined using a technique that smoothes the effect of short-term volatility in the fair value of investments over a two to five year period depending on the size of investment gains and/or losses. The District's unfunded actuarial accrued liability (UAAL) (or excess assets) is being amortized as a level percentage of projected payroll on a closed basis. The remaining amortization period at June 30, 2003, was 17 years.

Three Year Trend Information for the District Public Employees' Retirement Plan

Year Ending	Annual Pension Cost (APC)	Percentage of APC Contribution	Net Pension Obligation
12/31/02	\$ -	100%	\$ -
12/31/03	\$ -	100%	\$ -
12/31/04	\$108,198	100%	\$ -

Funded Status of Miscellaneous Plan

Retirement Program

Valuation Date	Accrued Liability (a)	Actuarial Value of Assets (b)	Unfunded Liability (a)-(b)	Funded Status (b)/(a)	Annual Covered Payroll (c)	Unfunded Actuarial Accrued Liability as a % of Payroll ((a)-(b))/(c)
6/30/01	\$ 4,539,990	\$4,803,246	\$ (263,256)	105.8%	\$ 1,211,312	(21.7%)
6/30/02	\$ 5,017,608	\$ 4,501,010	\$ 516,598	89.7%	\$ 1,310,467	39.4%)
6/30/03	\$ 5,883,559	\$ 4,584,905	\$1,298,654	77.9%	\$ 1,469,558	88.4%

CITRUS HEIGHTS WATER DISTRICT

Notes to Basic Financial Statements December 31, 2004

Note 8: 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. During October 1979, the District determined it was unable to obtain general liability and property insurance at a cost it considered to be economically justifiable. The District participates in the Association of California Water Agencies Joint Powers Insurance Authority (ACWA/JPIA), a public entity risk pool currently operating as a common risk carrier management and insurance program for member agencies. The purpose of ACWA/JPIA is to spread the adverse effect of losses among the members and to purchase excess insurance as a group, thereby reducing its expenses. The District pays an annual premium to the ACWA/JPIA for its general liability, automobile, and property coverage. The formation agreement of the ACWA/JPIA provides that the ACWA/JPIA will be self-sustaining through member premiums and will reinsure through commercial companies for claims in excess of \$500,000 for liability and \$10,000 for property for each insured event.

The District has a self-insured retention (similar to a deductible) of \$10,000 for automobile and general liability and \$1,000 for property.

The District's workers' compensation program is carried through ACWA/JPIA and the District pays annual premiums to the fund.

Below is the most recent condensed financial information for the ACWA/JPIA for the fiscal year ended September 30, 2003:

Total Assets	\$ <u>73,883,784</u>
Total Liabilities	\$ 54,046,940
Retained Earnings	<u>19,836,844</u>
Total Liabilities and Retained Earnings	\$ <u>73,883,784</u>
Total Revenues	\$ 30,583,883
Total Expenses	<u>28,118,670</u>
Net Income	\$ <u>2,465,213</u>

Complete separate audited financial statements for the ACWA/JPIA may be obtained at 5620 Birdcage Street, Suite 200, Citrus Heights, California 95610-7632.

Note 9: Post-Employment Health Care Benefits

In addition to providing pension benefits through PERS, the District provides certain health care benefits for retired employees through written policy approved by the Board of Directors. Benefits cover the participant and his/her dependents, depending on years of services, with a qualifying minimum of twenty (20) years of service. Currently, three retirees and their dependents meet eligibility requirements and participate in the plan.

The District's contributions are financed on a pay-as-you-go basis and are recognized as expenses when paid. During the year ended December 31, 2004 expense of \$4,150 was recognized for post-employment health care.

CITRUS HEIGHTS WATER DISTRICT

**Notes to Basic Financial Statements
December 31, 2004**

Note 10: Commitments and Contingencies

Various claims have been filed against the District. In the opinion of the District's management and legal counsel, the claims will not have a material impact on the basic financial statements.

The District has received state and federal grants for specific purposes that are subject to review and audit by the federal government. Although such audits could result in expenditure disallowances under grant terms, any required reimbursements are not expected to be material.

Note 11: Net Assets

Unrestricted net assets have been designated by the District for the following at December 31, 2004:

Operations	\$ 471,901
Rate Stabilization	<u>800,000</u>
Total Designation	<u>\$ 1,271,901</u>

Note 12: Economic Dependency

During 2004, the District purchased 93.6% of its water supply from San Juan Water District (SJWD). Total purchases for the year ended December 31, 2004 was \$1,472,399. In addition, the District owns water transmission capacity entitlements through the cooperative transmission pipeline project with SJWD.

MOSS, LEVY & HARTZHEIM

Certified Public Accountants

4740 NORTHGATE BLVD., SUITE 160
SACRAMENTO, CALIFORNIA 95834

TELEPHONE (916) 925-5141
FAX (916) 925-7632

ROBERT M. MOSS, C.P.A.*
RONALD A. LEVY, C.P.A.*
CRAIG A. HARTZHEIM, C.P.A.*
BRETT I. MILLER, C.P.A.

HADLEY HUI, C.P.A.
PAUL NIEDERMULLER, C.P.A.
KARAN C. POHL, C.P.A.

*DENOTES PROFESSIONAL CORPORATION

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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*

To the Board of Directors
Citrus Heights Water District
Citrus Heights, California

We have audited the basic financial statements of the Citrus Heights Water District as of and for the year ended December 31, 2004, and have issued our report thereon dated January 21, 2005. 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 Citrus Heights Water District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Citrus Heights Water District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 or other matters that are required to be reported under *Government Auditing Standards*.

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

MOSS, LEVY & HARTZHEIM, C.P.A.s

January 21, 2005