

Purissima Hills Water District

Annual Financial Report

For the Fiscal Years Ended June 30, 2010 and 2009

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Service to the Hills Since 1955

Purissima Hills Water District Board of Directors as of June 30, 2010

<u>Name</u>	<u>Title</u>	<u>Elected/ Appointed</u>	<u>Current Term</u>
Gary C. Waldeck	President	Elected	12/06-12/10
Robert N. Anderson	Vice President	Elected	12/06-12/10
Brian Holtz	Director	Elected	12/08-12/12
Stephen A. Jordan	Director	Apointed	12/08-12/12
Ernest Solomon	Director	Elected	12/08-12/12

**Purissima Hills Water District
Patrick Walter, General Manager
26375 Fremont Road
Los Altos Hills, California 94022
(650) 948-1217 – www.purissimawater.org**

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Annual Financial Report
For the Fiscal Years Ended June 30, 2010 and 2009**

Table of Contents

	<u>Page No.</u>
Table of Contents	i
Introductory Section	
Letter of Transmittal	1-3
Financial Section	
Independent Auditor's Report	4
Management's Discussion and Analysis	5-8
Basic Financial Statements:	
Statements of Net Assets	9
Statements of Revenues, Expenses and Changes in Net Assets	10
Statements of Cash Flows	11-12
Notes to the Basic Financial Statements	13-23
Report on Internal Controls and Compliance	
Independent Auditor's Report on Internal Control Over Financial Reporting And on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	24

Introductory Section

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September 10, 2010

Board of Directors
Purissima Hills Water District

Introduction

It is our pleasure to submit the Annual Financial Report for the Purissima Hills Water District (District) for the fiscal years ended June 30, 2010 and 2009, following guidelines set forth by the Governmental Accounting Standards Board. District staff prepared this financial report. The District is ultimately responsible for both the accuracy of the data and the completeness and the fairness of presentation, including all disclosures in this financial report. We believe that the data presented is accurate in all material respects. This report is designed in a manner that we believe necessary to enhance your understanding of the District's financial position and activities.

This report is organized into two sections: (1) Introductory and (2) Financial. The Introductory section offers general information about the District's organization and current District activities and reports on a summary of significant financial results. The Financial section includes the Independent Auditors' Report, Management's Discussion and Analysis of the District's basic financial statements, and the District's audited basic financial statements with accompanying Notes.

Generally Accepted Accounting Principles (GAAP) requires that management provide a narrative introduction, overview and analysis to accompany the financial statements in the form of the Management's Discussion and Analysis (MD&A) section. This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. The District's MD&A can be found immediately after the Independent Auditors' Report.

District Structure and Leadership

The Purissima Hills Water District is an independent special district, which operates under the authority of Division 12 of the California Water Code. The District was formed in 1955 and is governed by a five-member Board of Directors, elected at-large from within the District's service area. The General Manager administers the day-to-day operations of the District in accordance with policies and procedures established by the Board of Directors. The District employs approximately nine regular employees, five in the field, three in the office and a conservation coordinator. The District's Board of Directors meets each month. Meetings are publicly noticed and citizens are encouraged to attend.

District Services

The Purissima Hills Water District provides service to two-thirds of the Town of Los Altos Hills, a rural community adjacent to the cities of Palo Alto and Los Altos, and unincorporated areas in Santa Clara County to the south. The District serves predominantly single-family homes on minimum one-acre lots. The District's largest customer is Foothill College.

District Services, continued

Purissima Hills Water District receives 100% of its water supply from San Francisco Public Utilities Commission (SFPUC) via two turnouts from the Hetch Hetchy pipeline along the Foothill Expressway on the northern edge of the District. The SFPUC water supply is gravity-fed through 18" transmission mains to two pump stations that pump to tanks distributed throughout the District. The distribution system consists of 4 pressure zones, 10 tanks, 5 pumping stations, 14 pumps, and 80 miles of pipeline. All services within the District are pressurized or gravity fed from tanks in the respective pressure zones. The tanks have a total capacity of 10 million gallons.

Economic Condition and Outlook

The District office is located in the City of Los Altos Hills in Santa Clara County which has experienced significant economic growth within the region. The economic outlook for the Northern California region is one of cautious growth due to the prolonged real estate correction, the financial crisis that may impact customers, suppliers, and the California State budget deficit that may impact collection of property tax revenues which is projected to continue through fiscal year 2011.

Internal Control Structure

District management is responsible for the establishment and maintenance of the internal control structure that ensures the assets of the District are protected from loss, theft or misuse. The internal control structure also ensures adequate accounting data is compiled to allow for the preparation of financial statements in conformity with generally accepted accounting principles. The District's internal control structure is designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that (1) the cost of a control should not exceed the benefits likely to be derived, and (2) the valuation of costs and benefits requires estimates and judgments by management.

Budgetary Control

The District's Board of Directors annually adopts an operating and capital budget prior to the new fiscal year. The budget authorizes and provides the basis for reporting and control of financial operations and accountability for the District's enterprise operations and capital projects. The budget and reporting treatment applied to the District is consistent with the accrual basis of accounting and the financial statement basis.

Investment Policy

The Board of Directors has adopted an investment policy that conforms to state law, District ordinance and resolutions, prudent money management, and the "prudent person" standards. The objective of the Investment Policy is safety, liquidity and yield. District funds are invested in the State Treasurer's Local Agency Investment Fund and an institutional checking account.

Water Rates and District Revenues

District policy direction ensures that all revenues from user charges and surcharges generated from District customers must support all District operations including capital project funding. Accordingly, water rates are reviewed on an annual basis. Water rates are user charges imposed on customers for services and are the primary component of the District's revenue. Water rates are composed of a commodity (usage) charge and a fixed meter standby charge.

Audit and Financial Reporting

State Laws require the District to obtain an annual audit of its financial statements by an independent certified public accountant. The accounting firm of Charles Z. Fedak & Company, CPAs has conducted the audit of the District's financial statements. Their unqualified Independent Auditor's Report appears in the Financial Section.

Other References

More information is contained in the Management's Discussion and Analysis and the Notes to the Basic Financial Statements found in the Financial Section of the report.

Acknowledgements

Preparation of this report was accomplished by the combined efforts of District staff. We appreciate the dedicated efforts and professionalism that these staff members contribute to the District. We would also like to thank the members of the Board of Directors for their continued support in planning and implementation of the Purissima Hills Water District's fiscal policies.

Respectfully submitted,

Patrick Walter
General Manager

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Financial Section

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Independent Auditor's Report

Board of Directors
Purissima Hills Water District
Los Altos Hills, California

We have audited the accompanying financial statements of the Purissima Hills Water District (District) as of and for the fiscal years ended June 30, 2010 and 2009, which collectively comprise the District's basic financial statements as listed in the table of contents. These basic financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these basic financial statements based on our audits.

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

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the respective financial position of the Purissima Hills Water District as of June 30, 2010 and 2009, and the respective changes in net assets and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated September 10, 2010 on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit. This report can be found on page 25.

Management's discussion and analysis on pages 5 through 8 are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit this information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the District's basic financial statements. The accompanying introductory section on pages 1 through 3 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The introductory section 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.

September 10, 2010
Cypress, California

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Purissima Hills Water District
Management's Discussion and Analysis
For the Fiscal Years Ended June 30, 2010 and 2009

The following Management's Discussion and Analysis (MD&A) of activities and financial performance of the Purissima Hills Water District (District) provides an introduction to the financial statements of the District for the fiscal years ended June 30, 2010 and 2009. The two year presentation is provided for comparative purposes. We encourage readers to consider the information presented here in conjunction with the transmittal letter in the Introductory Section and with the basic financial statements and related notes, which follow this section.

Financial Highlights

- The District's net assets increased 1.3% or \$257,122 to \$19,429,539 in fiscal year 2010 primarily due to the increase in contributed capital of \$252,969. In 2009, the District's net assets increased 4.6% or \$833,845 to \$19,172,417 primarily due to operating revenues over expenses of \$45,228 combined with non-operating income of \$788,618.
- The District's operating revenues decreased 9.6% or \$387,597 in 2010 primarily due to a 13% reduction in consumption demand that was partially offset by a rate increase effective in March 2010. In 2009, the District's operating revenues increased 3.5% or \$137,291 in 2009 of which \$81,965 is attributed to the full year's effect of a rate increase which was offset by reduced consumption from prior year levels.
- The District's operating expenses increased 14.8% or \$497,432 in 2010 primarily due to increases in transmission and distribution expenses of \$285,303 and general and administration expenses of \$157,134. In 2009, the District's operating expenses decreased 2.8% or \$98,314 in 2009 primarily due to a decrease in water acquisition costs of \$56,706 as the result of lower demand and maintenance costs of \$91,843, which were offset by an increase in administration costs of \$61,835.

Required Financial Statements

This annual report consists of a series of financial statements. The Statement of Net Assets, Statement of Revenues, Expenses and Changes in Net Assets and Statement of Cash Flows provide information about the activities and performance of the District using accounting methods similar to those used by private sector companies.

The Statement of Net Assets includes all of the District's investments in resources (assets) and the obligations to creditors (liabilities). It also provides the basis for computing a rate of return, evaluating the capital structure of the District and assessing the liquidity and financial flexibility of the District. All of the current year's revenue and expenses are accounted for in the Statement of Revenues, Expenses and Changes in Net Assets. This statement measures the success of the District's operations over the past year and can be used to determine if the District has successfully recovered all of its costs through its rates and other charges. This statement can also be used to evaluate profitability and credit worthiness. The final required financial statement is the Statement of Cash Flows, which provides information about the District's cash receipts and cash payments during the reporting period. The Statement of Cash Flows reports cash receipts, cash payments and net changes in cash resulting from operations, investing, non-capital financing, and capital and related financing activities and provides answers to such questions as where did cash come from, what was cash used for, and what was the change in cash balance during the reporting period.

Financial Analysis of the District

One of the most important questions asked about the District's finances is, "Is the District better off or worse off as a result of this year's activities?" The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets report information about the District in a way that helps answer this question.

Purissima Hills Water District
Management's Discussion and Analysis
For the Fiscal Years Ended June 30, 2010 and 2009

Financial Analysis of the District, continued

These statements include all assets and liabilities using the *accrual basis of accounting*, which is similar to the accounting method used by most private sector companies. All of the current year's revenues and expenses are taken into account regardless of when the cash is received or paid.

These two statements report the District's *net assets* and changes in them. You can think of the District's net assets – the difference between assets and liabilities – as one way to measure the District's financial health, or *financial position*. Over time, *increases or decreases* in the District's net assets are one indicator of whether its *financial health* is improving or deteriorating. However, one will need to consider other non-financial factors such as changes in economic conditions, population growth, zoning and new or changed government legislation, such as changes in Federal and State water quality standards.

Notes to the Basic Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the basic financial statements can be found on pages 13 through 23.

Statement of Net Assets

Condensed Statements of Net Assets			
	2010	2009	Change
Assets:			
Current assets	\$ 3,110,359	1,832,991	1,277,368
Non-current assets	44,049	-	44,049
Capital assets, net	18,972,301	17,785,686	1,186,615
Total assets	22,126,709	19,618,677	2,508,032
Liabilities:			
Current liabilities	1,097,170	446,260	650,910
Non-current liabilities	1,600,000	-	1,600,000
Total liabilities	2,697,170	446,260	2,250,910
Net assets:			
Net investment in capital assets	16,972,301	17,697,387	(725,086)
Restricted for capital improvement	454,846	-	454,846
Unrestricted	2,002,392	1,475,030	527,362
Total net assets	19,429,539	19,172,417	257,122
Total liabilities and net assets	\$ 22,126,709	19,618,677	2,508,032

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the District, assets of the District exceeded liabilities by \$19,429,539 and \$19,172,417 as of June 30, 2010 and June 30, 2009, respectively.

By far the largest portion of the District's net assets (87% as of June 30, 2010 and 92% as of June 30, 2009) reflects the District's investment in capital assets (net of accumulated depreciation) less any related debt used to acquire those assets that is still outstanding. The District uses these capital assets to provide services to customers within the District's service area; consequently, these assets are not available for future spending.

At the end of fiscal years 2010 and 2009, the District showed a balance in its restricted net assets of \$454,846 and \$0, respectively, which may be utilized in future years for capital improvements.

Purissima Hills Water District
Management's Discussion and Analysis
For the Fiscal Years Ended June 30, 2010 and 2009

Statement of Net Assets, continued

At the end of fiscal years 2010 and 2009, the District showed a positive balance in its unrestricted net assets of \$2,002,392 and \$1,475,030, respectively, which may be utilized in future years. See note 8 for further discussion.

Statement of Revenues, Expenses and Changes in Net Assets

Condensed Statements of Revenues, Expenses and Changes in Net Assets

	<u>2010</u>	<u>2009</u>	<u>Change</u>
Revenues:			
Operating revenues	\$ 3,641,276	4,028,873	(387,597)
Non-operating revenues	732,714	724,829	7,885
Total revenues	<u>4,373,990</u>	<u>4,753,702</u>	<u>(379,712)</u>
Expenses:			
Operating expenses	3,854,093	3,356,661	497,432
Depreciation and amortization	597,856	626,984	(29,128)
Non-operating expenses	1,678	20,002	(18,324)
Total expenses	<u>4,453,627</u>	<u>4,003,647</u>	<u>449,980</u>
Net income before capital contributions	<u>(79,637)</u>	<u>750,055</u>	<u>(829,692)</u>
Capital contributions	<u>336,759</u>	<u>83,790</u>	<u>252,969</u>
Change in net assets	<u>257,122</u>	<u>833,845</u>	<u>(576,723)</u>
Net assets, beginning of year	<u>19,172,417</u>	<u>18,338,572</u>	<u>833,845</u>
Net assets, end of year	<u>\$ 19,429,539</u>	<u>19,172,417</u>	<u>257,122</u>

The statement of revenues, expenses and changes of net assets shows how the District's net assets changed during the fiscal years. In the case of the District, net assets increased by \$257,122 and \$833,845 for the fiscal years ended June 30, 2010 and 2009, respectively.

A closer examination of the sources of changes in net assets reveals that:

In 2010 the District's total revenues decreased by \$379,712 due primarily to a \$387,597 or 9.6% decrease in operating revenues attributed to a 13% reduction in water consumption that was partially offset by a rate increase effective March 2010. The District's operating expenses increased 14.8% or \$497,432 primarily due to increases in transmission and distribution expenses of \$285,303 and general and administration expenses of \$157,134.

In 2009 the District's total revenues increased by \$149,928 due primarily to a \$137,291 or 3.5% increase in operating revenues of which \$81,965 is attributed to the full year's effect of a rate increase which was offset by reduced consumption from prior year levels. Also, the District's operating expenses decreased 2.8% or \$98,314 primarily due to a decrease in water acquisition costs of \$56,706 as the result of lower demand and maintenance costs of \$91,843, which were offset by an increase in administration costs of \$61,835.

Capital Asset Administration

At the end of fiscal year 2010 and 2009, the District's investment in capital assets amounted to \$18,972,301 and \$17,785,686 (net of accumulated depreciation), respectively. This investment in capital assets includes land, transmission and distribution systems, tanks, pumps, buildings, equipment, vehicles and construction-in-process, etc. Major capital assets additions during the year include improvements to portions the District's transmission and distribution system.

Purissima Hills Water District
Management's Discussion and Analysis
For the Fiscal Years Ended June 30, 2010 and 2009

Capital Asset Administration, continued

	<u>Balance 2009</u>	<u>Additions</u>	<u>Transfers/ Deletions</u>	<u>Balance 2010</u>
Capital assets:				
Non-depreciable assets	\$ 1,002,241	1,784,471	(902,555)	1,884,157
Depreciable assets	25,680,581	902,555	-	26,583,136
Accumulated depreciation and amortization	(8,897,136)	(597,856)	-	(9,494,992)
Total capital assets ,net	<u>\$ 17,785,686</u>	<u>2,089,170</u>	<u>(902,555)</u>	<u>18,972,301</u>

Changes in capital assets amounts for 2009 were as follows:

	<u>Balance 2008</u>	<u>Additions</u>	<u>Transfers/ Deletions</u>	<u>Balance 2009</u>
Capital assets:				
Non-depreciable assets	\$ 616,983	1,278,201	(892,943)	1,002,241
Depreciable assets	24,789,998	904,227	(13,644)	25,680,581
Accumulated depreciation and amortization	(8,272,062)	(626,984)	1,910	(8,897,136)
Total capital assets ,net	<u>\$ 17,134,919</u>	<u>1,555,444</u>	<u>(904,677)</u>	<u>17,785,686</u>

Debt Administration

Changes in long-term debt amounts for 2010 were as follows:

	<u>Balance 2009</u>	<u>Additions</u>	<u>Transfers/ Deletions</u>	<u>Balance 2010</u>
Long-term debt:				
Installment loan payable	\$ 88,299	-	(88,299)	-
LAHCFD loan payable	-	2,000,000	-	2,000,000
Total long-term debt	<u>\$ 88,299</u>	<u>2,000,000</u>	<u>(88,299)</u>	<u>2,000,000</u>

Changes in long-term debt amounts for 2009 were as follows:

	<u>Balance 2008</u>	<u>Additions</u>	<u>Transfers/ Deletions</u>	<u>Balance 2009</u>
Long-term debt:				
Loan payable	\$ 258,799	-	(170,500)	88,299
Total long-term debt	<u>\$ 258,799</u>	<u>-</u>	<u>(170,500)</u>	<u>88,299</u>

Conditions Affecting Current Financial Position

Management is unaware of any conditions which could have a significant impact on the District's current financial position, net assets or operating results based on past, present and future events.

Requests for Information

This financial report is designed to provide the District's funding sources, customers, stakeholders and other interested parties with an overview of the District's financial operations and financial condition. Should the reader have questions regarding the information included in this report or wish to request additional financial information, please contact the District's General Manager at 26375 Fremont Road, Los Altos Hills, CA 94022.

Basic Financial Statements

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Purissima Hills Water District
Statements of Net Assets
June 30, 2010 and 2009

<i>Assets</i>	2010	2009
Current assets:		
Cash and cash equivalents (note 2)	\$ 1,831,611	998,269
Restricted – cash and cash equivalents (note 2)	454,846	-
Accrued interest receivable	2,739	3,015
Accounts receivable – water sales and services	415,349	435,727
Accounts receivable – other	8,238	810
Water in storage inventory	11,356	8,903
Materials and supplies inventory	351,234	341,222
Prepaid expenses and deposits	34,986	45,045
Total current assets	<u>3,110,359</u>	<u>1,832,991</u>
Non-current assets:		
Note receivable - property tax from State (note 3)	44,049	-
Capital assets, net (note 4)	18,972,301	17,785,686
Total non-current assets	<u>19,016,350</u>	<u>17,785,686</u>
Total assets	<u>\$ 22,126,709</u>	<u>19,618,677</u>
<i>Liabilities and Net Assets</i>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 532,304	304,158
Accrued salaries and wages	5,879	5,280
Customer deposits and deferred revenue	40,936	37,175
Accrued interest on long-term debt	-	1,049
Contractor retention	107,662	-
Long-term liabilities - due within one year:		
Compensated absences (note 5)	10,389	10,299
Long-term debt - current portion (note 6)	400,000	88,299
Total current liabilities	<u>1,097,170</u>	<u>446,260</u>
Non-current liabilities:		
Long-term liabilities - due in more than one year:		
Long-term debt (note 6)	1,600,000	-
Total non-current liabilities	<u>1,600,000</u>	<u>-</u>
Total liabilities	<u>2,697,170</u>	<u>446,260</u>
Net assets: (note 8)		
Net investment in capital assets	16,972,301	17,697,387
Restricted for capital improvement	454,846	-
Unrestricted	2,002,392	1,475,030
Total net assets	<u>19,429,539</u>	<u>19,172,417</u>
Total liabilities and net assets	<u>\$ 22,126,709</u>	<u>19,618,677</u>

See accompanying notes to the basic financial statements

Purissima Hills Water District
Statements of Revenues, Expenses and Changes in Net Assets
For the Fiscal Years Ended June 30, 2010 and 2009

	2010	2009
Operating revenues:		
Water consumption sales	\$ 3,069,495	3,462,291
Service charges	476,447	474,339
Other charges	95,334	92,243
Total operating revenues	3,641,276	4,028,873
Operating expenses:		
Source of supply	1,519,378	1,439,445
Pumping	227,844	256,203
Transmission and distribution	1,074,858	789,555
Water treatment	16,724	14,068
Customer accounts	82,775	82,010
General and administrative	932,514	775,380
Total operating expenses	3,854,093	3,356,661
Operating income before depreciation and amortization	(212,817)	672,212
Depreciation and amortization	(597,856)	(626,984)
Operating income (loss)	(810,673)	45,228
Non-operating revenue (expense)		
Property taxes	552,918	549,776
Rental income – cellular antennas	170,758	156,181
Investment earnings and interest	9,038	18,872
Interest expense – long-term debt	(1,678)	(8,268)
Loss on disposition of capital assets	-	(11,734)
Total non-operating revenues, net	731,036	704,827
Net income before capital contributions	(79,637)	750,055
Capital contributions:		
Connection fees	86,759	83,790
Contributed capital - Fire Department	250,000	-
Total capital contributions	336,759	83,790
Change in net assets	257,122	833,845
Net assets, beginning of year	19,172,417	18,338,572
Net assets, end of year	\$ 19,429,539	19,172,417

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See accompanying notes to the basic financial statements

Purissima Hills Water District
Statements of Cash Flows
For the Fiscal Years Ended June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Cash flows from operating activities:		
Cash receipts from customers for water sales and services	\$ 3,610,177	4,011,674
Cash paid to employees for salaries and wages	(933,422)	(889,344)
Cash paid to vendors and suppliers for materials and services	<u>(2,690,481)</u>	<u>(2,661,045)</u>
Net cash (used) provided by operating activities	<u>(13,726)</u>	<u>461,285</u>
Cash flows from non-capital financing activities:		
Proceeds from rental income – cellular antennas	170,758	156,181
Proceeds from property taxes	<u>552,918</u>	<u>549,776</u>
Net cash provided by non-capital financing activities	<u>723,676</u>	<u>705,957</u>
Cash flows from capital and related financing activities:		
Acquisition and construction of capital assets	(1,784,471)	(1,289,485)
Proceeds from contractor retentions	107,662	-
Capital contributions	336,759	83,790
Proceeds from long-term debt	2,000,000	-
Principal paid on long-term debt	(88,299)	(170,500)
Interest paid on long-term debt	<u>(2,727)</u>	<u>(10,292)</u>
Net cash provided by (used) in capital and related financing activities	<u>568,924</u>	<u>(1,386,487)</u>
Cash flows from investing activities:		
Interest earnings	<u>9,314</u>	<u>21,032</u>
Net cash provided by investing activities	<u>9,314</u>	<u>21,032</u>
Net increase(decrease) in cash and cash equivalents	1,288,188	(198,213)
Cash and cash equivalents, beginning of year	<u>998,269</u>	<u>1,196,482</u>
Cash and cash equivalents, end of year	<u>\$ 2,286,457</u>	<u>998,269</u>
Reconciliation of cash and cash equivalents to statements of financial position:		
Cash and cash equivalents	\$ 1,831,611	998,269
Restricted – cash and cash equivalents	<u>454,846</u>	<u>-</u>
Total cash and cash equivalents	<u>\$ 454,846</u>	<u>998,269</u>

Continued on next page

See accompanying notes to the basic financial statements

Purissima Hills Water District
Statements of Cash Flows, continued
For the Fiscal Years Ended June 30, 2010 and 2009

	<u>2009</u>	<u>2008</u>
Reconciliation of operating income (loss) to net cash (used) provided		
by operating activities:		
Operating income (loss)	\$ <u>(810,673)</u>	<u>45,228</u>
Adjustments to reconcile operating income (loss) to net cash (used) provided		
by operating activities:		
Depreciation and amortization	597,856	626,984
Changes in assets and liabilities:		
(Increase) Decrease in assets:		
Accounts receivable	12,950	(17,199)
Inventory	(12,465)	(79,182)
Prepaid expenses and deposits	10,059	(5,616)
Note receivable	(44,049)	-
Increase (Decrease) in liabilities:		
Accounts payable and accrued expenses	228,146	(123,998)
Accrued salaries and wages	599	(3,534)
Compensated absences	90	2,894
Customer deposits and deferred revenue	<u>3,761</u>	<u>15,708</u>
Total adjustments	<u>796,947</u>	<u>416,057</u>
Net cash (used) provided by operating activities	\$ <u><u>(13,726)</u></u>	<u><u>461,285</u></u>

See accompanying notes to the basic financial statements

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Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

(1) Reporting Entity and Summary of Significant Accounting Policies

A. Organization and Operations of the Reporting Entity

The Purissima Hills Water District (District) was formed in 1955 and provides service to two-thirds of the Town of Los Altos Hills, a rural community adjacent to the cities of Palo Alto and Los Altos, and unincorporated areas in Santa Clara County to the south. The District serves predominantly single-family homes on minimum one-acre lots. The District's largest customer is Foothill College. The District is governed by a five-member Board of Directors who serve four year terms.

Purissima Hills Water District receives 100% of its water supply from San Francisco Public Utilities Commission (SFPUC) via two turnouts from the Hetch Hetchy pipeline along the Foothill Expressway on the northern edge of the District. The SFPUC water supply is gravity-fed through 18" transmission mains to two pump stations that pump to tanks distributed throughout the District. The distribution system consists of 4 pressure zones, 10 tanks, 5 pumping stations, 14 pumps, and 80 miles of pipe. All services within the District are pressurized or gravity fed from tanks in the respective pressure zones. The tanks have a total capacity of 10 million gallons.

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

B. Basis of Accounting and Measurement Focus

The District reports its activities as an enterprise fund, which is used to account for operations that are financed and operated in a manner similar to a private business enterprise, where the intent of the District is that the costs of providing water to its service area on a continuing basis be financed or recovered primarily through user charges (water sales), capital grants and similar funding. Revenues and expenses are recognized on the full accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred, regardless of when the related cash flows take place.

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

C. Financial Reporting

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

Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

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

C. Financial Reporting

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

Under GASB No. 34, enterprise funds, such as the District, have the option of consistently following or not following pronouncements issued by the Financial Accounting Standards Board (FASB) subsequent to November 30, 1989. The District has elected not to follow FASB standards issued after that date, unless such standards are specifically adopted by GASB.

D. Assets, Liabilities and Net Assets

1. Use of Estimates

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

2. Cash and Cash Equivalents

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

3. Investments

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

4. Accounts Receivable and Allowance for Uncollectible Accounts

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

5. Property Taxes and Assessments

The Santa Clara County Assessor's Office assesses all real and personal property within the County each year. The Santa Clara County Tax Collector's Offices bills and collects the District's share of property taxes and assessments. The Santa Clara County Treasurer's Office remits current and delinquent property tax collections to the District throughout the year. Property tax in California is levied in accordance with Article 13A of the State Constitution at one percent (1%) of countywide assessed valuations.

Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

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

D. Assets, Liabilities and Net Assets, continued

Property taxes receivable at year-end are related to property taxes collected by the Santa Clara County which have not been credited to the District's cash balance as of June 30. The property tax calendar is as follows:

Lien date	March 1
Levy date	July 1
Due dates	November 1 and March 1
Collection dates	December 10 and April 10

6. Materials and Supplies Inventory

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

7. Prepaid Expenses

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

8. Compensated Absences

The District's policy is to permit employees to accumulate earned vacation up to a total of 240 hours with amounts exceeding the limit being paid out as part of the employee's regular compensation. Upon termination of employment, employees are paid all unused vacation and forfeit any unused sick time.

9. Water Sales

Water sales are billed on a monthly cyclical basis.

10. Capital Contributions

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

11. Capital Assets

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

- Transmission and distribution mains – 33 to 50 years
- Buildings – 33 years
- Transportation and other equipment – 10 years
- Computer and office equipment – 5 years

Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

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

D. Assets, Liabilities and Net Assets, continued

12. Budgetary Policies

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

13. Net Assets

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

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

(2) Cash and Investments

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

	2010	2009
Cash and cash equivalents	\$ 1,831,611	998,269
Restricted for capital improvement	454,846	-
Total	\$ 2,286,457	998,269

Cash and cash equivalents as of June 30, consist of the following:

	2010	2009
Petty cash	\$ 758	32
Deposits with financial institutions	306,810	278,533
Local Agency Investment Fund (LAIF)	1,978,889	719,704
Total cash and cash equivalents	\$ 2,286,457	998,269

Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

(2) Cash and Investments, continued

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

The table below identifies the investment types that are authorized by the District in accordance with the California Government Code (or the District's investment policy, where more restrictive). The table also identifies certain provisions of 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.

Authorized Investment Type	Maximum Maturity	Maximum Percentage Of Portfolio	Maximum Investment in One Issuer
U.S. Treasury obligations	5 years	None	None
Federal agency and bank obligations	5 years	None	None
Certificates-of-deposit (negotiable or placed)	5 years	30%	10%
Commercial paper (prime)	270 days	10%	10%
Money market mutual funds	N/A	20%	None
State and local bonds, notes and warrants	N/A	None	None
California Local Agency Investment Fund (LAIF)	N/A	None	None

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 California Government Code and the District's investment policy does 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. The District had deposits with bank balances of \$327,407 and \$292,196 as of June 30, 2010 and 2009, respectively. Of the bank balances, up to \$250,000 at June 30, 2010 and at June 30, 2009 were federally insured and the remaining balance is collateralized in accordance with the Code; however, the collateralized securities are not held in the District's name.

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 Code and the District's investment policy contains legal and policy requirements that would limit the exposure to custodial credit risk for investments. With respect to investments, custodial credit risk generally applies only to direct investments in marketable securities. Custodial credit risk does not apply to a local government's indirect investment in securities through the use of mutual funds or government investment pools (such as LAIF).

Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

(2) Cash and Investments, continued

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

Investment in State Investment Pool

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

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. One of the ways that the District manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio matures or comes close to maturity evenly over time as necessary to provide for cash flow requirements and liquidity needed for operations.

Credit Risk

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.

Concentration of Credit Risk

The District's investment policy contains no limitations on the amounts that can be invested in any one issuer as beyond that stipulated by the California Government Code. There were no investments in any one issuer (other than for U.S. Treasury securities, mutual funds, and external investment pools) that represent 5% or more of total District's investments at June 30, 2010 and 2009, respectively.

(3) Note Receivable – Property Tax from State

Under the provisions of the State of California Proposition 1A and as part of the 2010 fiscal year State of California budget package passed by the California State Legislature on July 28, 2009, the State of California borrowed 8.0% of the amount of property tax revenue apportioned to cities, counties and special districts. The State of California is required to repay this borrowing plus interest by June 30, 2013. After repayment of this initial borrowing, the California State Legislature may consider only one additional borrowing within a ten-year period. The amount of the borrowing pertaining to the District was \$44,049. The borrowing by the State of California was recognized as a note receivable in the accompanying financial statements.

Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

(4) Capital Assets

Changes in capital assets for 2010 were as follows:

	<u>Balance 2009</u>	<u>Additions/ Transfers</u>	<u>Deletions/ Transfers</u>	<u>Balance 2010</u>
Non-depreciable assets:				
Land & land rights	\$ 180,099	-	-	180,099
Construction-in-process	822,142	1,784,471	(902,555)	1,704,058
Total non-depreciable assets	<u>1,002,241</u>	<u>1,784,471</u>	<u>(902,555)</u>	<u>1,884,157</u>
Depreciable assets:				
Supply plant	468,703	-	-	468,703
Pumping plant	1,662,361	885,181	-	2,547,542
Transmission and distribution mains	21,276,058	-	-	21,276,058
General plant and equipment	2,273,459	17,374	-	2,290,833
Total depreciable assets	25,680,581	902,555	-	26,583,136
Accumulated depreciation and amortization	<u>(8,897,136)</u>	<u>(597,856)</u>	<u>-</u>	<u>(9,494,992)</u>
Total depreciable assets, net	<u>16,783,445</u>	<u>304,699</u>	<u>-</u>	<u>17,088,144</u>
Total capital assets, net	<u>\$ 17,785,686</u>			<u>18,972,301</u>

Major capital assets additions during the year include upgrades and extensions of the District's transmission and distribution systems mains.

Changes in capital assets for 2009 were as follows:

	<u>Balance 2008</u>	<u>Additions/ Transfers</u>	<u>Deletions/ Transfers</u>	<u>Balance 2009</u>
Non-depreciable assets:				
Land & land rights	\$ 180,099	-	-	180,099
Construction-in-process	436,884	1,278,201	(892,943)	822,142
Total non-depreciable assets	<u>616,983</u>	<u>1,278,201</u>	<u>(892,943)</u>	<u>1,002,241</u>
Depreciable assets:				
Supply plant	468,703	-	-	468,703
Pumping plant	1,662,361	-	-	1,662,361
Transmission and distribution mains	20,443,301	846,401	(13,644)	21,276,058
General plant and equipment	2,215,633	57,826	-	2,273,459
Total depreciable assets	24,789,998	904,227	(13,644)	25,680,581
Accumulated depreciation and amortization	<u>(8,272,062)</u>	<u>(626,984)</u>	<u>1,910</u>	<u>(8,897,136)</u>
Total depreciable assets, net	<u>16,517,936</u>	<u>277,243</u>	<u>(11,734)</u>	<u>16,783,445</u>
Total capital assets, net	<u>\$ 17,134,919</u>			<u>17,785,686</u>

Major capital assets additions during the year include upgrades and extensions of the District's transmission and distribution systems mains.

Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

(4) Capital Assets, continued

Construction-In-Process

The District is involved in various construction projects throughout the year. Once completed, projects are capitalized and depreciated over the life of the asset. The balance of construction-in-process was \$1,704,058 and \$822,142 at June 30, 2010 and 2009, respectively.

(5) Compensated Absences

The changes to compensated absences balances at June 30, were as follows:

<u>Balance 2009</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance 2010</u>
\$ 10,299	52,088	(51,998)	10,389
<u>Balance 2008</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance 2009</u>
\$ 7,405	48,856	(45,962)	10,299

(6) Long-Term Debt

Changes in long-term debt amounts for 2010 were as follows:

	<u>Balance 2009</u>	<u>Additions</u>	<u>Transfers/ Deletions</u>	<u>Balance 2010</u>
Long-term debt:				
Installment loan payable	\$ 88,299	-	(88,299)	-
LAHCFD loan payable	-	2,000,000	-	2,000,000
Total loans payable	88,299	2,000,000	(88,299)	2,000,000
Less: current portion due	(88,299)			(400,000)
Long-term portion due	\$ -			1,600,000

Changes in long-term debt amounts for 2009 were as follows:

	<u>Balance 2008</u>	<u>Additions</u>	<u>Transfers/ Deletions</u>	<u>Balance 2009</u>
Long-term debt:				
Loan payable	\$ 258,799	-	(170,500)	88,299
Total loans payable	258,799	-	(170,500)	88,299
Less: current portion due	(170,500)			(88,299)
Long-term portion due	\$ 88,299			-

Installment Loan

In 2007, the Purissima Hills Water District entered into installment sales contract with the Municipal Finance Corporation for a \$500,000, 3-year loan to assist in financing the construction of capital improvements and is scheduled to mature in 2010. Principal and interest payments of \$90,396 are payable semi-annually on March 29th and September 29th each year at a rate of 4.75%. At June 30, 2010 the Installment Loan was paid in full.

Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

(6) Long-Term Debt, continued

Los Altos Hills County Fire District Loan

In 2010, the Purissima Hills Water District entered into \$2,000,000 loan payable agreement with the Los Altos Hills County Fire District (LAHCFD) to assist in financing the construction of the Zone 2-1/2 Phase II and III mains project. Terms of the agreement provide for principal and interest payments payable semi-annually on July 15th and October 15th of each year maturing in 2015. Interest is calculated based on the Local Agency Investment Fund average monthly effective yield rate.

Principal and estimated interest payments are as follows:

<u>Fiscal Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2011	\$ 400,000	8,777	408,777
2012	400,000	6,698	406,698
2013	400,000	4,577	404,577
2014	400,000	2,465	402,465
2015	400,000	353	400,353
Total	2,000,000	22,870	2,022,870
Less current portion	(400,000)		
Total non-current	\$ 1,600,000		

(7) Defined Benefit Pension Plan

Plan Description

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

Funding Policy

The contribution rate for plan members in the CalPERS, 2.0% at 60 Risk Pool Retirement Plan is 7% of their annual covered salary and is paid by the District in lieu of approved COLA increases from 1998 to 2000. The District makes these contributions required of District employees on their behalf and for their account. Also, the District is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The required employer contribution rates are equal to the annual pension costs (APC) percentage of payroll for fiscal years 2010, 2009 and 2008 as noted below. The contribution requirements of the plan members are established by State statute, and the employer contribution rate is established and may be amended by CalPERS. For Fiscal years 2010, 2009 and 2008, the District's annual contributions for the CalPERS plan were equal to the Agencies required and actual contributions for each fiscal year as follows:

Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

(7) Defined Benefit Pension Plan, continued

Funding Policy, continued

Three Year Trend Information:

<u>Fiscal Year</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>	<u>APC Percentage of Payroll</u>
2007-2008	\$ 10,424	100%	-	1.822%
2008-2009	13,341	100%	-	2.301%
2009-2010	17,994	100%	-	2.825%

(8) Net Assets

Calculation of net assets as of June 30, were as follows:

	<u>2010</u>	<u>2009</u>
Net investment in capital assets:		
Capital assets, net	\$ 18,972,301	17,785,686
Loan payable, current	(400,000)	(88,299)
Loan payable, non-current	(1,600,000)	-
Total net investment in capital assets	<u>16,972,301</u>	<u>17,697,387</u>
Restricted for capital improvement	<u>454,846</u>	<u>-</u>
Unrestricted net assets:		
Non-spendable net assets:		
Water in storage inventory	11,356	8,903
Materials and supplies inventory	351,234	341,222
Prepaid expenses and deposits	34,986	45,045
Total non-spendable net assets	<u>397,576</u>	<u>395,170</u>
Spendable net assets are designated as follows:		
Undesignated net assets reserve	<u>1,604,816</u>	<u>1,079,860</u>
Total spendable net assets	<u>1,604,816</u>	<u>1,079,860</u>
Total unrestricted net assets	<u>2,002,392</u>	<u>1,475,030</u>
Total net assets	<u>\$ 19,429,539</u>	<u>19,172,417</u>

Purissima Hills Water District
Notes to the Financial Statements
For the Fiscal Years Ended June 30, 2010 and 2009

(9) Risk Management

The District is exposed to various risks of loss related to torts, theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District is insured for a variety of potential exposures. The following is a summary of the insurance policies carried by the District as of June 30, 2010:

- Property: \$500,000 to \$100,000,000 with liability limits varying by property type with a \$5,000 deductible.
- Boiler and machinery: \$1,000,000 to \$100,000,000 based on type of equipment and/or event.
- Underground storage tank pollution liability: \$500,000 per environmental accident claim with \$500,000 annual aggregate limit with \$10,000 deductible.
- Liability coverage: \$1,000,000 to \$40,000,000 excess insurance per occurrence.
- Crime coverage: \$100,000 per claim with a \$1,000 deductible.
- Workers compensation: \$2,000,000 each accident or each employee by disease.

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

The Governmental Accounting Standards Board (GASB) has issued several pronouncements prior to June 30, 2010, that has effective dates that may impact future financial presentations.

Governmental Accounting Standards Board Statement No. 59

In June 2010, the GASB issued Statement No. 59, *Financial Instruments Omnibus*. This statement improves existing standards regarding financial reporting and disclosure requirements of certain financial instruments and external investment pools. This statement is not effective for this District until the fiscal year ended June 30, 2011. This statement is not expected to have a significant impact on the presentation of the District's financial statements.

(11) Commitments and Contingencies

Grant Awards

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

Litigation

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

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Report on Internal Controls and Compliance

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

Board of Directors
Purissima Hills Water District
Los Altos Hills, California

We have audited the basic financial statements of the Purissima Hills Water District (District) as of and for the years ended June 30, 2010 and 2009 and have issued our report thereon dated September 18, 2010. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

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

Compliance and Other Matters

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

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

September 10, 2010
Cypress, California