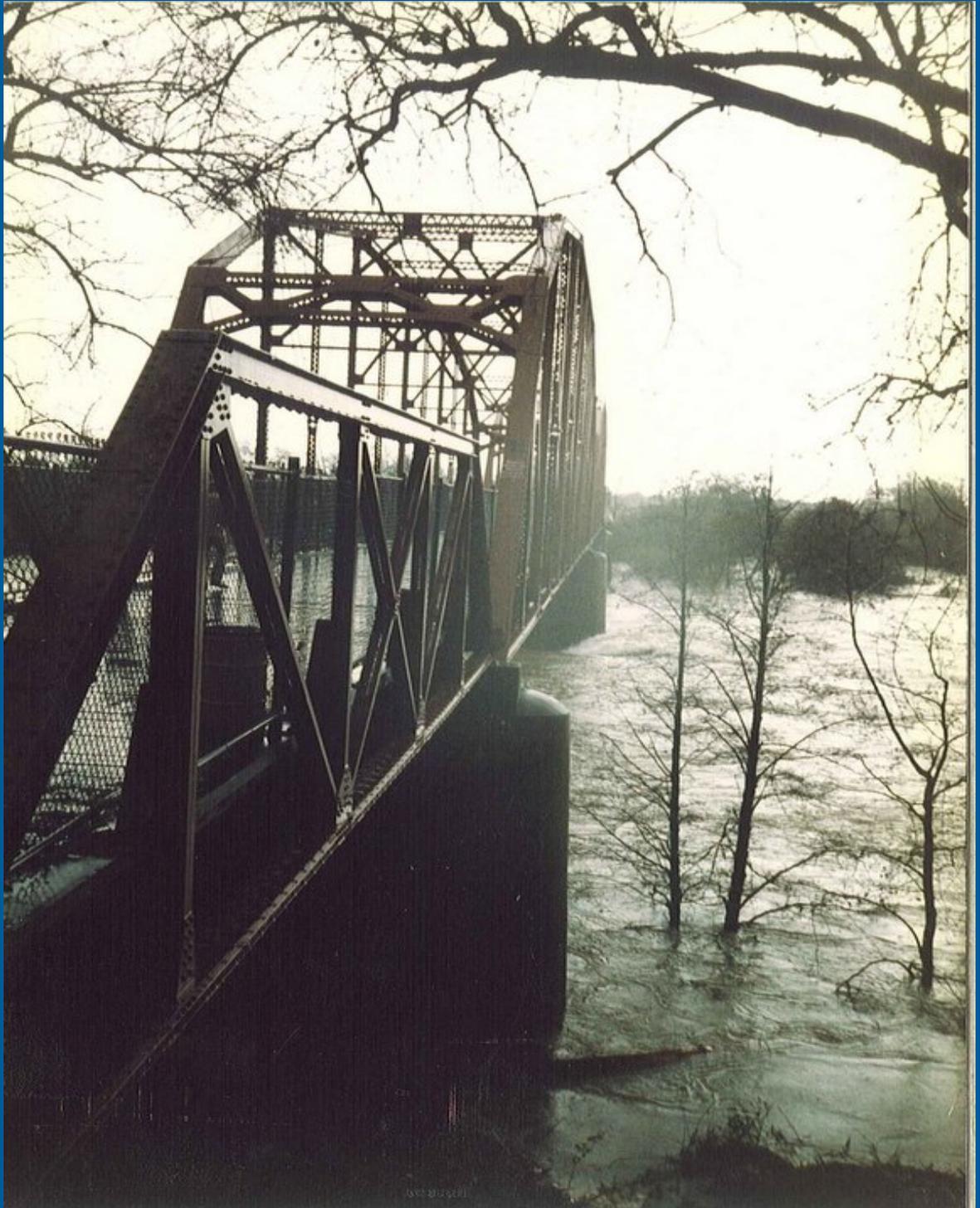
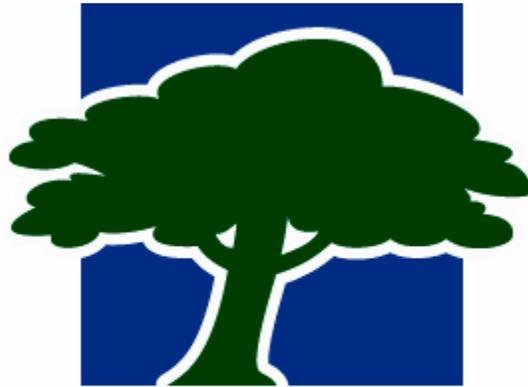


COMPREHENSIVE ANNUAL  
FINANCIAL REPORT  
FOR THE YEAR ENDED DECEMBER 31, 2006

FAIR OAKS WATER DISTRICT — Fair Oaks, California





**FAIR OAKS  
WATER DISTRICT**

*Fair Oaks, California*

**COMPREHENSIVE ANNUAL  
FINANCIAL REPORT**

**YEAR ENDED  
DECEMBER 31, 2006**

*Prepared By  
Finance Department*

**FAIR OAKS WATER DISTRICT**  
**COMPREHENSIVE ANNUAL FINANCIAL REPORT**  
**December 31, 2006**

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## **INTRODUCTORY SECTION**



March 6, 2007

The Board of Directors  
Fair Oaks Water District

The Fair Oaks Water District (“District”) hereby submits the Comprehensive Annual Financial Report (CAFR) for the year ending December 31, 2006. Responsibility for both the accuracy of the presented data and the completeness and fairness of the presentation, including all disclosures, rests with management. To the best of our knowledge and belief, the enclosed data is accurate in all material aspects and is reported in a manner designed to fairly present the financial positions and results of operations of the District. All disclosures necessary to enable the reader to gain an understanding of the District’s financial activities have been included.

The Comprehensive Annual Financial Report is presented in three sections: introductory, financial, and statistical. The introductory section includes the letter of transmittal, the District’s organization chart, and a list of principal officials. The financial section includes the management discussion and analysis which should be read in conjunction with the transmittal letter. The financial statements, schedules, and independent auditor’s report on these financial statements and schedules are included on the financial section of the report. The statistical section includes selected unaudited financial information of the District.

This report includes all funds, agencies, boards, commissions, and authorities that are financially accountable to the District’s Board of Directors. Financial accountability was determined on the basis of budget adoption, imposition of will, funding, and appointment of governing board. Based upon these criteria, the Fair Oaks Water District Financing Corporation (the Financing Corporation) is considered a component unit of the District. The Financing Corporation provides specific financial benefits or imposes specific financial burdens on the District in regards to proceeds from certificates of participation used for capital outlay.

### **District History and Service Description**

Fair Oaks Water District was originally formed as the Fair Oaks Irrigation District in 1917. By 1979, residential development in the community had replaced all significant agricultural land; therefore, the board of directors passed a resolution declaring “irrigation district” no longer described the District’s actual functions and changed the name to Fair Oaks Water District. Even with the name change, the District is legally structured as an irrigation district operating under the California Water Code, Division 11.

The District is a retail water agency supplying water to a population of approximately 40,000 people on approximately 6,000 acres in Fair Oaks and a small portion of Orangevale. The District purchases most of its water from San Juan Water District ("San Juan") as treated water, and delivers it to approximately 14,470 residential and commercial service connections. Additionally, the District maintains seven groundwater wells, 180 miles of pipeline, and a three million gallon water storage facility.

### **Mission Statement**

The District's mission statement is as follows: "Our mission is to provide our community with an adequate and reliable supply of water, exceeding all drinking water standards, at the lowest practicable cost. Our watchword is excellence. We operate in a responsive, professional, environmentally responsible manner, balancing immediate and long-term needs. The District strives to provide leadership in the community, and in regional water resource activities."

### **Economic Condition and Outlook**

Fair Oaks is primarily a residential bedroom community, with some commercial enterprises within its boundaries, located in Sacramento County in Northern California. The District area is almost built out; therefore, the District does not depend upon new growth to maintain revenue. Based on actual results from prior years, the District is forecasting a slow but steady revenue increase of 20 new system connections per year from the demand for semi-custom housing in the Fair Oaks area.

Revenues from residential accounts are based upon flat rate billing with a plan to convert the accounts to metered rates in 2011. During 2002 commercial customers were converted from a flat rate to a metered rate, which decreased the revenues for commercial accounts. To mitigate the forecasted future decline in revenues from account conversions to metered rates, the District has implemented a rate stabilization fund. Given this planning effort, the future financial stability of the District is positive relative to projected revenues.

The District continues the practice of establishing and maintaining reserves and designations to offset expected and unexpected significant expense fluctuations encountered year to year.

The Fair Oaks Water District and its wholesale water supplier continue to encounter changes in operations due to new regulations. The impact of current and future regulations and the resetting cost on water supply operations are an ongoing challenge for District management. The District used the best available data at the time of its budget preparation to forecast the impact of the regulatory environment on operational costs on the 2007 budget as adopted on January 8, 2007.

## **Significant Projects and Future Plans**

### Meters

The Central Valley Project Improvement (CVPIA) was enacted by the Federal Government in 1992 requiring any water purveyor contracted to receive surface water from United States Bureau of Reclamation to implement metering within five years of the date of contract. On September 28, 1999 the Reed Consulting Group presented the District's Metering Implementation Plan at the Board meeting. At the meeting, the District's Board of Directors adopted the proposed plan to have meter installation program complete and functioning by 2011. The current management of the District updated the Metering Implementation Plan (MIP) in 2006. With the updated MIP, the District anticipates installing 1,141 meters a year at a cost of approximately \$2.7 million per year through 2011. The District's total estimated cost for the Meter Implementation Program is approximately \$17.4 million.

During 2006, the District installed 947 meters as part of the Meter Implementation Plan. As of December 31, 2006, the District has installed approximately 8,627 meters and has approximately 5,840 existing service connections that require meters to be installed. To expedite the metering installation, the District intends to use all of its crew to install meters in 2007; while contracting out capital budget water main projects. Mandatory-metered rates for residential customers will go into effect after all residential meters are installed.

### Infrastructure and Water Delivery

The District continues to repair and replace aging infrastructure throughout its system. The District completed Timothy Way, North Winding Way and Watkins Drive water main replacement projects in 2006. In addition, the District completed drilling of the Heather Well and Town Well groundwater projects in 2006. The Town Well and Heather Well building structures are in progress and the District anticipates completing them in 2007. Additional projects scheduled for 2007 include:

- Fair Oaks Blvd. Phase I and II at an estimated cost of \$173,000.
- Hawaiian Tract Phase I and II at an estimated cost of \$818,000.
- Bracken Road at an estimated cost of \$90,300.
- T-Main Feasibility Study and Phase I at an estimated cost of \$467,200.

### Customer Service and Administration

To increase the quality of service to the public, as well as accommodate internal needs, the District is planning to build new administrative and operations facilities. The existing facilities do not meet current building codes or accessibility requirements, are cramped, poorly ventilated, worn and poorly lit, making it increasingly difficult for the District's employees to adequately serve customers. Furthermore, preliminary structural investigations indicate the building does not meet current seismic or wind loading requirements. The District solicited and reviewed proposals from several architectural firms to design the future

administrative center and master plan a new corporate yard. Murray & Downs Architects, Inc. was selected to provide preliminary recommendations, estimated costs and design work. The District incurred \$5,480 in preliminary costs in 2005 and \$804,604 in 2006 for the purchase of the new property as recommended by Murray & Downs Architects, Inc. The District anticipates completing construction of the building within the next two years at the estimated cost of \$6.3 million.

### Water Conservation

Conservation is an integral component of District's operations. Conservation is governed by local, state, and federal programs, such as those outlined by the: California Urban Water Conservation Council (CUWCC), Water Forum Agreement, and the U.S. Bureau Reclamation Central Valley Project Improvement Act. The District's objective is to implement water conservation best management practices (BMPs) in an efficient, cost effective and positive manner.

The District has developed the following proactive water efficiency outreach programs:

- Water-wise house calls; onsite water efficiency reviews that provide information on efficient water application at the specific property.
- The District toilet incentive rebate program; offered in partnership with the Sacramento Regional County Sanitation District and Regional Water Authority.
- Large landscape reviews; offered in conjunction with a grant from the U.S. Bureau of Reclamation and Proposition 13 through the Regional Water Authority Large Landscape Irrigation System Incentive Program.
- The Water Conservation School Poster Contest program. This program reaches out to grades 4 through 6 within the District, stressing an annual water conservation theme.
- Public outreach through community events such as: the Sacramento Convention Center Landscape Exposition, local Home and Garden Shows, Fair Oaks Spring Fest, Get W.E.T. sponsored in part with the Bureau of Reclamation, Fair Oaks Harvest Day events and the Department of Fish and Games Salmon Festival.

These programs are designed to raise water conservation awareness among our customers and increase water supply available to the District.

### Regional Planning

In early 1998, the District and other water utilities north of the American River initiated an effort to study and evaluate projects and programs for using surface water and groundwater resources better, particularly during supply shortages. This conjunctive use effort generally calls for the use of surface water from lakes and rivers in wet periods, while storing underground water supplies for later, when surface waters are needed for environmental purposes. As a follow up effort to the Sacramento region's *Water Forum Agreement*, participating members are motivated to plan for and meet the greater Sacramento areas' water needs to the year 2030, especially in drought years.

Two separate pilot studies have been undertaken to test conjunctive use concepts in the Sacramento groundwater basin; one with the Sacramento Area Flood Control Agency, and one program with the CALFED Environmental Water Account. Both programs are deemed a success in understanding hydrologic and hydraulic operations, while addressing regulatory, governmental and institutional constraints. In 2002, seven water utilities, including the District, sought and received grant funds from Proposition 13 in the amount of nearly \$23 million to construct and install groundwater storage and extraction facilities that advance conjunctive use strategies. The Proposition 13 grant requires a 50% local cost share proportionate to the partnering agency benefit. The District used most of these funds to construct groundwater storage and recovery facilities in 2006 and will use the remaining grant funds to complete the Heather and Town Wells in 2007. The success of the Proposition 13 grant is a testament to the District's participation in recent regional cooperation efforts and joint planning, serving as a basis for future partnering efforts.

## **Financial Information**

### Internal Control

Management is responsible for establishing and maintaining an internal control structure designed to ensure its assets are protected from loss, theft, or misuse and to ensure adequate accounting data is compiled to allow for the preparation of financial statements in conformity with generally accepted accounting principles. The internal control structure is designed to:

- (1) provide reasonable, but not absolute, assurance these objectives are met;
- (2) transactions are executed in accordance with management's authorization; and
- (3) transactions are recorded properly.

The concept of reasonable assurance recognizes:

- (1) the cost of the control should not exceed the benefits likely to be derived; and
- (2) the evaluation of costs and benefits requires estimates and judgments by management.

### Budgetary Control

While the District is not mandated to prepare budgets by State law, the District does prepare budgets as a matter of policy and financial control. The budget is a financial plan for detailing operating expenses, capital infrastructure investments, debt obligations, designations and reserves. For the year ending December 31, 2006, the budget was adopted December 19, 2005.

The financial plan establishes project priorities based upon District goals, policies and water distribution needs. The budget is developed following these steps:

- Assess current conditions and needs, including system quality and safety;
- Develop goals, objectives, policies, and plans based upon the assessment;
- Prioritize projects and develop work programs, based upon short-term and long-term cost effectiveness; and
- Prepare a plan to evaluate the effectiveness and shortcomings of the budget.

The budget is prepared on a cash basis, which differs from the basis used in preparing financial statements in conformity with generally accepted accounting principles (GAAP). The District staff works with a budget committee, which extensively reviews the proposed budget. The proposed budget is then presented to the board of directors for comments, suggestions, and feedback prior to notifying District customers.

The District notifies customers 45 days in advance of the public hearing and also holds public workshops designed to provide extensive budget information prior to the public hearing date. The District follows a very extensive and open budget process. The process is designed to educate and inform customers about the District's financial operations and requirements. The District adopts its budget at a Public Hearing. The adopted budget is then used as a management tool for projecting and measuring revenues and expenses for a ten to fifteen year planning horizon.

### Cash Management

The District complies with published investment policies and the provisions of the State statutes pertaining to the types of investments held. The District's cash, except for small amounts on hand for paying current expenses and amounts held with fiscal agents, is deposited in the State of California's Local Agency Investment Fund. Cash surpluses in these accounts are invested and investment earnings are allocated to the District's funds on the basis of average daily cash balances. Amounts held with fiscal agents are invested according to permitted investments outlined in official statements.

### Risk Management

The District participates in the Association of California Water Agency Joint Powers Insurance Authority (ACWA JPIA), a pooled self-insurance group. The District purchases its property, general liability, and automobile insurance from ACWA JPIA. Additionally, all contractors doing work for the District are required to furnish certificates of insurance for general liability, automobile liability, and workers' compensation and indemnification clauses.

The District purchases worker's compensation insurance through Association of California Water Agency Joint Powers Insurance Authority (ACWA JPIA). The District has a defined safety program, holding monthly safety and training sessions as well as on the spot training sessions to ensure employees conduct their work in a safe manner.

### **Other Information**

#### Independent Audit

California Government Code Section 26909 requires independent annual audits to be conducted for special districts. Richardson & Company has been selected to conduct the annual audit. The auditor's report is included in the financial section of the Comprehensive Annual Financial Report.

## Awards and Acknowledgements

The preparation of the comprehensive annual financial report on a timely basis requires the dedicated efforts of several staff members. We wish to express our appreciation to all District staff and managers who contributed to this report. Additionally, thank you to the Fair Oaks Water District Board of Directors for their interest and support in planning and conducting the financial operation of the District. The preparation of this report could not have been accomplished without the combined effort of the District leadership, Richardson & Company and staff.

The District received a certificate of achievement for excellence in financial reporting from the Government Finance Officers Association of the United States and Canada for year ended December 31, 2005.

Respectfully submitted,



Tom R. Gray  
General Manager



Chi Ha-Ly  
Senior Financial Analyst

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

## Fair Oaks Water District California

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
December 31, 2005

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

**BOARD OF DIRECTORS**

Daniel Gilliam  
President

Randy Marx  
Vice President

Barry Brown  
Director

Kyle Ericson  
Director

Misha Sarkovich  
Director

**STAFF**

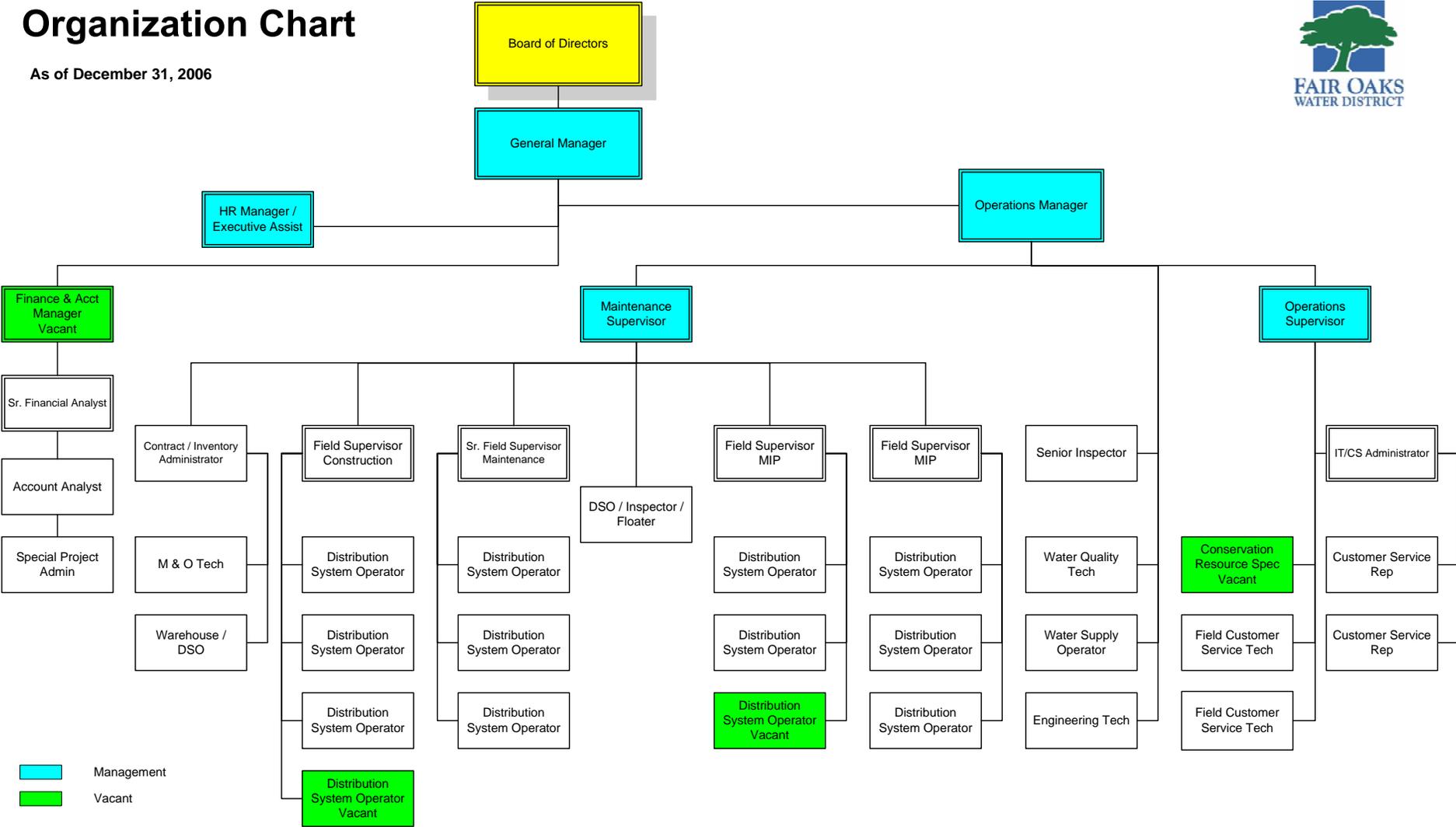
Tom R. Gray  
General Manager

Michael Nisenboym  
Operations Manager

Chi Ha-Ly  
Senior Financial Analyst

# Organization Chart

As of December 31, 2006



Management  
 Vacant



## **FINANCIAL SECTION**

**INDEPENDENT AUDITOR'S REPORT**

**To the Board of Directors  
Fair Oaks Water District  
Fair Oaks, California**

We have audited the accompanying balance sheets of the Fair Oaks Water District as of December 31, 2006 and 2005 and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District as of December 31, 2006 and 2005 and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis, as listed in the accompanying table of contents, 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 the supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report thereon dated March 6, 2007 on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts. 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.

To the Board of Directors  
Fair Oaks Water District

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The Additional Information listed in the table of contents is presented for the 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 stated in all material respects in relation to the basic financial statements taken as a whole.

The Introductory and Statistical Sections listed in the table of contents are presented for purposes of additional analysis and is not a required part of the basic financial statements. Such additional information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

*Richardson & Company*

March 6, 2007

**MANAGEMENT'S DISCUSSION  
AND ANALYSIS**

## MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the Fair Oaks Water District (the District), we offer the readers of the District financial statements this narrative overview and analysis of the financial activities for the District for the year ended December 31, 2006. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal and the audited financial statements.

### Financial Highlights

- The assets of the District exceeded its liabilities at the close of the most recent fiscal year by \$30,922,479 (net assets). Of this amount, \$10,315,265 of unrestricted net assets may be used to meet the District's ongoing obligations to citizens and creditors.
- The District has designated \$8.0 million dollars for future investment in capital assets, emergency and rate stabilization.
- The District has invested \$1.5 million dollars of unrestricted net assets in water capacity entitlements.
- The District's total net assets increased by \$3,741,672.
- The District's total debt decreased by \$773,800 during the fiscal year due to scheduled principal payments.
- Water sales increased by \$41,918, while other operating revenues decreased by \$26,847 during the fiscal year.
- Maintenance and Operation costs had a net decrease of \$4,118 and customer service had a net decrease of \$32,883, and administration and general costs had a net increase of \$30,725.

### Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements which are comprised of the financial statements and the notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

#### Financial Statements

The financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business. The revenues and expenses for 2004 and 2005 have been reclassified to conform to the 2006 presentation.

The statement of net assets presents information on all of the District's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the District's financial position is improving or deteriorating.

The statement of revenues, expenses and changes in net assets presents information showing how net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs,

regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (i.e. uncollected water sales and amounts due to vendors).

Since the District's primary function is to provide water delivery to its customers, with recovery of all the costs through user fees and charges, the financial statements only include business-type activities.

The accounts of the District are organized on the basis of fund accounting. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. Because the District provides water delivery and recovers these costs through user fees and charges, the District's funds are accounted for as an enterprise fund type of the proprietary fund group.

The District has determined that the Fair Oaks Water District Financing Corporation (Financing Corporation) meets the requirements for inclusion within the financial reporting entity and has, therefore, included the Financing Corporation as a blended component unit in the District's financial statements.

The financial statements can be found on pages 12 to 15.

#### Notes to Financial Statements

The notes provide additional information that is essential to a full understanding of the financial data provided in the financial statements. The notes to the financial statements can be found on pages 16 to 31 of this report.

#### Other Information

In addition to the basic financial statements and accompanying notes, this report also presents certain supplementary information regarding the District's debt service rate covenant compliance. This information can be found on page 32. The report also includes a statistical section of selected financial information over a 10 year period. This information can be found on pages 35 to 41 of this report.

#### **Financial Analysis**

As noted earlier, net assets may serve as a useful indicator of a government's financial position over time. In the case of the District, assets exceeded liabilities by \$30,922,479 at the close of the most recent fiscal year.

The largest portion of the District's net assets (62 percent) reflects its investment in capital assets (e.g., land, buildings, machinery, and equipment), less any related debt and unused proceeds used to acquire those assets that are still outstanding. The District uses these capital assets to provide water service delivery to its users. Consequently, these assets are not available for future spending. Although the District's investment in its capital assets is reported net of related debt, resources are needed to repay this debt and

must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

### Fair Oaks Water District Net Assets

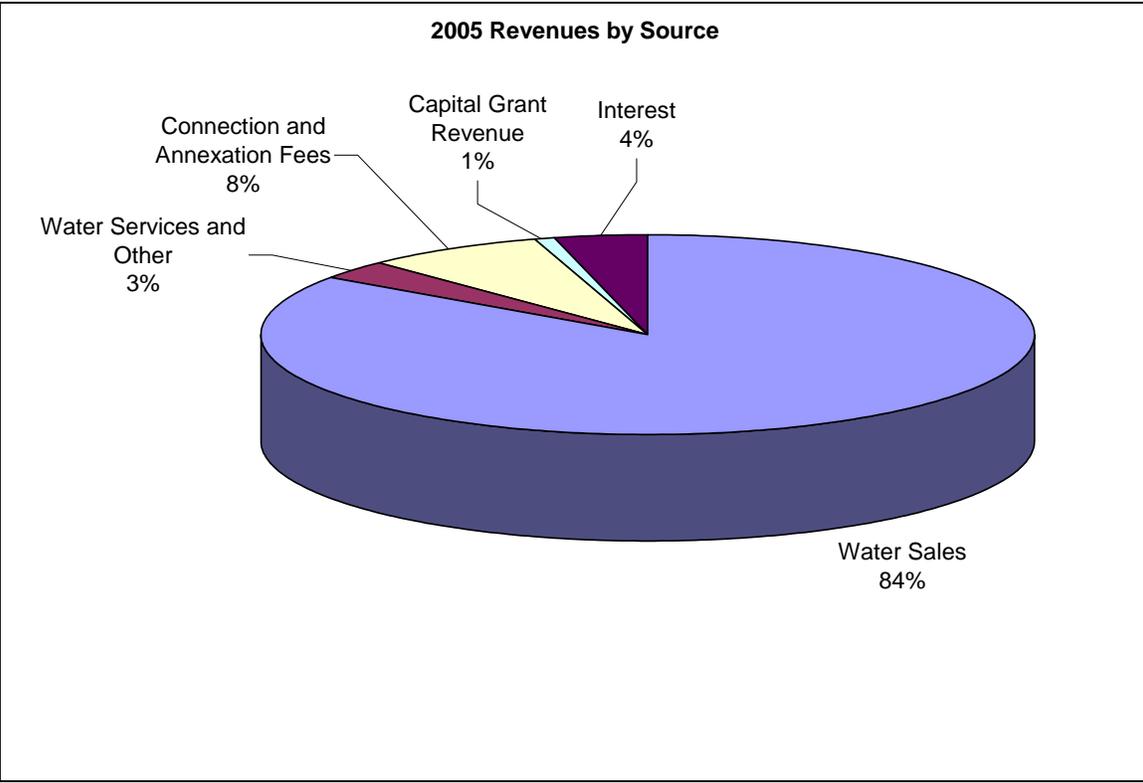
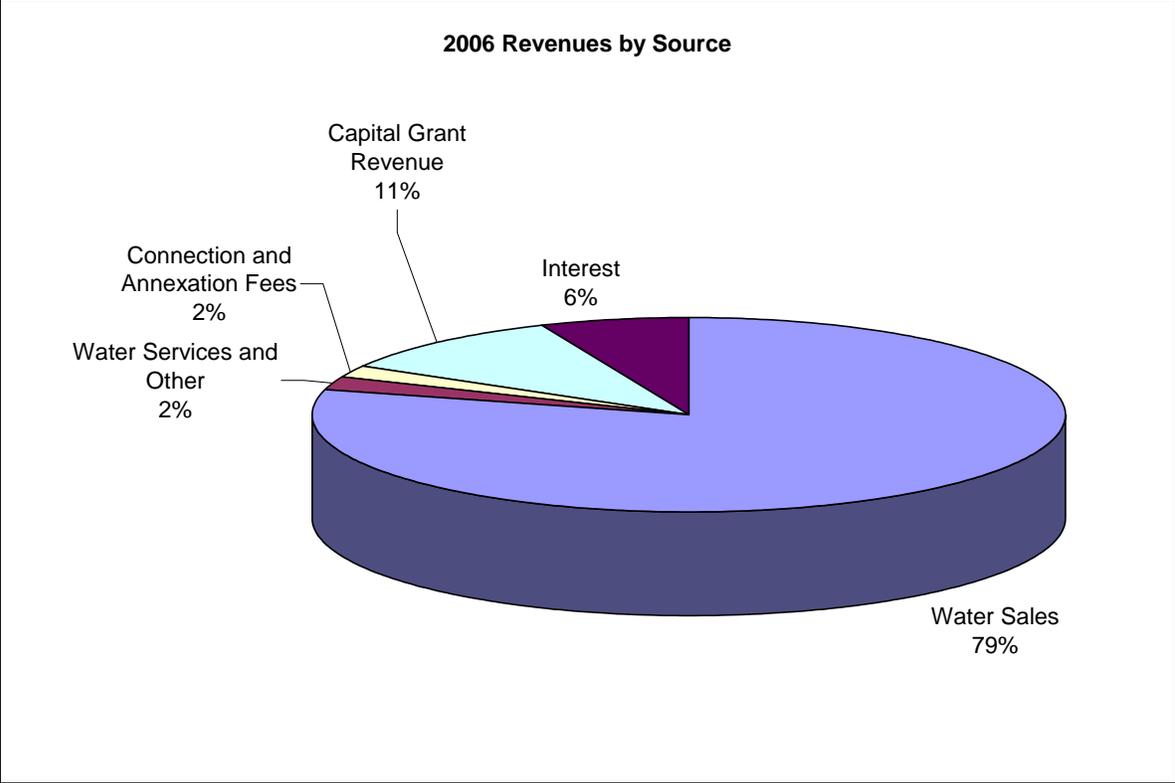
	<u>2006</u>	<u>2005</u>	<u>2004</u>
Current assets	\$13,205,713	\$14,558,485	\$12,157,565
Other assets	3,160,664	3,276,531	3,392,030
Capital assets	<u>21,571,276</u>	<u>17,063,510</u>	<u>16,444,818</u>
Total assets	<u>37,937,653</u>	<u>34,898,526</u>	<u>31,994,413</u>
Long-term liabilities	\$ 3,234,969	\$ 4,004,554	\$ 4,763,211
Other liabilities	<u>3,780,205</u>	<u>3,713,165</u>	<u>3,377,948</u>
Total liabilities	7,015,174	7,717,719	8,141,159
Net assets:			
Invested in capital assets,			
Net of related debt	19,041,276	13,938,510	12,744,821
Restricted	1,565,938	2,052,570	1,389,828
Unrestricted	<u>10,315,265</u>	<u>11,189,727</u>	<u>9,718,605</u>
Total net assets	<u>\$30,922,479</u>	<u>\$27,180,807</u>	<u>\$23,853,254</u>

The increase in net assets is largely due to meter installations, work on the Town and Heather Wells projects and the purchase of land for new administration building.

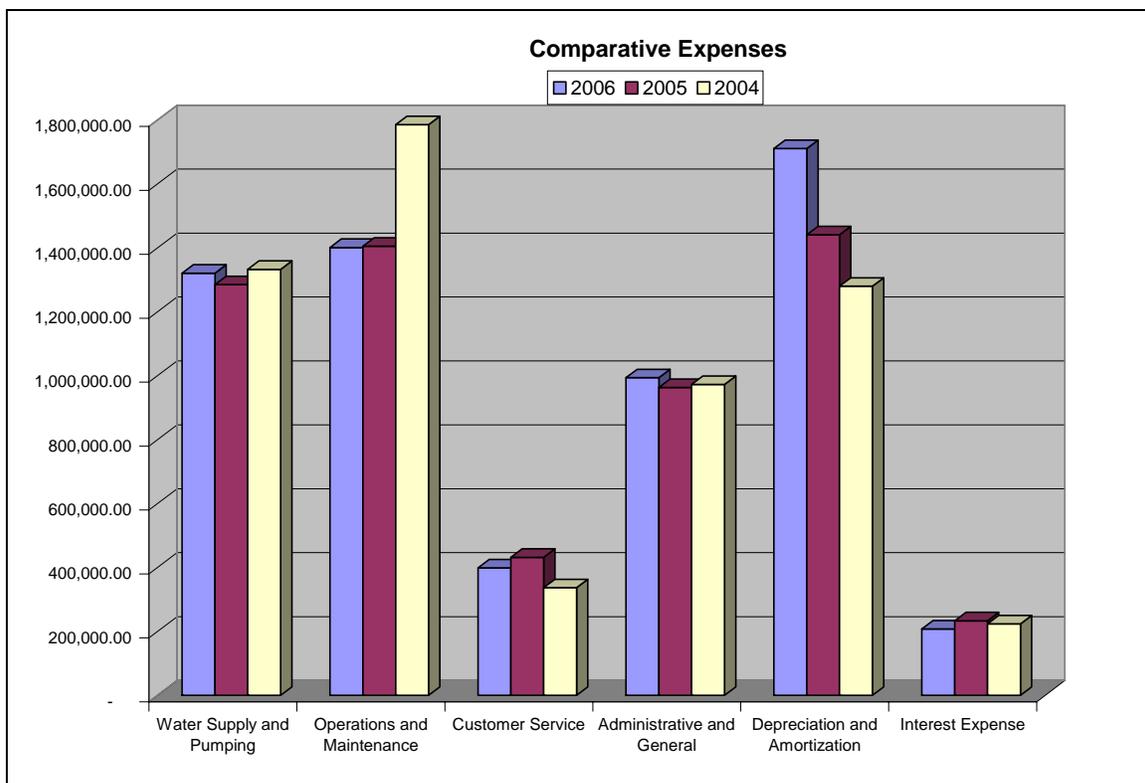
A portion of the District's net assets (approximately 5 percent) represents resources that are subject to external restrictions on how they may be used. Of the unrestricted portion, 14 percent of the District's net assets have been invested in water pipeline capacity entitlements, net of related debt (see footnote D, page 26). The District has also designated \$8.0 million dollars for future investment in capital assets, emergency and rate stabilization (see footnote F, pages 28-29).

## Fair Oaks Water District Changes in Net Assets

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Operating Revenues:			
Water Sales	\$7,723,313	\$7,681,395	\$7,052,897
Water Services	113,255	146,794	57,657
Other	<u>118,046</u>	<u>111,354</u>	<u>77,506</u>
Total Operating Revenues	7,954,614	7,939,543	7,188,060
Non-Operating Revenues:			
Interest Revenue	610,556	354,769	170,533
Grant Revenue		15,000	30,000
(Loss) Gain on Disposal of Capital Assets	<u>11,570</u>	<u>12,190</u>	<u>(4,614)</u>
Total Non-Operating Revenues	622,126	381,959	195,919
Capital Revenues:			
Contributed Assets		8,000	289,839
Capital Grant Revenue	1,030,162	63,257	
Connections and Annexation Fees	<u>169,901</u>	<u>695,200</u>	<u>158,188</u>
Total Capital Revenues	1,200,063	766,457	448,027
Total Revenues	9,776,803	9,087,959	7,832,006
Operating Expenses:			
Water Supply and Pumping	1,321,268	1,285,208	1,333,038
Operations and Maintenance	1,401,320	1,405,438	1,785,638
Customer Service	399,124	432,007	337,202
Administrative and General	994,004	963,279	972,740
Depreciation and Amortization	<u>1,711,211</u>	<u>1,441,207</u>	<u>1,279,989</u>
Total Operating Expenses	5,826,927	5,527,139	5,708,607
Non-Operating Expenses:			
Interest Expense	<u>208,204</u>	<u>233,267</u>	<u>223,590</u>
Total Non-Operating Expenses	208,204	233,267	223,590
Total Expenses	6,035,131	5,760,406	5,932,197
Increase in net assets	3,741,672	3,327,553	1,899,809
Net assets January 1	<u>27,180,807</u>	<u>23,853,254</u>	<u>21,953,445</u>
Net assets December 31	<u>\$30,922,479</u>	<u>\$27,180,807</u>	<u>\$23,853,254</u>



- Water sales increased by \$41,918 (less than 1 percent) in 2006 and by \$628,498 (9 percent) in 2005. The District did not increase water rates in 2006. The District increased water rates in 2005 by 10 percent.
- Interest income increased by \$255,787 in 2006 and increased by \$ 184,236 in 2005 due to market interest rates fluctuation.
- Capital grant revenue increased by \$966,905 due to reimbursable expenses from Town and Heather Wells projects from the Department of Water Resources Proposition 13 grant.
- Connections and annexation fees decreased by \$525,299 in 2006. The District collected approximately \$595,000 from Gum Ranch development in 2005. The District did not have any significant development in 2006.



- The operations and maintenance had a net decrease of \$4,118. The net decrease is due to a net decrease in salaries and benefits of \$10,132 and a net increase in system repairs and maintenance of \$6,014.
- Customer service had a net decrease of \$32,883 due to one vacant position.
- Administration and general expenses had a net increase of \$30,725. The increases in administrative and general are due to increases in legal fees of \$92,818; decreases in other professional fees of \$61,181.
- Water supply costs increased by \$36,060 due to increased wholesale water cost.

## Capital Asset and Debt Administration

The District's investment in capital assets as of December 31, 2006, amounts to \$21,571,276 (net of accumulated depreciation). This investment in capital assets includes land, buildings, system and distribution construction and improvements, machinery and equipment, wells, tanks, office equipment, and vehicles. The total net increase in investment in capital assets for the current fiscal year was 26 percent.

Major capital asset events during the current fiscal year included the following:

- The District began construction on Heather and Town Wells in 2005. The District incurred expenses totaling \$2,060,323 for both wells in 2006 (\$1,086,798 for Heather and \$973,525 for Town Wells). The total cost for both wells for 2005 and 2006 is \$2,186,836. The District has grant funding from the Department of Water Resources up to \$1,103,904 for the well projects. The District received \$440,900 of grant revenue in 2006 and expects to receive the remaining grant funding of \$659,000 in 2007. The District anticipates completing the well projects in 2007 with the projected remaining costs of \$1,939,000.
- The District installed 947 meters and 1,192 AMR (Automatic Meter Read) units on customer service connections at a cost of approximately \$1.9 million as part of the Metering Implementation Program (MIP) in 2006.
- The District completed construction on Watkins Drive Main Replacement at a cost of \$292,000.
- The District completed the North Winding Way project with a total cost of \$373,950.
- The District completed main replacement on Timothy Way for a total cost of \$298,252.
- Approximately \$176,000 was spent on various individual service line and hydrant upgrades in 2006.
- The District purchased: one Backhoe for \$82,242; one Service truck for \$37,497; two Dodge Dakota vehicles totaling \$28,911 in 2006.
- The administrative building was budgeted in 2005 for \$1,500,000 in building costs, but only \$5,480 was expended. The District incurred \$804,604 in 2006 for the purchase of land for the new building. The project will continue in 2007 and 2008.

## Fair Oaks Water District Capital Assets, net of depreciation

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Capital Assets, not being depreciated:			
Land	\$1,128,565	\$323,961	\$323,961
Construction in Progress	<u>2,286,979</u>	<u>229,929</u>	<u>54,214</u>
Total Capital Assets, not being depreciated	<u>3,415,544</u>	<u>553,890</u>	<u>378,175</u>
Capital Assets, being depreciated:			
Wells and Pumps	52,171	69,492	82,020
Transmission and Distribution System	13,471,192	11,395,551	10,486,664
Maintenance Equipment	56,716	41,168	52,410
Trucks, Trailers, and Mobile Equipment	407,538	386,857	460,708
Buildings	99,922	121,278	132,339
Office Equipment and Furnishings	102,102	258,474	357,879
Contributed Distribution Systems	3,805,537	4,034,269	4,254,733
Water Tank and Pumping	<u>160,554</u>	<u>202,531</u>	<u>239,890</u>
Total Capital Assets, being depreciated	<u>18,155,732</u>	<u>16,509,620</u>	<u>16,066,643</u>
 Total	 <u>\$21,571,276</u>	 <u>\$17,063,510</u>	 <u>\$16,444,818</u>

Additional information on the capital assets can be found in Note C on pages 24 to 25 of this report.

### Long-Term Debt

At the end of the current fiscal year, the District had total debt outstanding of \$4,088,912. Of this amount, \$2,530,000 is comprised of certificates of participation debt secured solely by pledged water revenues. These certificates were issued to advance refund outstanding 1989 and 1991 certificates of participation. The reacquisition price of the 1999 certificates compared to the net carrying value of the 1989 and 1991 certificates is deferred and is systematically amortized over the remaining life of the refinanced certificates. The remaining debt represents a capacity entitlement agreement between the District and San Juan Water District for the District to pay a portion of principal and interest payments related to San Juan's certificates of participation debt for to the acquisition of capacity water rights in a transmission pipeline.

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Certificates of Participation	\$2,530,000	\$3,125,000	\$3,700,000
Capacity Entitlement Agreement	<u>1,558,912</u>	<u>1,737,712</u>	<u>1,912,787</u>
Total Debt	4,088,912	4,862,712	5,612,787
Unamortized Difference	<u>(144,621)</u>	<u>(173,544)</u>	<u>(202,467)</u>
Total	<u>\$3,944,291</u>	<u>\$4,869,168</u>	<u>\$5,410,320</u>

Total debt decreased during the fiscal year by \$773,800 due to payments of scheduled principal made during the year. The District maintains an “AAA” rating by Moody’s and “AAA” rating by Fitch and Standard & Poor’s on the certificates of participation debt. Additional information on the District’s long-term debt can be found in Note E on pages 26 to 28 of this report.

### **Economic Factors and assumptions in preparing the 2007 Budget and Rates**

- The unemployment rate for the greater Sacramento County in which the District resides averaged 4.3% in 2006, up from an average 4.1 % in 2005.
- The District is largely built out, serving approximately 14,467 customers.
- Inflationary trends in the region are comparable to national indices.
- The District continues to face increasing regulatory requirements that ultimately add new costs to delivering the water service (i.e. security measures, new water quality tests, etc.)
- There will be no rate increases in 2007.
- Health benefit costs are expected to increase another 10% in 2007.
- The District must continue to install water meters for its residential customers to meet the Federal and State mandates. In order to meet the time deadline, the District plans to install 1,141 meters in 2007. These costs are extensive and factored into the budget.
- The District intends to use the reserve to fund for the shortfall of revenues in 2007.

All of these factors were considered in preparing the District’s budget for the 2007 fiscal year.

### **Requests for Information**

This financial report is designed to provide a general overview of the District’s finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Senior Financial Analyst, Fair Oaks Water District, 10317 Fair Oaks Boulevard, Fair Oaks, CA 95628.

# **BASIC FINANCIAL STATEMENTS**

# FAIR OAKS WATER DISTRICT

## BALANCE SHEETS

**December 31, 2006 and 2005**

	2006	2005
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 9,766,886	\$ 11,335,598
Restricted cash and cash equivalents	1,565,938	2,052,570
Accounts receivable	840,518	170,293
Water service receivable	157,678	162,212
Interest receivable	143,944	110,595
Inventory	588,217	577,963
Prepaid expenses	142,532	149,254
<b>TOTAL CURRENT ASSETS</b>	<b>13,205,713</b>	<b>14,558,485</b>
<b>NON-CURRENT ASSETS</b>		
Dues on deposit	74,810	77,928
Capital assets, net	21,571,276	17,063,510
Unamortized bond expenses, net	69,214	83,057
Capacity entitlements, net	3,016,640	3,115,546
<b>TOTAL NON-CURRENT ASSETS</b>	<b>24,731,940</b>	<b>20,340,041</b>
<b>TOTAL ASSETS</b>	<b>\$ 37,937,653</b>	<b>\$ 34,898,526</b>
<b>LIABILITIES</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 470,333	\$ 315,835
Accrued expenses	32,825	10,204
Accrued payroll expense	95,467	103,569
Accrued interest expense	48,069	51,347
Deposits	24,975	15,500
Unearned revenue	2,304,149	2,442,910
Current portion of long-term debt	804,387	773,800
<b>TOTAL CURRENT LIABILITIES</b>	<b>3,780,205</b>	<b>3,713,165</b>
<b>LONG-TERM LIABILITIES</b>		
Long-term debt	3,139,904	3,915,368
Compensated absences	95,065	89,186
<b>TOTAL LONG-TERM LIABILITIES</b>	<b>3,234,969</b>	<b>4,004,554</b>
<b>TOTAL LIABILITIES</b>	<b>7,015,174</b>	<b>7,717,719</b>
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	19,041,276	13,938,510
Restricted:		
Connection and annexation fees	907,683	1,392,095
Certificates of participation	658,255	660,475
Unrestricted	10,315,265	11,189,727
<b>TOTAL NET ASSETS</b>	<b>30,922,479</b>	<b>27,180,807</b>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>\$ 37,937,653</b>	<b>\$ 34,898,526</b>

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

**FAIR OAKS WATER DISTRICT**

**STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS**

**For the years ended December 31, 2006 and 2005**

	2006	2005
<b>OPERATING REVENUES</b>		
Water sales	\$ 7,723,313	\$ 7,681,395
Water services	113,255	146,794
Other	118,046	111,354
<b>TOTAL OPERATING REVENUES</b>	<b>7,954,614</b>	<b>7,939,543</b>
<b>OPERATING EXPENSES</b>		
Water supply and pumping	1,321,268	1,285,208
Operations and maintenance	1,401,320	1,405,438
Customer service	399,124	432,007
Administrative and general	994,004	963,279
Depreciation and amortization	1,711,211	1,441,207
<b>TOTAL OPERATING EXPENSES</b>	<b>5,826,927</b>	<b>5,527,139</b>
<b>NET INCOME FROM OPERATIONS</b>	<b>2,127,687</b>	<b>2,412,404</b>
<b>NON-OPERATING REVENUES (EXPENSES)</b>		
Interest revenue	610,556	354,769
Grant revenue		15,000
Gain on disposal of capital assets	11,570	12,190
Interest expense	(208,204)	(233,267)
<b>TOTAL NON-OPERATING REVENUES (EXPENSES)</b>	<b>413,922</b>	<b>148,692</b>
<b>NET INCOME BEFORE CAPITAL CONTRIBUTIONS</b>	<b>2,541,609</b>	<b>2,561,096</b>
<b>CAPITAL CONTRIBUTIONS</b>		
Contributed assets		8,000
Connection and annexation fees	169,901	695,200
Capital grant revenue	1,030,162	63,257
<b>TOTAL CAPITAL CONTRIBUTIONS</b>	<b>1,200,063</b>	<b>766,457</b>
<b>CHANGE IN NET ASSETS</b>	<b>3,741,672</b>	<b>3,327,553</b>
Net assets at beginning of year	27,180,807	23,853,254
<b>NET ASSETS AT END OF YEAR</b>	<b>\$ 30,922,479</b>	<b>\$ 27,180,807</b>

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

**FAIR OAKS WATER DISTRICT**

**STATEMENTS OF CASH FLOWS**

**For the years ended December 31, 2006 and 2005**

	2006	2005
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Cash receipts from customers	\$ 7,729,906	\$ 8,046,083
Cash paid to suppliers	(1,918,239)	(2,266,608)
Cash paid to employees	(2,026,113)	(1,883,571)
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>3,785,554</b>	<b>3,895,904</b>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Proceeds from disposal of capital assets	39,600	12,190
Principal payments on long-term debt	(773,800)	(750,075)
Interest payments on long-term debt	(182,559)	(177,795)
Grants received	459,893	15,000
Connection and annexation fees received	169,901	695,200
Purchases of capital assets	(6,134,258)	(1,939,150)
<b>NET CASH USED BY RELATED FINANCING ACTIVITIES</b>	<b>(6,421,223)</b>	<b>(2,144,630)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Interest received	577,207	307,566
Dues on deposit received	3,118	2,750
<b>NET CASH PROVIDED BY INVESTING ACTIVITIES</b>	<b>580,325</b>	<b>310,316</b>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>(2,055,344)</b>	<b>2,061,590</b>
 Cash and cash equivalents at beginning of year	 13,388,168	 11,326,578
 <b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	 <b>\$ 11,332,824</b>	 <b>\$ 13,388,168</b>
 <b>COMPONENTS OF CASH AND CASH EQUIVALENTS</b>		
Cash and equivalents	\$ 9,766,886	\$ 11,335,598
Restricted cash and cash equivalents	1,565,938	2,052,570
 <b>TOTAL CASH AND CASH EQUIVALENTS</b>	 <b>\$ 11,332,824</b>	 <b>\$ 13,388,168</b>

(Continued)

**FAIR OAKS WATER DISTRICT**

**STATEMENTS OF CASH FLOWS (Continued)**

**For the years ended December 31, 2006 and 2005**

	2006	2005
<b>RECONCILIATION OF NET INCOME FROM OPERATIONS TO</b>		
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES:</b>		
Net income from operations	\$ 2,127,687	\$ 2,412,404
Adjustments to reconcile net income from operations to net cash provided by operating activities:		
Depreciation and amortization	1,711,211	1,441,207
Changes in assets and liabilities:		
Accounts receivable	(99,956)	(51,108)
Water service receivable	4,534	(12,668)
Inventory	(10,254)	(343,896)
Prepaid expenses	6,722	178,802
Accounts payable	154,498	92,119
Accrued expenses	22,621	4,521
Accrued payroll expense	(8,102)	17,987
Deposits	9,475	3,525
Unearned revenue	(138,761)	166,791
Compensated absences	5,879	(13,780)
	<b>\$ 3,785,554</b>	<b>\$ 3,895,904</b>
 <b>SUPPLEMENTAL DISCLOSURE OF NON-CASH ACTIVITIES</b>		
Receipt of contributed assets		\$ 8,000

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

# FAIR OAKS WATER DISTRICT

## NOTES TO THE BASIC FINANCIAL STATEMENTS

December 31, 2006 and 2005

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### NOTE A--REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the Fair Oaks Water District (the District) have been prepared in conformity with generally accepted accounting principles as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. As allowed by the GASB, the District has elected not to apply to its proprietary activities Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee of Accounting Procedures issued after November 30, 1989. The more significant of the District's accounting policies are described below.

Reporting Entity: The District was formed March 26, 1917 under the provisions of the California Water Code. The District is governed by a five member Board of Directors elected by the voters within the District for staggered, four-year terms, every two years. The District provides water to retail customers in the Fair Oaks area. The accompanying basic financial statements present the District and its component unit. The component unit discussed below is included in the District's reporting entity because of the significance of its operational and financial relationship with the District.

The District has created the Fair Oaks Water District Financing Corporation (the Financing Corporation) to provide assistance to the District in the issuance of debt. Although legally separate from the District, the Financing Corporation is reported as if it were part of the primary government because it shares a common Board of Directors with the District and its sole purpose is to provide financing to the District under the debt issuance documents of the District. Debt issued by the Financing Corporation is reflected as debt of the District in these financial statements. The Financing Corporation has no other transactions and does not issue separate financial statements.

Jointly Governed Organization: The District is a signatory to the Regional Water Authority's (the RWA) Joint Powers Agreement, formally known as Sacramento Metropolitan Water Authority. The mission of the RWA is to serve and represent the regional water supply interest, and to assist the members of the RWA in protecting and enhancing the reliability, availability, affordability and quality of water resources. The goals of the RWA are to assist in voluntary consolidation of services provided by existing industry associations; develop and provide subscription-based support services; and coordinate and implement regional water master planning, grant-funding acquisition, and related planning efforts.

The RWA carries out its missions and goals, yet does not exercise governing or regulatory authority over its members. The relationship between the District and the RWA is such that the RWA is not a component unit of the District for financial reporting purposes. Additionally, the District does not have an ongoing financial responsibility to the RWA and therefore is considered a jointly governed organization. Separate financial statements are available from RWA.

# FAIR OAKS WATER DISTRICT

## NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2006 and 2005

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### NOTE A--REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Basis of Presentation--Fund Accounting: The District's resources are allocated to and accounted for in these basic financial statements as an enterprise fund type of the proprietary fund group. The enterprise fund is used to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges, or where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other policies. Net assets for the enterprise fund represents the amount available for future operations.

Basis of Accounting: The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. The enterprise fund type is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of this fund are included on the balance sheet. Net assets is segregated into amounts invested in capital assets, net of related debt, amounts restricted and amounts unrestricted. Enterprise fund type operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets.

The District uses the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. Earned but unbilled water services are accrued as revenue. Water lines are constructed by private developers and then dedicated to the District, which is then responsible for their future maintenance. These lines are recorded as capital contributions when they pass inspection by the District and the estimated costs are capitalized as part of the distribution system.

Operating revenues and expenses consists of those revenues and expenses that result from the ongoing principal operations of the District. Operating revenues consist primarily of charges for services. Non-operating revenues and expense consist of those revenues and expenses that are related to financing and investing types of activities and result from nonexchange transactions or ancillary activities.

When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

Budgetary Principles: The Board of Directors does not operate under any legal budgeting constraints. Budget integration is employed as a management control device. Budgets are formally adopted by the Board and take effect on each January 1.

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

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**NOTE A--REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Use of Estimates: The preparation of 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 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.

Cash and Cash Equivalents: For purposes of the statement of cash flows, the District considers all highly liquid debt instruments purchased with an initial maturity of three months or less to be cash equivalents, including restricted assets. Cash in banks, deposits in the State of California Local Agency Investment Fund (LAIF) and deposits with fiscal agents are considered to be cash and cash equivalents.

Water Service Receivable and Deferred Revenue: Customers that are invoiced on a flat rate basis have the options of making payments annually, semi-annually, or bimonthly. Advanced collections on water services invoiced in the current year for service in the following year are recorded as deferred revenue since these collections have not been earned as of December 31. Customers who are invoiced on a metered basis receive their bills bimonthly in arrears of the service provided. Unpaid amounts as of December 31 are recorded as water service receivable. Water invoices that remain unpaid when the new water invoices are issued may have a lien placed on the property.

Capital Assets: Capital assets are recorded at historical cost. Contributed assets are valued at estimated fair value on the date received. Depreciation is calculated using the straight line method over the following estimated useful lives:

<u>Description</u>	<u>Estimated Life</u>
Wells and Pumps	5-30 years
Transmission and distribution system	30 years
Maintenance Equipment	5-30 years
Trucks, Trailers, and Mobile Equipment	5-10 years
Buildings	5-30 years
Office Equipment and Furnishings	3-5 years
Contributed distribution systems	30 years
Water Tank and Pumping	5-10 years

Maintenance and repairs are charged to operations when incurred. It is the District's policy to capitalize all capital assets with a cost of \$500 or more. Costs of assets sold or retired (and the related amounts of accumulated depreciation) are eliminated from the balance sheet in the year of sale or retirement, and the resulting gain or loss is recognized in operations.

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

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**NOTE A--REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Inventory: Inventories are stated at the lower of cost, on a first-in, first-out method, or market. Inventories consist of materials and supplies.

Issuance Costs: Bond issuance costs are deferred and amortized over the life of the bonds. Bond issuance costs are reported as unamortized bond expenses, a component of Other Assets.

Compensated Absences: The District's policy allows employees to accumulate earned but unused vacation and administrative leave which will be paid to employees upon separation from the District's service, subject to a vesting policy. The cost of vacation and administrative leave is recorded in the period accrued.

Reclassifications: Certain reclassifications have been made to the 2006 financial statements to conform to the current presentation. These reclassifications had no effect on previously reported change in net assets.

**NOTE B--CASH AND INVESTMENTS**

Cash and investments as of December 31, 2006 and 2005 are classified in the accompanying financial statements as follows:

	<u>2006</u>	<u>2005</u>
Cash and cash equivalents	\$ 9,766,886	\$ 11,335,598
Restricted cash and cash equivalents	<u>1,565,938</u>	<u>2,052,570</u>
Total cash and investments	<u>\$ 11,332,824</u>	<u>\$ 13,388,168</u>

Cash and investments as of December 31, 2006 and 2005 consisted of the following:

	<u>2006</u>	<u>2005</u>
Cash on hand	\$ 1,387	\$ 950
Deposits with financial institutions	<u>2,285,905</u>	<u>1,691,788</u>
Total cash	<u>2,287,292</u>	<u>1,692,738</u>

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

**NOTE B--CASH AND INVESTMENTS (Continued)**

	<u>2006</u>	<u>2005</u>
Mutual funds	\$ 255	\$ 594
Investments in Local Agency Investment Fund (LAIF)	<u>9,045,277</u>	<u>11,694,836</u>
Total investments	<u>9,045,532</u>	<u>11,695,430</u>
 Total cash and cash equivalents	 <u>\$ 11,332,824</u>	 <u>\$ 13,388,168</u>

Investment policy: California statutes authorize districts to invest idle or surplus funds in a variety of credit instruments as provided for in the California Government Code, Section 53600, Chapter 4 - Financial Affairs. The table below identifies the investment types that are authorized for the District by the California Government Code (or the District's investment policy, where more restrictive) that address interest rate risk, credit risk, and concentration of credit risk. This table does not address investments of debt proceeds held by the bond trustee that are governed by the provisions of debt agreements of the District, rather than the general provisions of the California Government Code or the District's investment policy. During the year ended December 31, 2006, the District's permissible investments included the following instruments:

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Maximum Percentage Of Portfolio *</u>	<u>Maximum Investment In One Issuer</u>
Local Agency Bonds	5 years	None	None
U.S. Treasury Obligations	5 years	None	None
U.S. Agency Securities	5 years	None	None
Bankers Acceptances	180 days	40%	30%
Commercial Paper	270 days	25%	10%
Negotiable Certificates and Time Deposits	5 years	30%	None
Repurchase Agreements	92 days	20%	None
Medium Term Corporate Notes	5 years	30%	None
Mutual Funds	N/A	20%	10%
LAIF	N/A	None	None

\*Excluding amounts held by the bond trustee that are not subject to California Government Code restrictions.

The District complied with the provisions of the California Government Code pertaining to the types of investments held, the institutions in which deposits were made and the security requirements. The District will continue to monitor compliance with applicable statutes pertaining to public deposits and investments.

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

**NOTE B--CASH AND INVESTMENTS (Continued)**

Investments Authorized by Debt Agreements: Investment of debt proceeds held by the bond trustee are governed by provisions of the debt agreements, rather than the general provisions of the California Government Code or the District's investment policy. The 1999 Revenue Certificates of Participation debt agreement contains certain provisions that address interest rate risk and credit risk, but not concentration of credit risk.

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Maximum Percentage Of Portfolio</u>	<u>Maximum Investment In One Issuer</u>
Local Agency Bonds	None	None	None
U.S. Treasury Obligations	None	None	None
U.S. Agency Securities	None	None	None
Bankers Acceptances	360 days	None	None
Commercial Paper	270 days	None	None
Negotiable Certificates Deposits	None	None	None
Investment Agreements	None	None	None
Repurchase Agreements	None	None	None
Mutual Funds	N/A	None	None
LAIF	N/A	None	None

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. Information about the sensitivity of the fair values of the District's investments (including investments held by bond trustee) to market interest rate fluctuations is provided by the following table that shows the distribution of the District's investments by maturity:

	<u>Total</u>	<u>Remaining Maturity 12 Months or less</u>
LAIF	\$ 8,387,277	\$ 8,387,277
Held by bond trustee:		
LAIF	658,000	658,000
Mutual funds	<u>255</u>	<u>255</u>
Total	<u>\$ 9,045,532</u>	<u>\$ 9,045,532</u>

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

**NOTE B--CASH AND INVESTMENTS (Continued)**

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

	<u>Total</u>	<u>Minimum Legal Rating</u>	<u>Ratings as of Year End AAA</u>	<u>Not Rated</u>
LAIF	\$ 8,387,277	N/A		\$ 8,387,277
Held by bond trustee:				
LAIF	658,000	N/A		658,000
Mutual funds	<u>255</u>	AAA	<u>\$ 255</u>	<u>                    </u>
Total	<u>\$ 9,045,532</u>		<u>\$ 255</u>	<u>\$ 9,045,277</u>

Concentration of Credit Risk: The investment policy of the District limits the amount that can be invested in any one issuer to the California Government Code. There are no investments in any one issuer (other than external investment pools) that represent 5% or more of total District investments.

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. The California Government Code and the District's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits, other than the following provision for deposits: 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 public agency deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

# FAIR OAKS WATER DISTRICT

## NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2006 and 2005

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### NOTE B--CASH AND INVESTMENTS (Continued)

At December 31, 2006, the carrying amount of the District's deposits were \$2,285,905 and the balances in financial institutions was \$2,457,206. Of the balance in financial institutions, \$100,000 was covered by federal depository insurance and \$2,357,206 was collateralized as required by State law (Government Code Section 53630), by the pledging financial institution with assets held in a common pool for the District and other governmental agencies, but not in the name of the District. At December 31, 2005, the carrying amount of the District's deposits were \$1,691,788 and the balances in financial institutions was \$1,769,269. Of the balance in financial institutions, \$100,000 was covered by federal depository insurance and \$1,669,269 was collateralized.

Investment in LAIF: LAIF is stated at amortized cost, which approximates fair value. The LAIF is a special fund of the California State Treasury through which local governments may pool investments. The total amount invested on December 31, 2006 by all public agencies in LAIF is \$57,120,735,065 managed by the State Treasurer. Of that amount, 96.8 percent is invested in non-derivative financial products and 3.2 percent in derivative financial products and structured financial instruments. The Local Investment Advisory Board (Board) has oversight responsibility for LAIF. The Board consists of five members as designated by State Statute. 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.

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

**NOTE C--CAPITAL ASSETS**

	<u>Balance</u>			<u>Transfers</u>	<u>Balance</u>
	<u>January 1</u>	<u>Additions</u>	<u>Disposals</u>	<u>And</u>	<u>December 31,</u>
	<u>2006</u>			<u>Adjustments</u>	<u>2006</u>
Capital assets not being depreciated					
Land	\$ 323,961	\$ 804,604			\$ 1,128,565
Construction in progress	<u>229,929</u>	<u>2,454,539</u>		\$ (397,489)	<u>2,286,979</u>
Total capital assets not being depreciated	553,890	3,259,143		(397,489)	3,415,544
Capital assets being depreciated:					
Wells and pumps	1,156,162		\$ (833)		1,155,329
Transmission and distribution system	18,548,042	2,646,475		397,489	21,592,006
Maintenance equipment	208,635	35,449	(15,698)		228,386
Trucks, trailers and mobile equipment	1,199,956	181,919	(118,155)		1,263,720
Buildings	702,156	1,575			703,731
Office equipment and furnishings	917,601	10,531	(114,358)		813,774
Contributed distribution system	6,861,935				6,861,935
Water tank and pumping	<u>416,292</u>				<u>416,292</u>
Total capital assets being depreciated, net	30,010,779	2,875,949	(249,044)	397,489	33,035,173
Less accumulated depreciation for:					
Wells and pumps	(1,086,670)	(16,488)			(1,103,158)
Transmission and distribution system	(7,152,491)	(968,323)			(8,120,814)
Maintenance equipment	(167,467)	(19,235)	15,032		(171,670)
Trucks, trailers and mobile equipment	(813,099)	(154,097)	111,014		(856,182)
Buildings	(580,878)	(22,931)			(603,809)
Office equipment and furnishings	(659,127)	(146,680)	94,135		(711,672)
Contributed distribution system	(2,827,666)	(228,732)			(3,056,398)
Water tank and pumping	<u>(213,761)</u>	<u>(41,977)</u>			<u>(255,738)</u>
Total accumulated depreciation	<u>(13,501,159)</u>	<u>(1,598,463)</u>	<u>220,181</u>		<u>(14,879,441)</u>
Total capital assets being depreciated, net	<u>16,509,620</u>	<u>1,277,486</u>	<u>(28,863)</u>	<u>397,489</u>	<u>18,155,732</u>
Capital assets, net book value	<u>\$ 17,063,510</u>	<u>\$ 4,536,629</u>	<u>\$ (28,863)</u>		<u>\$ 21,571,276</u>

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

**NOTE C--CAPITAL ASSETS (Continued)**

Capital asset activity for the years ended December 31, 2006 and 2005 are as follows:

	Balance January 1 <u>2005</u>	<u>Additions</u>	<u>Disposals</u>	Transfers And <u>Adjustments</u>	Balance December 31 <u>2005</u>
Capital assets not being depreciated					
Land	\$ 323,961				\$ 323,961
Construction in progress	<u>54,214</u>	\$ 175,715	_____	_____	<u>229,929</u>
Total capital assets not being depreciated	378,175	175,715			553,890
Capital assets being depreciated:					
Wells and pumps	1,151,968	4,194			1,156,162
Transmission and distribution system	16,942,172	1,605,870			18,548,042
Maintenance equipment	201,257	7,378			208,635
Trucks, trailers and mobile equipment	1,131,635	68,321			1,199,956
Buildings	692,316	9,840			702,156
Office equipment and furnishings	892,513	63,357	\$ (38,269)		917,601
Contributed distribution system	6,853,935	8,000			6,861,935
Water tank and pumping	<u>411,771</u>	<u>4,521</u>	_____	_____	<u>416,292</u>
Total capital assets being depreciated	28,277,567	1,771,481	(38,269)		30,010,779
Less accumulated depreciation for:					
Wells and pumps	\$ (1,069,948)	\$ (16,722)			\$ (1,086,670)
Transmission and distribution system	(6,455,508)	(696,983)			(7,152,491)
Maintenance equipment	(148,847)	(18,620)			(167,467)
Trucks, trailers and mobile equipment	(670,927)	(142,172)			(813,099)
Buildings	(559,977)	(20,901)			(580,878)
Office equipment and furnishings	(534,634)	(162,762)	\$ 38,269		(659,127)
Contributed distribution system	(2,599,202)	(228,464)			(2,827,666)
Water tank and pumping	<u>(171,881)</u>	<u>(41,880)</u>	_____	_____	<u>(213,761)</u>
Total accumulated depreciation	<u>(12,210,924)</u>	<u>(1,328,504)</u>	<u>38,269</u>		<u>(13,501,159)</u>
Total capital assets being depreciated, net	<u>16,066,643</u>	<u>442,977</u>	_____	_____	<u>16,509,620</u>
Capital assets, net book value	<u>\$ 16,444,818</u>	<u>\$ 618,692</u>	<u>\$ _____</u>	<u>_____</u>	<u>\$ 17,063,510</u>

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

**NOTE D--CAPACITY ENTITLEMENTS**

In 1993, the District participated with four other water districts in a cooperative transmission pipeline project for the construction of additional transmission pipeline facilities. As a result of this project, the District participated with San Juan Water District (SJWD) to finance their share of the pipeline costs. The District's share of these pipeline costs totaled \$3,956,248. The Capacity Entitlements asset represents the capacity rights the District has purchased in the cooperative transmission pipeline project with SJWD. The asset will be amortized over the pipeline's estimated useful life of forty years. At December 31, 2006 and 2005, accumulated amortization was \$939,608 and \$840,702, respectively. In addition, the District has entered into an agreement with SJWD to pay for its share of these transmission pipeline facilities costs (see Note E).

**NOTE E--LONG-TERM LIABILITIES**

The activity of the District's long-term liabilities during the years ended December 31, 2006 and 2005 are as follows:

	Balance January 1, 2006	Additions	Repayments	Balance December 31, 2006	Due Within One Year
1999 Revenue Certificates of Participation	\$ 3,125,000		\$ (595,000)	\$ 2,530,000	\$ 620,000
Capacity entitlement agreement	<u>1,737,712</u>		<u>(178,800)</u>	<u>1,558,912</u>	<u>184,387</u>
Total	4,862,712		<u>\$ (773,800)</u>	4,088,912	<u>\$ 804,387</u>
Deferred amount on refunding	(173,544)			(144,621)	
Less: Current portion of long-term debt	<u>(773,800)</u>			<u>(804,387)</u>	
	<u>\$ 3,915,368</u>			<u>\$ 3,139,904</u>	
Compensated absences	<u>\$ 89,186</u>	<u>\$ 5,879</u>		<u>\$ 95,065</u>	

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

**NOTE E--LONG-TERM LIABILITIES (Continued)**

	<u>Balance</u> <u>January 1,</u> <u>2005</u>	<u>Additions</u>	<u>Disposals</u>	<u>Balance</u> <u>December 31,</u> <u>2005</u>	<u>Due Within</u> <u>One Year</u>
1999 Revenue Certificates of Participation	\$ 3,700,000		\$ (575,000)	\$ 3,125,000	\$ 595,000
Capacity entitlement agreement	<u>1,912,787</u>		<u>(175,075)</u>	<u>1,737,712</u>	<u>178,800</u>
Total	5,612,787		<u>\$ (750,075)</u>	4,862,712	<u>\$ 773,800</u>
Deferred amount on refunding	(202,467)			(173,544)	
Less: Current portion of long-term debt	<u>(750,075)</u>			<u>(773,800)</u>	
	<u>\$ 4,660,245</u>			<u>\$ 3,915,368</u>	
Compensated absences	<u>\$ 102,966</u>		<u>\$ (13,780)</u>	<u>\$ 89,186</u>	

Long-term debt consists of the following:

1999 Certificates of Participation: On January 13, 1999, the District issued \$6,580,000 of Revenue Certificates of Participation (Certificates) with interest ranging from 3.875% to 4.25%. These 1999 Certificates were issued to advance refund outstanding 1989 and 1991 Certificates. The repayment of the debt is secured by a pledge of and first lien on the revenue of the District's water system. Annual principal payments, ranging from \$270,000 to \$690,000 are due on December 1 through December 1, 2011 and semi-annual interest payments, ranging from \$5,737 to \$51,744 are due on June 1 and December 1 through December 1, 2011. On or after December 1, 2007, the Certificates are subject to prepayment at the option of the District.

The following is a schedule of maturities for the certificates of participation:

Year Ending December 31,	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2007	\$ 620,000	\$ 103,488	\$ 723,488
2008	650,000	78,688	728,688
2009	690,000	52,688	742,688
2010	300,000	24,225	324,225
2011	<u>270,000</u>	<u>11,475</u>	<u>281,475</u>
	<u>\$ 2,530,000</u>	<u>\$ 270,564</u>	<u>\$ 2,800,564</u>

The District is required by its 1999 Revenue Certificates of Participation to collect rates and charges from its water system that will be sufficient to yield net revenues equal to 115% of debt service payments on any future debt issued.

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

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**NOTE E--LONG-TERM LIABILITIES (Continued)**

The advance refunding of the 1989 and 1991 Certificates of Participation resulted in differences between the reacquisition price and the net carrying amount of the outstanding debt of \$376,005 at December 31, 2006 and 2005, net of accumulated amortization of \$231,384 and \$202,461, respectively. This deferred amount on refunding, reported in the accompanying financial statements as a deduction from long-term debt, is being charged to operations over 13 years.

Capacity entitlement agreement: On November 8, 1993, the District's Board of Directors passed Resolution No. 9313 requesting SJWD to acquire and construct additional pipeline facilities to supplement the existing transmission facilities which served the District. The water rate to be charged to the District, under its contract with SJWD which ends in 2013, will include installment payments relating to Certificates of Participation executed and delivered by SJWD to acquire the project. The District's share of the amount borrowed for the project is \$3,235,163 (37.25%), with interest rates ranging from 2.0% to 4.25%. On or after February 1, 2013, the Certificates with stated maturities on or after February 1, 2014 are subject to prepayment prior to their respective stated maturities.

Future estimated debt requirements for the agreement as of December 31, 2006 are as follows:

Year Ending December 31,	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2007	\$ 184,387	\$ 49,673	\$ 234,060
2008	188,113	43,145	231,258
2009	195,562	36,938	232,500
2010	201,150	31,476	232,626
2011	206,737	25,357	232,094
2012-2013	<u>582,963</u>	<u>25,954</u>	<u>608,917</u>
	<u>\$ 1,558,912</u>	<u>\$ 212,543</u>	<u>\$ 1,771,455</u>

**NOTE F--NET ASSETS**

Restrictions: Restricted net assets consist of constraints placed on net asset use through external requirements imposed by creditors (such as through debt covenants), grantors, contributors, or laws and regulations of other governments or constraints by law through constitutional provisions or enabling legislation. Restrictions include connection and annexation fees collected for future water system capacity and debt service reserves on the 1999 Certificates of Participation.

# FAIR OAKS WATER DISTRICT

## NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

December 31, 2006 and 2005

### NOTE F--NET ASSETS (Continued)

Designations: Designations of unrestricted net assets may be imposed by the Board of Directors to reflect future spending plans or concerns about the availability of future resources. Designations may be modified, amended or removed by Board action. The following is a summary of designated net asset balances at December 31:

	<u>2006</u>	<u>2005</u>
<u>Designated for Emergency</u> : For unanticipated expenditures	\$1,000,000	\$ 990,531
<u>Designated for Fixed Asset Replacement</u> : For future improvements, acquisition and replacement of the water distribution system, well sites, tank sites, vehicles, and equipment as identified in the annual budget and rate process	4,033,604	4,537,290
<u>Designated for Rate Stabilization</u> : To offset the estimated impact of revenue fluctuations and lag effects in converting to meter based billing	1,710,759	1,324,630
<u>Designated Administrative Facility Reserve</u> : For future administrative facility improvements and acquisitions	<u>1,265,567</u>	<u>1,994,520</u>
Total Designated Net Assets	<u>\$ 8,009,930</u>	<u>\$ 8,846,971</u>

### NOTE G--EMPLOYEES' RETIREMENT PLAN

Plan Description: The District contributes to the California Public Employees Retirement System (PERS), a cost-sharing multiple-employer public employee defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments and death benefits to plan members and beneficiaries. PERS acts as a common investment and administrative agent for participating public employers within the State of California. All full and part time District employees working at least 1,000 hours per year are eligible to participate in PERS. Under PERS, benefits vest after five years of service. Upon retirement, participants are entitled to an annual retirement benefit, payable for life, in an amount equal to a benefit factor times the monthly average salary of their highest twelve consecutive months full-time equivalent monthly pay. Copies of the PERS annual financial report may be obtained from their Executive Office, 400 P Street, Sacramento, CA 95814.

Funding Policy: Active plan members are required to contribute 7% of their annual covered salary. The District makes the contributions required of District employees on their behalf and for their account. Contributions made on behalf of District employees total \$133,167 and \$124,128 for the years ended December 31, 2006 and 2005, respectively. The District is required to contribute to an actuarially determined rate; the rate for January 1 to June 30, 2006 was 4.44% and for July 1 to December 31, 2006 was 5.287%. The rate for January 1 to June 30, 2005 was zero and for July 1 to December 31, 2005 was 4.44%. The contribution requirements of plan members and the District are established and may be amended by PERS.

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

**NOTE G--EMPLOYEES' RETIREMENT PLAN (Continued)**

Annual Pension Cost: For the years ending December 31, 2006 and 2005, the District incurred an annual pension cost of \$95,772 and \$40,861, respectively. The required contribution was determined as part of the June 30, 2004 actuarial valuation using entry age actuarial cost method. The actuarial assumptions included (a) 7.75% investment rate of return (net of administrative expenses); (b) projected salary increases that vary in duration of service ranging from 3.25% to 14.45% and (c) 3.25% cost of living adjustment. Both (a) and (b) include an inflation component of 3.0%. The actuarial value of the plan's assets was determined using techniques that smooth the effects of short term volatility in the market value of investments over a three year period (smoothed market value). The plan's excess assets are being amortized as a level percentage of projected payroll on a closed basis. The remaining amortization period at June 30, 2005 was 15 years.

<u>Three-Year Trend Information for the District</u>		
<u>Fiscal</u> <u>Year</u> <u>Ending</u>	<u>Annual</u> <u>Pension</u> <u>Cost (APC)</u>	<u>Percentage</u> <u>Of APC</u> <u>Contributed</u>
December 31, 2004	\$ 0	100%
December 31, 2005	\$ 40,861	100%
December 31, 2006	\$ 95,355	100%

The funded status information for the risk pool in which the District belongs is as follows:

<u>Required Supplementary Information - Funded Status of Plan</u>						
<u>Actuarial</u> <u>Valuation</u> <u>Date</u>	<u>Actuarial</u> <u>Assets Value</u>	<u>Entry Age</u> <u>Actuarial</u> <u>Accrued</u> <u>Liability</u>	<u>Excess</u> <u>Assets</u> <u>(Unfunded</u> <u>Liability)</u>	<u>Funded</u> <u>Ratio</u>	<u>Covered</u> <u>Payroll</u>	<u>Excess Assets</u> <u>(Unfunded Liability)</u> <u>As a % of</u> <u>Covered Payroll</u>
June 30, 2003	\$ 2,372,879,034	\$ 2,596,966,545	\$ (224,087,511)	91.4%	\$ 725,020,458	(30.9%)
June 30, 2004	2,460,944,656	2,746,095,668	(285,151,012)	89.6%	743,691,970	(38.3%)
June 30, 2005	2,588,713,000	2,891,460,651	(302,747,651)	89.5%	755,046,679	(40.1%)

**NOTE H--INSURANCE**

The District participates in the Association of California Water Agencies Joint Powers Insurance Authority (ACWA/JPIA) a public entity risk pool of California water agencies, for general and auto liability, public officials liability property damage and fidelity insurance. ACWA/JPIA provides insurance through the pool up to a certain level, beyond which group-purchased commercial excess insurance is obtained.

**FAIR OAKS WATER DISTRICT**

**NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)**

**December 31, 2006 and 2005**

**NOTE H--INSURANCE (Continued)**

The District pays an annual premium to ACWA/JPIA that includes its pro-rata share of excess insurance premiums, charges for the pooled risk, claims adjusting and legal costs, and administrative and other costs to operate the ACWA/JPIA. The District's deductibles and maximum coverage are as follows:

<u>Coverage</u>	<u>ACWA/JPIA</u>	<u>Commercial Insurance</u>	<u>Deductible</u>
General and Auto Liability (includes public officials liability)	\$ 1,000,000	\$ 49,000,000	None
Property Damage	50,000	50,000,000	\$500 to 25,000
Fidelity	100,000		1,000
Workers Compensation	2,000,000	Statutory	None
Employers liability	2,000,000	Statutory	None

The District continues to carry commercial insurance for all other risks of loss to cover all claims for risk of loss to which the District is exposed. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

**NOTE I--COMMITMENTS AND CONTINGENCIES**

The District has developed a meter implementation plan that will entail installing meters at a cost of over \$17,314,000 for all District customers by approximately 2011. As of December 31, 2006, the estimated remaining cost to install meters is approximately \$10,910,000.

The District has the following capital project commitments as of December 31, 2006:

Town Well Project	\$ 836,643
Heather Well Project	<u>1,102,213</u>
Total	<u>\$1,938,856</u>

**NOTE J--ECONOMIC DEPENDENCY**

The District purchases approximately 97% of its water supplies from SJWD. During the years ended December 31, 2006 and 2005, the District's total water purchases from SJWD were \$1,062,505 and \$1,071,645, respectively.

## **ADDITIONAL INFORMATION**

**FAIR OAKS WATER DISTRICT**  
**DEBT SERVICE RATE COVENANT**

**December 31, 2006 and 2005**

In conjunction with the 1999 Certificate of Participation, the District has covenanted to fix, prescribe and collect rates and charges for the water service which will be sufficient to yield during the year net revenues equal to 115% of the debt service paid during the year. For purposes of this calculation, net revenues equals net income plus depreciation and amortization expenses. The debt service requirement for 2006 and 2005 is as follows:

	<u>2006</u>	<u>2005</u>
Operating Income	\$ 2,127,687	\$ 2,412,404
Add:		
Depreciation and Amortization	1,711,211	1,441,207
Interest Revenue	610,556	354,769
Unrealized loss on investments	4,662	26,968
Gain on disposal of capital assets	<u>11,570</u>	<u>12,190</u>
Net Revenue	4,465,686	4,247,538
 Debt Service		
Principal	773,800	750,075
Interest	<u>208,204</u>	<u>233,267</u>
Total Debt Service	<u>\$ 982,004</u>	<u>\$ 983,342</u>
 Calculated Coverage	 <u>455%</u>	 <u>432%</u>

# **COMPLIANCE REPORT**

**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER  
FINANCIAL REPORTING BASED ON AN AUDIT OF  
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH  
*GOVERNMENT AUDITING STANDARDS***

**Board of Directors  
Fair Oaks Water District  
Fair Oaks, California**

We have audited the basic financial statements of the Fair Oaks Water District (the District) of and for the year ended December 31, 2006 and have issued our report thereon dated March 6, 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.

Compliance

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*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the 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 in amounts that would be material in relation to the basic 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

Board of Directors  
Fair Oaks Water District

noted no matters involving internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting, which we have reported to management of the District in a separate letter dated March 6, 2007.

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

*Richardson & Company*

March 6, 2007



## **STATISTICAL SECTION**

**FAIR OAKS WATER DISTRICT**  
**Schedule of Net Assets by Component**  
**(Accrual Basis of Accounting)**  
**Last Nine Years**

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Net Assets:									
Invested in Capital Assets, Net of Related Debt	\$ 7,505,734	\$ 7,265,293	\$ 7,587,801	\$ 8,435,962	\$ 9,044,398	\$ 10,711,397	\$ 12,744,821	\$ 13,938,510	\$ 19,041,276
Restricted	1,706,960	971,783	868,747	921,109	1,079,144	1,230,338	1,389,828	2,052,570	1,565,938
Unrestricted	<u>4,512,401</u>	<u>6,260,016</u>	<u>7,451,378</u>	<u>8,454,256</u>	<u>9,289,608</u>	<u>10,011,710</u>	<u>9,718,605</u>	<u>11,189,727</u>	<u>10,315,265</u>
Total Net Assets	<u>\$ 13,725,095</u>	<u>\$ 14,497,092</u>	<u>\$ 15,907,926</u>	<u>\$ 17,811,327</u>	<u>\$ 19,413,150</u>	<u>\$ 21,953,445</u>	<u>\$ 23,853,254</u>	<u>\$ 27,180,807</u>	<u>\$ 30,922,479</u>

1997 information not available

Source:  
District Finance Department

**FAIR OAKS WATER DISTRICT**  
**Schedule of Changes in Net Assets (a)**  
**(Accrual Basis of Accounting)**  
**Last Ten Years**

	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
<b>Operating Revenues:</b>										
Water Sales	\$ 3,552,718	\$ 3,639,761	\$ 4,248,439	\$ 5,068,311	\$ 5,780,430	\$ 6,025,807	\$ 6,569,055	\$ 7,052,897	\$ 7,681,395	\$ 7,723,313
Water Service and Other	<u>171,883</u>	<u>92,271</u>	<u>193,919</u>	<u>145,872</u>	<u>234,725</u>	<u>284,925</u>	<u>263,387</u>	<u>135,163</u>	<u>258,148</u>	<u>231,301</u>
Total Operating Revenues	3,724,601	3,732,032	4,442,358	5,214,183	6,015,155	6,310,732	6,832,442	7,188,060	7,939,543	7,954,614
<b>Non-Operating Revenues:</b>										
Interest Revenue	400,634	430,522	391,062	510,144	464,309	265,141	192,194	170,533	354,769	610,556
Grants								30,000	15,000	0
Gain (Loss) on Disposal	<u>1,887</u>	<u>582</u>	<u>3,631</u>	<u>2,219</u>	<u>2,200</u>	<u>4,555</u>	<u>10,709</u>	<u>(4,614)</u>	<u>12,190</u>	<u>11,570</u>
Total Non-Operating Revenues	402,521	431,104	394,693	512,363	466,509	269,696	202,903	195,919	445,216	622,126
<b>Capital Revenues:</b>										
Connection Fees and Annexation Fees							263,323	158,188	695,200	169,901
Capital Contributions	-	-	-	-	235,800	295,000	504,800	289,839	8,000	-
Capital Grant Revenue	<u>-</u>	<u>63,257</u>	<u>1,030,162</u>							
Total Capital Revenues	-	-	-	-	235,800	295,000	768,123	448,027	703,200	1,200,063
Total Revenues	<u>\$ 4,127,122</u>	<u>\$ 4,163,136</u>	<u>\$ 4,837,051</u>	<u>\$ 5,726,546</u>	<u>\$ 6,717,464</u>	<u>\$ 6,875,428</u>	<u>\$ 7,803,468</u>	<u>\$ 7,832,006</u>	<u>\$ 9,087,959</u>	<u>\$ 9,776,803</u>
<b>Operating Expenses:</b>										
Water Supply and Pumping	\$ 784,952	\$ 817,910	\$ 855,186	\$ 893,682	\$ 987,537	\$ 987,140	\$ 1,066,372	\$ 1,333,038	\$ 1,285,208	\$ 1,321,268
Operations and Maintenance	899,735	860,315	917,542	1,042,020	1,275,303	1,698,240	1,496,583	1,785,638	1,405,438	1,401,320
Customer Service								337,202	432,007	399,124
Administrative and General	963,978	969,087	1,075,638	1,082,505	1,069,037	996,913	1,248,202	972,740	963,279	994,004
Depecciation and Amortization	<u>734,646</u>	<u>1,111,811</u>	<u>1,037,935</u>	<u>1,014,439</u>	<u>1,102,859</u>	<u>1,247,291</u>	<u>1,219,006</u>	<u>1,279,989</u>	<u>1,441,207</u>	<u>1,711,211</u>
Total Operating Expenses	3,383,311	3,759,123	3,886,301	4,032,646	4,434,736	4,929,584	5,030,163	5,708,607	5,527,139	5,826,927
<b>Non-Operating Expenses:</b>										
Interest Expense	<u>587,890</u>	<u>555,056</u>	<u>406,023</u>	<u>435,066</u>	<u>379,327</u>	<u>344,021</u>	<u>233,010</u>	<u>223,590</u>	<u>233,267</u>	<u>208,204</u>
Total Non-Operating Expenses	587,890	555,056	406,023	435,066	379,327	344,021	233,010	223,590	233,267	208,204
Total Expenses	<u>\$ 3,971,201</u>	<u>\$ 4,314,179</u>	<u>\$ 4,292,324</u>	<u>\$ 4,467,712</u>	<u>\$ 4,814,063</u>	<u>\$ 5,273,605</u>	<u>\$ 5,263,173</u>	<u>\$ 5,932,197</u>	<u>\$ 5,760,406</u>	<u>\$ 6,035,131</u>
Changes in Net Assets	<u>\$ 155,921</u>	<u>\$ (151,043)</u>	<u>\$ 544,727</u>	<u>\$ 1,258,834</u>	<u>\$ 1,903,401</u>	<u>\$ 1,601,823</u>	<u>\$ 2,540,295</u>	<u>\$ 1,899,809</u>	<u>\$ 3,327,553</u>	<u>\$ 3,741,672</u>

(a) The 2004 through 2005 revenues and expenses have been reclassified to reflect the current 2006 classification for comparative purposes. The 2003 and prior were not adjusted for these reclassifications.

Source:  
District Finance Department

**FAIR OAKS WATER DISTRICT**  
**Water Sales by Type of Customers (a)**  
**Last Ten Years**

	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Water Sales:										
Residential	\$ 3,552,718	\$ 3,639,761	\$ 4,248,439	\$ 5,068,311	\$ 5,780,430	\$ 5,302,791	\$ 5,721,390	\$ 6,112,407	\$ 6,757,231	\$ 6,844,879
Commercial	-	-	-	-	-	723,016	847,665	940,490	924,164	878,434
Total Water Sales	\$ 3,552,718	\$ 3,639,761	\$ 4,248,439	\$ 5,068,311	\$ 5,780,430	\$ 6,025,807	\$ 6,569,055	\$ 7,052,897	\$ 7,681,395	\$ 7,723,313
Total Water Deliveries (AF)	14,253	12,515	14,423	14,377	15,148	14,067	12,574	14,153	12,453	12,024
Rate per Acre Foot (AF)	\$ 249.26	\$ 290.83	\$ 294.56	\$ 352.53	\$ 381.60	\$ 428.36	\$ 522.43	\$ 498.33	\$ 616.83	\$ 642.32

(a) The 2001 and prior years' Commercial Revenues have been included under Residential.

Source:  
District Finance Department

**FAIR OAKS WATER DISTRICT**  
**Principal Rate Payers**  
**Current Year and Two Years Prior**

	<u>2006</u>		<u>2004</u>	
	<u>Revenues Collected</u>	<u>Percent of Total Water Sales</u>	<u>Revenues Collected</u>	<u>Percent of Total Water Sales</u>
<b>Rate Payers</b>				
San Juan School District	\$ 81,814	1.06%	\$ 68,444	0.89%
Fair Oaks Park/Recreation District	45,647	0.59%	27,153	0.35%
Bre Properties	45,167	0.58%	47,770	0.62%
Rollingwood, LLC	31,901	0.41%	64,600	0.84%
Fountains of Fair Oaks	27,135	0.35%	20,662	0.27%
Madision Hills	23,339	0.30%	27,275	0.36%
Village @ Fair Oaks	20,698	0.27%	19,024	0.25%
The Lakes at Fair Oaks	16,859	0.22%	16,426	0.21%
Huntcliff Apartments	15,449	0.20%	15,415	0.20%
Fair Oaks Lake Apartments	15,140	<u>0.20%</u>	14,217	<u>0.19%</u>
<b>Total</b>	<b>\$ 323,150</b>	<b>4.18%</b>	<b>\$ 320,986</b>	<b>4.18%</b>
<b>Total Water Sales</b>	<b>\$ 7,723,313</b>		<b>\$ 7,681,395</b>	

Information prior to 2004 was not available.

**FAIR OAKS WATER DISTRICT**  
**Ratios of Outstanding Debt by Type and Number of Connections**  
**Last Ten Years**

	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Debt:										
1999 Revenue Certificates of Participation	\$ -	\$ -	\$ 6,265,000	\$ 5,790,000	\$ 5,300,000	\$ 4,785,000	\$ 4,255,000	\$ 3,700,000	\$ 3,125,000	\$ 2,530,000
Capacity Entitlement Agreement	<u>2,905,500</u>	<u>2,788,163</u>	<u>2,667,100</u>	<u>2,540,450</u>	<u>2,408,213</u>	<u>2,270,388</u>	<u>2,119,525</u>	<u>1,912,787</u>	<u>1,737,712</u>	<u>1,558,912</u>
Total Debt	\$ 2,905,500	\$ 2,788,163	\$ 8,932,100	\$ 8,330,450	\$ 7,708,213	\$ 7,055,388	\$ 6,374,525	\$ 5,612,787	\$ 4,862,712	\$ 4,088,912
Number of Service Connections	12,952	12,988	13,090	13,217	13,441	13,588	13,554	13,577	13,544	14,467
Debt Per Capita	224.33	214.67	682.36	630.28	573.49	519.24	470.31	413.40	359.03	282.64

Source:  
District Finance Department

**FAIR OAKS WATER DISTRICT**  
**Schedule of Debt Service**  
**Last Ten Years**

	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Net Revenue	\$ 1,075,936	\$ 1,515,825	\$ 1,979,985	\$ 2,703,739	\$ 3,139,387	\$ 2,894,134	\$ 3,195,488	\$ 2,910,576	\$ 4,247,538	\$ 4,465,686
Debt Service	657,402	1,017,393	1,183,246	976,591	972,643	971,923	942,298	1,021,028	983,342	982,004
Coverage	164%	149%	167%	276%	323%	298%	339%	285%	432%	455%

Source:  
District Finance Department

**FAIR OAKS WATER DISTRICT**  
**Operating Function**  
**Last Nine Years**

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
<b>Water Services:</b>									
Number of Service Connections	12,988	13,090	13,217	13,441	13,588	13,554	13,577	13,544	14,467
Annual Demand in AF	12,515	14,423	14,377	15,148	14,067	12,574	14,153	12,453	12,024
Average Daily Demand in MGD	11.17	12.88	12.83	13.52	12.56	11.22	12.63	11.12	10.73
Maximum Day Demand in MGD	21.23	24.46	24.38	25.69	23.86	21.33	24.00	21.12	20.39
<b>Meters:</b>									
New Installations	295	383	446	457	410	484	1,025	816	947
Replacement	-	2	-	-	-	-	13	454	103
<b>Leaks:</b>									
Water Main	16	3	15	18	24	9	21	17	16
Service	54	15	54	54	70	145	92	89	66
<b>Hydrants:</b>									
New Installations	1	2	2	6	3	4	3	-	2
Upgrades	1	2	10	9	13	21	23	19	14
<b>Main Line Valves:</b>									
New Installations	10	8	10	26	33	56	18	15	17
Replacement	8	2	1	8	6	12	14	9	14
<b>Services:</b>									
New Installations	7	4	3	18	5	16	4	3	18
Replacement	36	66	88	146	323	483	612	548	857
Personnel (FTE)	29	29	29.5	29	29	35.5	39	35.50	38

1997 information not available

Source:  
District Finance Department