

**WATER UTILITY ENTERPRISE FUND  
OF THE  
Santa Clara Valley Water District  
San Jose, California**

Basic Financial Statements  
For the Fiscal Year Ended June 30, 2008

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**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT  
Basic Financial Statements  
For the Year Ended June 30, 2008**

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## INDEPENDENT AUDITORS' REPORT

The Honorable Members of the Board of Directors of the  
Santa Clara Valley Water District

We have audited the accompanying basic financial statements of the Santa Clara Valley Water District (the District), as of and for the fiscal year ended June 30, 2008. 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 audit.

We conducted our audit 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 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.

As discussed in Note 1, the financial statements present the financial activity of the Water Enterprise Fund only, and do not purport to, and do not, present the financial position and results of operations of the Santa Clara Valley Water District as a whole, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Fund, as of June 30, 2008, and the changes in financial position for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

*Vavrinek, Trine, Day & Co. LLP*

Palo Alto, California  
June 25, 2009

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## **Management's Discussion and Analysis**

Our discussion and analysis of the Santa Clara Valley Water District's Water Utility Enterprise Fund (the "Fund") financial performance provides an overview of the Water Utility Enterprise Fund financial activities for the fiscal year ended June 30, 2008. This information is presented in conjunction with the audited financial statements that follow this section.

The Fund manages and supplies wholesale treated water, groundwater, recycled water and surface water for the residents of Santa Clara County. The Fund is a separate enterprise fund of the Santa Clara Valley Water District (District) that was established to account for the water utility transactions of the District. Because service needs are different in the northern and southern portions of the county, operations and expenditures are tracked based on the relative benefit to North County and South County zones. Likewise, the District's water charges between the two zones are set separately.

The District engaged Vavrinek, Trine, Day & Co., LLP to conduct an audit of the District's Water Utility Enterprise Fund for the fiscal year ended June 30, 2008. The purpose of the audit was to analyze the reasonableness of the allocations of cost and revenue between the two groundwater charge zones within the Water Utility Enterprise Fund, the North County zone and the South County zone.

### **Overview of the Financial Statements**

The accounting policies of the Fund of the Santa Clara Valley Water District conform to accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB) and the American Institute of Certified Public Accountants.

The financial statements include the financial activity of the Water Enterprise Fund only. The Fund was established to account for the revenues and expenses of the Fund. These financial statements are not intended to present the financial position and results of operations of the Santa Clara Valley Water District as a whole, in conformity with accounting principles generally accepted in the United States of America. The Fund is accounted for as a Proprietary Fund. When the District charges users for the services it provides, these services are generally reported in proprietary funds. The following are the statements of the Fund:

*The Statement of Net Assets* presents information on all of the Fund'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 financial position of the District is improving or deteriorating

*The Statement of Revenues, Expenses and Changes in Net Assets* provides information about the Fund's revenues and expenses on accrual basis.

*The Statement of Cash Flows* provides relevant information of the Fund's cash receipts and cash payments during the period. This statement presents changes in the Fund's cash and cash equivalents resulting from operating, noncapital financing, capital and related financing, and investing activities.

**Notes to Basic Financial Statements.** The notes provide additional information that is essential to a full understanding of the data provided in the Fund's financial statements. The Fund accounts for operations in a manner similar to a private business enterprise. Operations are accounted for in such a manner as to show net income or loss and the Fund is intended to be entirely or predominantly self supported from user charges.

### Financial Highlights

*Water Utility Enterprise Fund's Net Assets*  
(Dollars in Thousands)

	<u>2008</u>	<u>2007</u> <sup>1</sup>
Current and other assets	\$ 241,790	\$ 135,834
Capital assets	<u>648,049</u>	<u>599,396</u>
Total assets	<u>889,839</u>	<u>735,230</u>
Current liabilities	31,974	29,293
Long-term liabilities outstanding	<u>231,505</u>	<u>108,683</u>
Total liabilities	<u>263,479</u>	<u>137,976</u>
Net assets:		
Investment in capital assets, net of related debt	500,821	487,993
Restricted	24,011	22,729
Unrestricted	<u>101,528</u>	<u>86,532</u>
Total net assets	<u>\$ 626,360</u>	<u>\$ 597,254</u>

<sup>1</sup> FY2007 Investment in capital assets, net of related debt was recalculated to include investment in contract water rights.

- The total net assets of the Fund exceeded its liabilities by \$626.4 million. Of this amount, \$101.5 million (unrestricted net assets) may be used to meet the Fund's ongoing obligations to citizens and creditors.
- The largest portion of the Fund's net assets (79.9 percent) reflects its investment in capital assets (e.g., land, buildings, infrastructure, machinery, equipment, and contract water rights), less any related debt used to acquire those assets still outstanding. These capital assets are used to provide services to citizens and consumers; consequently these assets are not available for future spending. Although the Fund's investment in its capital assets is reported net of related debts, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.



- Investment in capital assets, net of related debt increased by \$12.8 million due to capitalization of water delivery rights for \$9.2 million and ongoing major water treatment plant improvements. The Water Quality Laboratory project incurred costs of \$12.1 million and was completed during fiscal year 2008.

*Water Utility Enterprise Fund's Changes in Net Assets*

(Dollars in Thousands)

	<u>2008</u>	<u>2007</u>
Revenues:		
Ground water charges	\$ 60,998	\$ 50,251
Treated water charges	71,879	74,165
Surface and recycled water charges	2,600	818
Operating grants and contributions	2,437	2,818
Capital grants and contributions	708	105
Property taxes	22,945	21,491
Investment earnings	9,556	6,401
Miscellaneous	992	3,469
Total revenues	<u>172,115</u>	<u>159,518</u>
Expenses:		
Operating expenses	131,799	123,840
Nonoperating and other expenses	9,812	5,198
Total expenses	<u>141,611</u>	<u>129,038</u>
Increase in net assets before transfers	30,504	30,480
Transfers	(1,398)	(2,429)
Increase in net assets	<u>29,106</u>	<u>28,051</u>
Net assets, beginning	597,254	561,070
Prior period adjustment	-	8,133
Net assets, ending	<u>\$ 626,360</u>	<u>\$ 597,254</u>

- The net assets of the Fund increased by \$29.1 million. Compared to the previous fiscal year, key elements of the increase are as follows:
  - Revenues from ground water charges increased by \$10.7 million or 21.4 percent due to increases in rates and acre feet deliveries of ground water for non-agricultural usage. The rates per acre foot for non-agricultural usage increased by 9.2 percent and 10.9 percent in North and South Counties, respectively. The total acre feet of ground water deliveries for non-agricultural use went up by 21 percent.
  - Receipts of treated water charges decreased by \$2.3 million or 3.1 percent primarily due to lower acre feet deliveries of treated water. The total acre feet of treated water delivered declined by 10.9 percent, but was offset by increases in rates for contract of 7.5 percent and non-contract of 16.2 percent.
  - Revenues from surface and recycled water charges increased by \$1.8 million or 217.8 percent due to increases in acre feet deliveries and rates per acre foot. The total acre feet deliveries of surface and recycled waters increased by 62.5 percent and 33.2 percent, respectively. The rates per acre foot of surface water for non-agricultural usage increased by 9.2 percent and 10.9 percent in North and South Counties, respectively. Likewise, the rate per acre foot of recycled water for non-agricultural usage increased by 25.1 percent.

- d. Operating and capital grants and contributions had a minimal net increase of \$222 thousand or 7.6 percent. The increase represents additional funding from the State of California Department of Water Resources and other local and county reimbursements.
- e. Investment earnings increased by \$3.2 million or 49.3 percent due to higher interest rates and cash balances maintained in the account, and positive impact from the GASB 31 fair market value adjustment of \$1.2 million. Additionally, the bond proceeds reserved for construction were not spent as of the end of fiscal year 2008 resulting in additional interest income.
- f. Total expenses increased by \$12.6 million or 9.7 percent, primarily due to the recognition of an additional \$6.0 million unfunded annual required contribution related to other post employment benefits expense and additional interest and fiscal agent fee incurred for the newly issued 2007A and 2007B revenue COP bonds.

*Water Utility Enterprise Fund's Schedule of Revenues and Expenses*  
(Dollars in Thousands)

	<u>North County</u>		<u>South County</u>		<u>Total</u>	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
Operating Revenues:						
Groundwater charges	\$ 53,063	\$ 42,467	\$ 7,935	\$ 7,784	\$ 60,998	\$ 50,251
Treated water charges	71,879	74,165	-	-	71,879	74,165
Surface and recycled water charges	2,176	500	424	318	2,600	818
Total water charges	<u>127,118</u>	<u>117,132</u>	<u>8,359</u>	<u>8,102</u>	<u>135,477</u>	<u>125,234</u>
Operating grants	1,693	2,531	744	287	2,437	2,818
Total Operating revenues	<u>128,811</u>	<u>119,663</u>	<u>9,103</u>	<u>8,389</u>	<u>137,914</u>	<u>128,052</u>
Operating Expenses:						
Source of supply	52,754	56,684	8,149	7,210	60,903	63,894
Water treatment	23,307	20,050	17	46	23,324	20,096
Transmission and distribution:						
Raw water	6,225	6,091	1,238	1,193	7,463	7,284
Treated water	<u>1,897</u>	<u>1,450</u>	<u>-</u>	<u>-</u>	<u>1,897</u>	<u>1,450</u>
Cost of goods sold	84,183	84,275	9,404	8,449	93,587	92,724
Administration and general	22,711	17,033	2,239	2,244	24,950	19,277
Capital cost recovery	-	-	1,752	1,416	1,752	1,416
Total operating expenses	<u>106,894</u>	<u>101,308</u>	<u>13,395</u>	<u>12,109</u>	<u>120,289</u>	<u>113,417</u>
Operating income (loss)	<u>21,917</u>	<u>18,355</u>	<u>(4,292)</u>	<u>(3,720)</u>	<u>17,625</u>	<u>14,635</u>
Non-operating income (expenses):						
Property taxes	20,924	19,636	2,021	1,855	22,945	21,491
Investment income	9,556	6,401	-	-	9,556	6,401
Rental income	22	22	25	25	47	47
Other	369	2,146	576	1,276	945	3,422
Interest/fiscal agent fees	(9,812)	(5,198)	-	-	(9,812)	(5,198)
Open space credit transfer	(1,255)	(900)	1,255	900	-	-
Interest earned credit	<u>6</u>	<u>(14)</u>	<u>(6)</u>	<u>14</u>	<u>-</u>	<u>-</u>
Net non-operating income	<u>19,810</u>	<u>22,093</u>	<u>3,871</u>	<u>4,070</u>	<u>23,681</u>	<u>26,163</u>
Income (loss)	<u>\$ 41,727</u>	<u>\$ 40,448</u>	<u>\$(421)</u>	<u>\$ 350</u>	<u>\$ 41,306</u>	<u>\$ 40,798</u>

- The Fund's total revenues from water charges were \$135.5 million in fiscal year 2007/08. Ninety-four percent of those revenues, or \$127.1 million were collected from customers in the North County, while the remaining six percent or \$8.4 million were collected from South County customers.
- Operating Grants applied for and received were \$1.7 million to augment North County revenue and \$744,000 in the South County. These grants helped to fund water conservation, desalination, and recycled/reclaimed water programs.
- Operating expenses for the North County include \$84.2 million in cost of goods sold, or 65 percent of its total operating revenues. Whereas, for the South County, cost of goods sold is \$9.4 million or 103 percent of its total operating revenues.
- Administration and general expenses make up 18% of total operating revenues in the North County and 25 percent of total operating revenues in the South County.
- Total operating revenues of \$137.9 million less total operating expenses of \$120.3 million results in a \$17.6 million income from operations. The income from North County operations is \$21.9 million, while the loss from South County operations is \$4.3 million.

Operations is supplemented with property tax and investment earnings of \$32.5 million overall.

- Property taxes collected in the North County amounted to \$20.9 million while \$2.0 million were collected in South County for a total of \$22.9 million. These are comprised of voter approved obligations for State Water Project and Zone W-1 Debt service; and the water utility's allocated share of the countywide 1 percent ad valorem taxes.
- \$9.5 million of investment earnings resulted from an average return of 4.4 percent on average balances of \$95.0 million was allocated to the North County.

Overall net income from total income and total expenses was \$41.3 million; \$41.7 million income was allocated to North County and \$421 thousand loss to South County.

The actual revenue and cost allocations for prior fiscal year 2007 between the North and the South County zones are based on best available data at the time which includes estimates. The allocations were adjusted subsequently as better data became known. The net impact is that the income of the North County Zone W-2 increased while the South County Zone W-5 decreased by \$527 thousand. The adjustment is not reflected in the fiscal year 2007 numbers in this report.

The following table shows the rates for water services for fiscal year 2007-08:

*Water Utility Enterprise Fund's Rate Summary  
Adopted 2007-08*

	<b>Rate</b>
<u>Groundwater</u>	
North County – Agricultural	\$ 15.50
North County – Non-Agricultural	475.00
South County – Agricultural	15.50
South County – Non-Agricultural	255.00
<u>Treated Water</u>	
Contract (Scheduled)	575.00
Non-Contract	575.00
<u>Untreated Water</u>	
North County – Agricultural	15.50
North County – Non-Agricultural	475.00
South County – Agricultural	15.50
South County – Non-Agricultural	255.00
<u>Water Master</u>	11.75
<u>Minimum Charge</u>	
North County	356.25
South County	191.25
<u>Reclaimed Water</u>	
Gilroy Reclamation Facility – Agricultural	40.50
Gilroy Reclamation Facility – Non-Agricultural	\$ 244.00

**Capital Assets**

The Fund's investment in capital assets as of June 30, 2008, amounts to \$648.0 million (net of accumulated depreciation). The investment in capital assets includes intangible rights, land, buildings, structures and improvements, machinery and equipment. During FY 2007/08, the total increase in the Fund's investment in capital assets for the current year was \$48.7 million.

Major capital projects expenses during the current fiscal year include the following:

- Leniham Dam Outlet Modifications - \$22.4 million
- Penitencia Water Treatment Plant Improvements - \$1.7 million
- Rinconada Water Treatment Plant Improvements - \$1.2 million
- Water Infrastructure Reliability Program Phase 1 - \$2.2 million
- Water Quality Laboratory - \$12.1 million

*Water Utility Enterprise Fund's Capital Assets*  
(Net of Accumulated Depreciation)  
(Dollars in Thousands)

	<u>2008</u>	<u>2007</u>
Land	\$ 22,461	\$ 17,059
Contract water and storage rights	62,591	54,285
Buildings	1,665	1,699
Structures and improvements	386,498	288,742
Equipment	10,785	11,836
Construction in progress	164,049	225,775
	\$ 648,049	\$ 599,396
Total	\$ 648,049	\$ 599,396

**Debt Administration**

At the end of the current fiscal year, the Fund had total debt outstanding of \$234.2 million. This Fund's long-term obligations outstanding as of June 30, 2008 consisted of the following:

*Water Utility Enterprise Fund's Outstanding Obligations*  
(Dollars in Thousands)

	<u>2008</u>	<u>2007</u>
General obligation bonds	\$ 2,025	\$ 2,630
Revenue bonds	226,980	98,115
Compensated absences	280	-
Semitropic water banking	7,408	8,512
State revolving fund loan	6,350	5,576
Bond discount	(982)	(497)
Deferred amount on refunding	(2,810)	(2,932)
Deferred interest swap	(8,132)	-
Premium on bond issue	3,073	-
	\$ 234,192	\$ 111,404
Total	\$ 234,192	\$ 111,404

In fiscal year 2007/08, the Fund issued \$131.0 million of Water Utility Revenue Certificates of Participation Bonds, Series 2007A and 2007B. The proceeds of these bonds will be used to finance capital construction projects in the water enterprise.

The District entered into a loan agreement with the State of California from the Safe Drinking Water State Revolving Fund. The State Revolving Fund is a low interest rate program to assist communities in meeting safe drinking water standards for domestic water supplies. In fiscal year 2007/08, the Fund received \$774 thousand from the State of California increasing the outstanding balance of the loan to \$6.3 million.

All other decreases in obligations were from the normal repayment of principal on existing outstanding debts.

The revenue bonds of the Fund have a bond rating from Moody's ranging from Aa to Aa3 and from Standard & Poor's from AA to AA-.

Additional information on the Fund's long-term debt can be found in note 7 on pages 28 to 31 of this report.

### **Economic Factors and Next Year's Budgets and Rates**

The Annual Budget outlines the staff's plan to carry out the District's mission, "...a healthy, safe and enhanced quality of living in Santa Clara County through watershed stewardship and comprehensive management of water resources in a practical, cost-effective and environmentally sensitive manner."

Guiding management and staff in carrying out the Board Ends policies is the District's vision, *Getting Cleaner, Greener, and Leaner*.

- Cleaner: meeting increasingly stringent regulatory requirements for drinking water quality and environmental protection.
- Greener: producing a net positive impact on the environment.
- Leaner: improving processes to do more with less, focus on collaboration and process improvements.

In considering the District's budget for fiscal year 2008/09, the Board of Directors and management used the following estimates:

- The Board of Directors adopted a 9.5% increase in groundwater production charges for the North County region and a 7.8% increase for the South County region.
- Property taxes are estimated at \$73.8 million or a 2% increase from fiscal year 2007/08.
- The District will eliminate 28 vacant positions, reduce overtime by half, and maintain the net operating outlays at approximately the same level as the prior year.
- The District's "streamline and sustain" initiative will constrain internal costs and shift existing resources towards core business work that directly benefits the community.
- The District's overhead charges are projected to continue a downward trend as a result of cost-saving efforts.

### **Requests for Information**

This financial report is designed to provide citizens, taxpayers, customers, investors, and creditors, of the North and South Counties with a general overview of the Water Utility Enterprise's finances and to demonstrate the Water Utility Enterprise's accountability for the money it receives. If you have any questions about this report or need any additional information, contact the General Accounting Unit at 5750 Almaden Expressway, San Jose, CA 95123, or phone (408) 265-2600.

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**  
Statement of Net Assets  
June 30, 2008  
(Dollars in Thousands)

**ASSETS**

Current assets:

Cash and investments (Note 3)	\$	108,363
Restricted cash and investments (Note 3)		109,848
Receivables:		
Accounts		19,817
Taxes		140
Deferred charge		1,375
Deposits and other assets		2,247
Total current assets		241,790

Non current assets:

Capital assets: (Note 6)		
Contract water rights, net		62,591
Nondepreciable		186,510
Depreciable, net		398,948
Total non current assets		648,049
Total assets		889,839

**LIABILITIES**

Current liabilities:

Accounts payable		10,911
Accrued liabilities		9,514
Deposits payable		1,985
Accrued interest payable		836
Other post employment benefits payable (Note 11)		6,041
General obligation bonds - current (Note 7)		635
Revenue bonds - current (Note 7)		1,884
Other Debt (Note 7)		168
Total current liabilities		31,974

Non current liabilities:

Long-term debt: (Note 7)		
General obligation bonds - non current		1,390
Revenue bonds (net of unamortized discount and deferred amount on refunding)		216,245
Other debt		13,870
Total non current liabilities		231,505
Total liabilities		263,479

**NET ASSETS** (Note 9)

Investment in capital assets, net of related debt		500,821
Restricted for:		
Debt service		6,691
State revolving loan requirement		401
San Felipe operations		3,637
Operating reserves		11,987
Rate stabilization		1,295
Unrestricted:		101,528
Total net assets	\$	626,360

See accompanying notes to basic financial statements.

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**  
Statement of Revenues, Expenses and Changes in Net Assets  
For the Year Ended June 30, 2008  
(Dollars in Thousands)

<b>Operating revenues:</b>	
Ground water charges	\$ 60,998
Treated water charges	71,879
Surface and recycled water charges	2,600
Operating grants	2,437
	<hr/>
Total operating revenues	137,914
<b>Operating expenses:</b>	
Sources of supply	60,903
Water treatment	23,324
Transmission and distribution:	
Raw water	7,463
Treated water	1,897
Administration and general	24,950
Depreciation and amortization	13,262
	<hr/>
Total operating expenses	131,799
	<hr/>
Operating income (loss)	6,115
<b>Nonoperating revenues (expenses):</b>	
Property taxes (Note 8)	22,945
Investment income (Note 5)	9,556
Rental income	47
Other	945
Interest and fiscal agent fees	(9,812)
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Net nonoperating revenues	23,681
	<hr/>
Income before capital contributions and transfers	29,796
Capital contributions (Note 4)	708
Transfers out (Note 13)	(1,398)
	<hr/>
Change in net assets	29,106
Net assets, beginning of year	597,254
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Net assets, end of year	\$ 626,360
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See accompanying notes to basic financial statements.



**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Statement of Cash Flows  
For the Year Ended June 30, 2008  
(Dollars in Thousands)

<b>Cash flows from operating activities:</b>	
Receipts from customers and users	\$ 139,545
Payments to suppliers	(59,312)
Payments to employees	(44,756)
Payments for internal services used	(4,450)
Other receipts	945
Net cash provided (used) by operating activities	<u>31,972</u>
<b>Cash flows from noncapital financing activities:</b>	
Property taxes received	22,945
Transfers out to other funds	(1,398)
Net cash provided (used) by noncapital financing activities	<u>21,547</u>
<b>Cash flows from capital and related financing activities:</b>	
Principal payments on general obligation bonds	(605)
Principal payments on revenue bonds	(2,135)
Proceeds from revenue bond issued	134,153
Payment of costs on bond issued	(9,709)
Capital contribution received	708
Interest and fiscal agent fees paid	(10,150)
Acquisition of contract water rights	(11,089)
Revolving loan proceeds	774
Acquisition and construction of capital assets	(50,788)
Net cash provided by capital and related financing activities	<u>51,159</u>
<b>Cash flows from investing activities:</b>	
Purchase of restricted investments	(1,309)
Rental income received	47
Interest received on cash and investments	9,556
Net cash provided by investing activities	<u>8,294</u>
Net increase in cash and cash equivalents	112,972
Cash and cash equivalents, beginning of year	98,519
Cash and cash equivalents, end of year	<u>\$ 211,491</u>
<b>Reconciliation to the combined balance sheet:</b>	
Cash and investments	\$ 108,363
Restricted cash and investments	109,848
Less cash and investments not meeting the definition of cash equivalents	(6,720)
	<u>\$ 211,491</u>
<b>Reconciliation of operating income (loss) to net cash provided by operating activities:</b>	
Operating income (loss)	\$ 6,115
<b>Adjustments to reconcile operating income (loss) to net cash provided by operating activities:</b>	
Depreciation and amortization	13,262
Other receipts	945
<b>Change in operating assets and liabilities:</b>	
(Increase) in deposits and other assets	7,410
(Increase) in accounts receivable	1,630
(Increase) in inventory	11
(Decrease) increase in accounts payable	(5,493)
(Decrease) increase in accrued liabilities	1,705
Increase in deposits payable	66
(Decrease) increase in other post employment benefits & compensated absence:	6,321
Net cash provided by operating activities	<u>\$ 31,972</u>

See accompanying notes to basic financial statements.

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**  
Combining Statement of Revenues & Expenses  
For the Year Ended June 30, 2008  
(Dollars in Thousands)

	North County	South County	Total
<b>Operating revenues:</b>			
Ground water charges	\$ 53,063	\$ 7,935	\$ 60,998
Treated water charges	71,879	-	71,879
Surface and recycled water charges	2,176	424	2,600
Operating grants	1,693	744	2,437
Total operating revenues	<u>128,811</u>	<u>9,103</u>	<u>137,914</u>
<b>Operating expenses:</b>			
Sources of supply	52,754	8,149	60,903
Water treatment	23,307	17	23,324
Transmission and distribution:			
Raw water	6,225	1,238	7,463
Treated water	1,897	-	1,897
Administration and general	22,711	2,239	24,950
Capital cost recovery	-	1,752	1,752
Total operating expenses	<u>106,894</u>	<u>13,395</u>	<u>120,289</u>
Operating income (loss)	<u>21,917</u>	<u>(4,292)</u>	<u>17,625</u>
<b>Nonoperating revenues (expenses):</b>			
Property taxes	20,924	2,021	22,945
Investment income	9,556	-	9,556
Rental income	22	25	47
Other	369	576	945
Interest and fiscal agent fees	(9,812)	-	(9,812)
Open space credit transfer	(1,255)	1,255	-
Interest earned credit	6	(6)	-
Net nonoperating revenues	<u>19,810</u>	<u>3,871</u>	<u>23,681</u>
Income (Loss)	<u>\$ 41,727</u>	<u>\$ (421)</u>	<u>\$ 41,306</u>

**Reconciliation to Statement of Revenues, Expenses and changes in Net Assets:**

Income (Loss)	\$ 41,306
Less Depreciation Expense not allocated between Zones	(13,262)
Less Transfers out	(1,398)
Add back: Capital cost recovery expense allocated to South County	1,752
Add back: Capital contributions	<u>708</u>
Total Income (Loss) per Statement of Revenues, Expenses and Changes in Net Assets	<u>\$ 29,106</u>

See accompanying notes to basic financial statements.

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**(1) THE FINANCIAL REPORTING ENTITY**

**(a) Description of the Reporting Entity**

The Santa Clara Valley Water District (the District) is a special district created by an act of the legislature of the State of California (State) in 1951 and as amended. The District encompasses all of Santa Clara County.

The District is governed by a seven member Board of Directors. Five of the members are elected from the area of each of the five District supervisory districts and two members are appointed from specific geographic areas by the Board of Supervisors to represent the District at large. The term of office for the directors is four years.

The District has broad powers relating to all aspects of flood control and storm waters within the District, whether or not such waters have their sources within the District. It is also authorized to store and distribute water for use within its jurisdictional boundaries and authorized to provide sufficient water for present or future beneficial use of the lands and inhabitants of the District. The District acquires, stores, and distributes water for irrigation, residential, fire protection, municipal, commercial, industrial, and all other uses. The District also directly supports the caring for the environment and the community through careful stewardship.

The Water Utility Enterprise Fund (the "Fund") is a separate enterprise fund of the District that was established to account for the water utility transactions of the District. The Water Utility Enterprise supplies wholesale treated water, ground water, recycled water, and surface water for the residents of the Santa Clara County.

**(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**(a) Basis of Presentation**

The Fund's financial statements are prepared in conformity with the generally accepted accounting principles (GAAP) in the United States of America. The Government Accounting Standards Board (GASB) is the acknowledged standard setting body for establishing accounting and financial reporting standards followed by governmental entities in the United States of America. The fund is included in the District's Comprehensive Annual Financial Report and therefore, these financial statements do not purport to represent the financial position and changes in financial position of the District.

The Fund accounts 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 (including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**(b) Basis of Accounting**

The Fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Nonexchange transactions, in which the District gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes, benefit assessments and grants. On an accrual basis, revenues from property taxes and benefit assessments are recognized in the fiscal year for which the taxes and assessments are levied; revenue from grants is recognized in the fiscal year in which all eligibility requirements have been satisfied; and revenue from investments is recognized when earned.

For its Fund, the District has elected, under Governmental Accounting Standard's Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, to apply all applicable GASB pronouncements as well as any applicable pronouncements of the Financial Accounting Standards Board (FASB), the Accounting Principles Board or any Accounting Research Bulletins issued on or before November 30, 1989 unless those pronouncements conflict with or contradict GASB pronouncements.

The Fund distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services in connection with the Fund's principal ongoing operations. The principal operating revenues of the Fund is the sale of water to outside customers. Operating expenses for the Fund include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Fund *operating* revenues, such as charges for services, result from the exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal value. *Nonoperating* revenues, such as subsidies and investment earnings, result from nonexchange transactions or ancillary activities.

**(c) Cash and Investments**

While maintaining safety and liquidity, the District maximizes its investment return by pooling its available cash for investment purposes. Interest earnings are apportioned among funds based upon the average monthly cash balance of each fund and are allocated to each fund on a monthly basis.

The District reported investments in nonparticipating interest earnings contracts (including guaranteed investment contracts) at cost, investments that mature beyond one year from the date of acquisition at fair value, and investments that mature within one year or less

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

from the date of acquisition at amortized cost. The fair value of investments is based on current market prices.

For purposes of the Statement of Cash Flows, the proprietary funds consider all highly liquid investments with a maturity of three months or less when purchased (including restricted investments), and their equity in the cash and investment pool to be cash equivalents.

**(d) Inventory**

Fund inventory consists of materials and supplies held for consumption. The cost of all inventory acquired is recorded as an expense at the time of purchase. At the end of the accounting period, the inventory values of materials and supplies on hand are determined using a current cost method which approximates market value. For financial statement purposes inventories are presented under deposits and other assets.

**(e) Capital Assets**

Capital assets (including infrastructure) are recorded at historical cost or at estimated historical cost if actual historical cost is not available. Contributed capital assets are valued at their estimated fair market value on the date contributed. The District defines capital assets as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of one year. Capital assets including assets under capital leases used in operations are depreciated or amortized using the straight-line method over the lesser of the capital lease period or their estimated useful lives in the Fund.

The estimated useful lives are as follows:

Water treatment facilities	50 Years
Buildings, structures, and trailers	25 – 50 Years
Flood control projects	30 – 100 Years
Dams, structures, and improvements	50 - 80 Years
Office furniture, fixtures, and equipment	5 - 20 Years
Automobiles and trucks	6 - 12 Years
Computer equipment	5 Years

Maintenance and repairs are charged to operations when incurred. Betterments and major improvements which significantly increase values, change capacities or extend useful lives are capitalized. Upon sale or retirement of capital assets, the cost and related accumulated depreciation are removed from the respective accounts and any resulting gain or loss is included in the results of operations.

**(f) Amortization of Contract Water Rights**

The District has contracted with the State for water deliveries from the State Water Project through calendar year 2035. A portion of the payments under this contract represent

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

reimbursement of capital costs for transportation facilities (the capital cost component).  
The

Fund capitalizes the capital cost component and amortizes such component, using the straight-line method, over the remaining entitlement period.

**(g) Amortization of Water Banking Rights**

The District has contracted with the Semitropic Water Storage District and its Improvement Districts for the water banking and exchange program. The program is in effect through calendar year 2035. Participation in the program provides the District a 35% allocation for storage rights at the Semitropic Water Storage District facility, totaling 350,000 acre-feet. The Fund has capitalized the cost of the program and amortizes its cost over the 40 year entitlement period using the straight-line method.

**(h) Amortization of Water Delivery Rights**

The District has contracted with the United States Department of the Interior Bureau of Reclamation for water deliveries from Central Valley through calendar year 2027. A portion of this contract represents reimbursement of capital costs for general construction in the San Felipe Division facilities. The Fund capitalized the capital cost component and amortizes such component, using the straight-line method, over the remaining entitlement period.

**(i) Receivables**

Receivables include amounts due from water utility customers as well as amounts due for property taxes and interest on investments. All receivables are shown net of an allowance for doubtful accounts of \$6,000.

**(j) Accrued Vacation and Sick Leave Pay**

It is the policy of the District to permit employees to accumulate earned but unused vacation and sick leave benefits. Vested or accumulated vacation and sick leave are reported as noncurrent liabilities on the statement of net assets.

Maximum vacation accruals may not exceed three times the employee's annual accrual rate, per employee. All regular full-time employees are eligible for twelve (12) days of sick leave per fiscal year. Unused sick leave may be carried forward to the following fiscal year without limitation. Upon termination, the eligible employees will be paid a portion of unused sick leave at the employee's base pay rate at the time of termination. The percentage of unused sick leave to be paid out varies with the employee's length of service at the District.

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**(k) Bond Premiums, Discounts and Issuance Costs**

The Fund bond discounts, as well as issuance costs, are deferred and amortized over the life of the bonds. Bonds payable are reported net of the applicable bond discounts. Issuance costs are reported as deferred charges.

On the statement of net assets the Bond premiums and Certificates of participation, as well as issuance costs, are deferred and amortized over the life of the certificates. Revenue COP payable and Revenue Bonds payable are reported net of the applicable bond premium and discounts. Issuance costs are reported as deferred charges.

**(l) Encumbrances**

The District employs encumbrance accounting as a significant aspect of budgetary control. Under encumbrance accounting, purchase orders, contracts and other commitments for expenditure of funds are recorded as reservations of fund balance since they are not treated as current expenditures or outstanding liabilities at year end for GAAP financial reporting.

**(m) Estimates**

The preparation of the basic financial statements in conformity with GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

**(3) CASH AND INVESTMENTS**

Total Fund cash and investments at June 30, 2008 are as follows (in thousands):

Statement of Net Assets:

Cash and investments	\$ 108,363
Restricted cash and investments	109,848
	<u>\$ 218,211</u>

**Investments**

At June 30, 2008, cash and investments consist of the following (in thousands):

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

Investment held by fiscal agent	
Cash	\$ 3
U.S. Government Agencies	42,196
Medium Term Notes	28,788
Guaranteed Investment Contracts	4,745
Mutual Funds	29,065
Nonnegotiable Certificates of Deposit	<u>4,691</u>
Total investments held by fiscal agent	109,488
Santa Clara County Investment Pool	360
District's Pooled Cash and Investment	<u>108,363</u>
Total cash and Investments	<u><u>\$ 218,211</u></u>

As of June 30, 2008, the District's investment in the State investment pool Local Agency Investment Fund (LAIF) is \$39,988,000. The total amount invested by all public agencies in LAIF at that date is \$69,955,386,000. Of that amount, 85.28 percent is invested in non-derivative financial products and 14.72 percent in asset-backed securities and medium-term and short-term structured notes. The Local Investment Advisory Board (Board) has oversight responsibility for LAIF. The Board consists of five members as designated by State Statute. The value of the pool shares in LAIF, which may be withdrawn, is determined on an amortized cost basis, which is different than the fair value of the District's position in LAIF.

As of June 30, 2008, the Fund's investment in the Santa Clara County Investment Pool (Pool) is \$360,000, which is restricted for interest and redemption of the 1963 water utility bonds. The Pool has established a treasury oversight committee to monitor and review the management of public funds maintained in the Pool. Participants' equity in the Pool is determined by the dollar amount of participant deposits, adjusted for withdrawals and distributed investment income. The value of the Fund's shares in the Pool is determined on an amortized cost basis, which is different than the fair value of the Fund's position in the Pool. The Fund's investment in the Pool is stated at fair value, available upon demand and considered a cash equivalent.

**Authorized Investments by the District**

The District's Investment Policy and the California Government Code allow the District to invest in the following types of instruments, provided the credit ratings of the issuers are acceptable to the District. The following table also identifies certain provisions of the District and California Government Code that address interest rate risk, credit risk, and concentration of credit risk. This does not address the District's investments of debt proceeds held by fiscal agents that are governed by the provisions of debt agreements of the District, rather than the general provisions of the California Government Code or the Entity's investment policy.



**WATER UTILITY ENTERPRISE FUND  
OF THE  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Minimum Credit Quality</u>	<u>Maximum Percentage of Portfolio</u>	<u>Maximum Investment in One Issuer</u>
U.S. Treasury Obligations	5 years	N/A	None	None
U.S. Agency Issues (A)	5 years	N/A	None	None
Bankers Acceptances	180 days	AA-	40%	4.8%
Commercial Paper	90 days	AA-	15%	1.8%
Negotiable Certificates of Deposit	1 year	AA-	30%	3.6%
				\$100,000 & FDIC
Nonnegotiable Certificates of Deposit	1 year	N/A	5%	Membership
Collateralized Repurchase Agreements	30 days	AA-	None	None
Medium Term Notes	3 years	AA-	15%	1.8%
Taxable Municipal Obligations	5 years	AAA	None	12%
California Local Agency Investment Fund (B)	N/A	N/A	(B)	(B)
Mutual Funds	N/A	AAA	10%	10%
Money Market Account with Union Bank	N/A	N/A	None	12%

(A) Securities issued by agencies of the federal government such as the Federal Farm Credit Bank (FFCB), the Federal Home Loan Bank (FHLB), the Federal National Mortgage Association (FNMA), and Federal Home Loan Mortgage Corporation (FHLMC), the Federal Agricultural Mortgage Corporation of America, the Tennessee Valley Authority and the Student Loan Marketing Association.

(B) LAIF will accept no more than \$40 million of an agency's unrestricted funds while placing no constraints on funds relating to unspent bond proceeds.

**Restricted Cash and Investments for Bond Interest and Redemption**

Under the provisions of the District's revenue bond resolutions and Installment Purchase Agreement for the 2006A & 2006B Water Utility Revenue and Refunding Bonds and 2007A & 2007B Revenue Certificates of Participation, a portion of the proceeds from these debt issuances is required to be held in custody accounts by a fiscal agent as trustee. As of June 30, 2008, the amount invested in assets held by fiscal agent amounted to \$1.2 million for certificates of participation and \$5.5 million for revenue bonds and was equal to or in excess of the amount required at that date.

**Restricted Cash and Investments for Capital Projects**

The Fund has construction funds from the 2007A and 2007B Revenue Certificates of Participation (COP) which are used to finance the cost of water utility system improvement projects. At June 30, 2008, the balance of this fund is \$102,768,000.

**Authorized Investments by Debt Agreements**

The District must maintain required amounts of cash and investments with trustees or fiscal agents under the terms of certain debt issues. These funds are unexpended bond proceeds or are pledged reserves to be used if the District fails to meet its obligations under these debt issues. The California Government Code requires these funds to be invested in accordance with District ordinances, bond indentures or State statutes. The

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

following table identifies the investment types that are authorized for investments held by fiscal agents. The table also identifies certain provisions of these debt agreements:

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Minimum Credit Quality</u>
U.S. Treasury Obligations (A)	N/A	N/A
U.S. Agency Securities (B)	N/A	N/A
State Obligations (C)	N/A	A
Commercial Paper	270 days	A1
Unsecured CD's, deposit accounts, time deposits, bankers acceptances	365 days	A-1
FDIC Insured Deposit (D)	N/A	N/A
Money Market Funds	N/A	AAAm
Collateralized Repurchase Agreements (E)	N/A	A-1
Investment Agreements (F)	N/A	AAA
Investment Approved in Writing by the Certificate Insurer	N/A	N/A

(A) Direct obligations of the United States of America and securities fully and unconditionally guaranteed as to the timely payment of principal and interest by the United States of America, provided, that the full faith and credit of the United States of America must be pledged to any such direct obligation or guarantee.

(B) Direct obligations and fully guaranteed certificates of beneficial interest of the Export-Import Bank of the United States; consolidated debt obligations and letter of credit-backed issues of the Federal Home Loan Banks; participation certificates and senior debt obligations of the Federal Home Loan Mortgage Corporation ("FHLMCs"); debentures of the Federal Housing Administration; mortgage-backed securities (except stripped mortgage securities which are valued greater than par on the portion of unpaid principal) and senior debt obligations of the Federal National Mortgage Association ("FNMA's"); participation certificates of the General Services Administration; guaranteed mortgage-backed securities and guaranteed participation certificates of the Government National Mortgage Association ("GNMA's"); guaranteed participation certificates and guaranteed pool certificates of the Small Business Administration; debt obligations and letter of credit-backed issues of the Student Loan Marketing Association; local authority Certificates of the U.S. Department of Housing & Urban Development; guaranteed Title XI financings of the U.S. Maritime Administration; guaranteed transit Certificates of the Washington Metropolitan Area Transit Authority; Resolution Funding Corporation securities.

(C) Direct obligations of any state of the United States of America or any subdivision or agency thereof whose unsecured, uninsured and unguaranteed general obligation debt is rated, at the time of purchase, "A" or better by Moody's and "A" or better by S&P.

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

(D) Deposits of any bank or savings and loan association which has combined capital, surplus and undivided profits of not less than \$3 million, provided such deposits are continuously and fully insured by the Bank Insurance Fund or the Savings Association Insurance Fund of the Federal Deposit Insurance Corporation.

(E) Repurchase agreements collateralized by Direct Obligations, GNMA's, FNMA's or FHLMC's with any registered broker/dealer subject to the Securities Investors' Protection Corporation jurisdiction or any commercial bank insured by the FDIC, if such broker/dealer or bank has an unsecured, unguaranteed obligation rated "P-1" or "A3" or better by Moody's and "A-1" or "A-" or better by S&P, provided: (1) a master repurchase agreement or specific written repurchase agreement governs the transaction; and (2) the securities are held free and clear of any lien by the Trustee or an independent third party acting solely as agent ("Agent") for the Trustee, and such third party is (i) a Federal Reserve Bank, or (ii) a bank which is a member of the Federal Deposit Insurance Corporation and which has combined capital, surplus and undivided profits of not less than \$50 million or (iii) a bank approved in writing for such purpose by the Certificate Insurer, and the Trustee shall have received written confirmation from such third party that it holds such securities, free and clear of any lien, as agent for the Trustee; and (3) a perfected first security interest under the Uniform Commercial Code, or book entry procedures prescribed at 31 C.F.R. 306.1 et seq. or 31 C.F.R. 350.0 et seq. in such securities is created for the benefit of the Trustee; and (4) the repurchase agreement has a term of 180 days or less, and the Trustee or the agent will value the collateral securities no less frequently than weekly and will liquidate the collateral securities if any deficiency in the required collateral percentage is not restored within two business days of such valuation; and (5) the fair market value of the securities in relation to the amount of the repurchase obligation, including principal and interest, is equal to at least 103%.

(F) Investment agreements, guaranteed investment contracts, funding agreement, or any other form of corporate note representing the unconditional obligations of entities or agencies with the unsecured long-term debt obligations or claims-paying ability rated in one of the top two rating categories by Moody's and S&P.

(G) Any investment approved in writing by the Certificate Insurer.

**Interest Rate Risk**

Interest Rate Risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The District generally manages its own interest rate risk by holding investments to maturity.

Information about the sensitivity of the fair values of the District's investments to market interest rate fluctuations is provided by the following table that shows the distribution to the District's investments by maturity or earliest call date (in thousands):

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

	Total	12 Months or less	13 to 24 Months	25 to 60 Months	More than 60 Months
U.S. Treasury Obligations	\$ 3,008	\$ 3,008	\$ -	\$ -	\$ -
U.S. Government Agencies	173,670	-	11,942	161,728	-
U.S. Government Agencies - Callable	148,745	71,336	42,901	34,508	-
Medium Term Notes	61,884	50,466	11,418	-	-
Local Agency Investment Fund	39,998	39,998	-	-	-
Guaranteed Investment Contracts	4,745	-	-	-	4,745
Santa Clara County Investment Pool	360	360	-	-	-
Mutual Funds	38,110	38,110	-	-	-
Mutual Funds-Restricted for Debt Service	44,938	44,938	-	-	-
Money Market Funds	144	144	-	-	-
Nonnegotiable Certificates of Deposit	5,935	1,244	4,691	-	-
<b>Total Investments</b>	<b>\$ 521,537</b>	<b>\$ 249,604</b>	<b>\$ 70,952</b>	<b>\$ 196,236</b>	<b>\$ 4,745</b>

**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 the California Government Code, the District's investment policy, or debt agreements and the actual rating as of June 30, 2008 for each investment type as provided by Standard and Poor's (in thousands):

	Total	Minimum Legal Rating	Exempt from Disclosure	Rating as of Year-end				
				AAA	AA+	AA	AA-	Not Rated
U.S. Treasury Obligations	\$ 3,008	N/A	\$ 3,008	\$ -	\$ -	\$ -	\$ -	\$ -
U.S. Government Agencies	322,415	AA-	-	322,415	-	-	-	-
Medium Term Notes	61,884	AA-	-	16,583	13,831	22,035	9,435	-
Local Agency Investment Fund	39,998	AA-	-	-	-	-	-	39,998
Guaranteed Investment Contracts	4,745	N/A	-	-	-	-	-	4,745
Santa Clara County Investment Pool	360	N/A	-	-	-	-	-	360
Mutual Funds	38,110	AAA	-	38,110	-	-	-	-
Mutual Funds-Restricted for Debt Service	44,938	AAA	-	44,938	-	-	-	-
Money Market Funds	144	N/A	-	-	-	-	-	144
Nonnegotiable Certificates of Deposit	5,935	N/A	-	-	-	-	-	5,935
<b>Total Investments</b>	<b>\$ 521,537</b>		<b>\$ 3,008</b>	<b>\$ 422,046</b>	<b>\$ 13,831</b>	<b>\$ 22,035</b>	<b>\$ 9,435</b>	<b>\$ 51,182</b>

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**Concentration of Credit Risk**

The District's investment policy regarding the amount that can be invested in any one issuer is stipulated by the California Government Code. However, the District is required to disclose investments that represent a concentration of five percent or more of investments in any one issuer, held by individual District Funds in the securities of issuers other than U.S. Treasury securities, mutual funds and external investments pools. At June 30, 2008, those investments consisted of (in thousands):

Issuer	Investment Type	Reported Amount
<b>District-Wide</b>		
Federal Home Loan Mortgage Corp.	U.S. Government Agency	\$56,298
Federal National Mortgage Association	U.S. Government Agency	58,497
Federal Home Loan Bank	U.S. Government Agency	182,501
<b>Fund Level</b>		
COP Debt Service Fund		
Federal National Mortgage Association	U.S. Government Agency	7,646
COP Construction Fund		
Federal National Mortgage Association	U.S. Government Agency	1,636
Water Enterprise Fund		
Wells Fargo NT	Medium-Term Notes	8,827
World Savings Bank FSB NT	Medium-Term Notes	19,962
Federal Farm Credit Banks	U.S. Government Agency	9,928
Federal Home Loan Banks	U.S. Government Agency	32,268

**Custodial Credit Risk**

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the District 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.

Under California Government Code Section 53651, depending on specific types of eligible securities, a bank must deposit eligible securities posted as collateral with its Agent having a fair value of 105% to 150% of the District's cash on deposit. All of the District's deposits are either insured by the Federal Depository Insurance Corporation (FDIC) or collateralized with pledged securities held in trust department of the financial institutions in the District's name.

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**(4) REIMBURSEMENT OF CAPITAL COSTS**

The District derives certain revenues from reimbursements of capital costs by local, state, federal agencies and other outside sources. The following is a summary of such reimbursements in fiscal year 2007/08 (in thousands):

South County Regional Wastewater	<u>\$ 708</u>
----------------------------------	---------------

**(5) INVESTMENT INCOME**

The District earns income from the investment of cash not required for current expenditures. Beginning after June 15, 1997, the Governmental Accounting Standard Board issued GASB pronouncement number 31 to establish accounting and financial reporting standards for all investments. One provision of this standard was to report investments at fair value in the balance sheets. Because of this requirement, investment income must be adjusted upwards or downwards to reflect the fair value change from one fiscal year to the next fiscal year. In making the adjustment, the investment income earned directly by the investments is modified.

The following represents the investment income as reported in the financial statements, the current year GASB 31 fair value adjustment, and the unadjusted investment income at June 30, 2008 (in thousands):

	<u>Interest as Reported</u>	<u>GASB 31 Fair Value Adjustment</u>	<u>Earned Before Adjustment</u>
Water Enterprise	<u>\$ 9,556</u>	<u>\$ 1,199</u>	<u>\$ 8,357</u>

**WATER UTILITY ENTERPRISE FUND  
OF THE  
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**(6) CAPITAL ASSETS**

Capital assets activity for the year ended June 30, 2008 was as follows (in thousands):

	Balance July 1, 2007	Additions	Deletions	Transfers / Reclassified	Balance June 30, 2008
Nondepreciable capital assets:					
Land	\$ 17,059	\$ -	\$ -	\$ 5,402	\$ 22,461
Construction in progress	225,775	50,460	-	(112,186)	164,049
Total nondepreciable capital assets	<u>242,834</u>	<u>50,460</u>	<u>-</u>	<u>(106,784)</u>	<u>186,510</u>
Depreciable capital assets:					
Contract water and storage rights	113,576	11,090	-	-	124,666
Buildings	1,722	-	-	-	1,722
Structures and improvements	444,792	-	-	106,784	551,576
Equipment	19,233	427	(142)	-	19,518
Total depreciable capital assets	<u>579,323</u>	<u>11,517</u>	<u>(142)</u>	<u>106,784</u>	<u>697,482</u>
Less accumulated depreciation and amortization					
Contract water and storage rights	(59,291)	(2,784)	-	-	(62,075)
Buildings	(23)	(34)	-	-	(57)
Structures and improvements	(156,050)	(9,028)	-	-	(165,078)
Equipment:	(7,397)	(1,407)	71	-	(8,733)
Total accumulated depreciation and amortization	<u>(222,761)</u>	<u>(13,253)</u>	<u>71</u>	<u>-</u>	<u>(235,943)</u>
Net depreciable capital assets	<u>356,562</u>	<u>(1,736)</u>	<u>(71)</u>	<u>106,784</u>	<u>461,539</u>
Total capital assets, net	<u>\$ 599,396</u>	<u>\$ 48,724</u>	<u>\$ (71)</u>	<u>\$ -</u>	<u>\$ 648,049</u>

New construction in progress increased in the Fund by \$50.5 million. The upgrades of the District's water treatment plants, dam modifications, and a new water quality lab constitute the largest portion of construction expenses. Forty-two projects were in progress during the fiscal year with major project listed below (in millions):

- Lenihan Dam Outlet Modifications - \$22.4M
- Penitencia Water Treatment Plant Improvements - \$1.7M
- Rinconada Water Treatment Plant Improvements - \$1.2M
- Water Infrastructure Reliability Program Phase 1 - \$2.2M
- Water Quality Lab - \$12.1M

Total depreciation and amortization expenses \$13,253

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**(7) SHORT-TERM AND LONG-TERM LIABILITIES**

**(a) Short-term debt**

On December 17, 2002, the District Board of Directors authorized a commercial paper program for financing primarily Water Utility capital expenditures. The commercial paper program allows the District to finance capital expenditures while taking advantage of short term rates. This program will be used in conjunction with issuing long-term liabilities to obtain the least cost financing for the District. The authorized limit for fiscal year 2008 was \$100 million (\$40 million for taxable debt and \$60 million for tax-exempt debt). This limit may change from fiscal year to fiscal year. Barclays is the approved dealer for the commercial paper program.

There was no commercial paper debt outstanding at June 30, 2008.

**(b) Long-term liabilities**

The Fund's long-term liabilities outstanding consisted of the following (in thousands):

<u>Type of indebtedness</u>	<u>Maturity</u>	<u>Interest Rates</u>	<u>Authorized and Issued</u>	<u>June 30, 2008</u>	<u>Due Within One Year</u>
1963 Water utility bonds - general obligation					
Series C	2008	4.6% - 5%	\$ 3,500	\$ 185	\$ 185
Series D	2012	2.25% - 7%	8,850	1,840	450
Total 1963 water utility - G.O.B.			<u>12,350</u>	<u>2,025</u>	<u>635</u>
2006A Water revenue bond	2035	3.5% - 5%	74,265	71,110	1,750
2006B Water revenue bond	2035	5.15%-5.31%	25,570	24,870	470
2007A Water revenue COP bond	2037	4.0% - 5.0%	77,270	77,270	-
2007B Water revenue COP bond	2037	5.50% -floating	53,730	53,730	-
Bond discount				(982)	(38)
Deferred amount on refunding				(2,810)	(123)
Interest rate swap deferral				(8,132)	(281)
Premium on debt issuance				3,073	106
Compensated absences				280	43
Semitropic water banking agreement	2035		46,900	7,408	-
State revolving fund loan	2027	2.39%	6,350	6,350	125
Total enterprise fund debt				<u>\$ 234,192</u>	<u>\$ 2,687</u>



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The following is a summary of changes in long-term liabilities as of June 30, 2008 (in thousands):

	Balance 7/1/2007	Additions	Reductions	Balance 6/30/2008	Due Withn One Year
1963 Water Utility bonds	\$ 2,630	\$ -	\$ (605)	\$ 2,025	\$ 635
2006A revenue bonds	72,800	-	(1,690)	71,110	1,750
2006B revenue bonds	25,315	-	(445)	24,870	470
2007A COP revenue bonds	-	77,270	-	77,270	-
2007B COP revenue bonds	-	53,730	-	53,730	-
Premium on issuance	-	3,153	(80)	3,073	106
Deferred amount on refunding	(2,932)	-	122	(2,810)	(123)
Discount amount on refunding	(497)	(519)	34	(982)	(38)
Deferred Interest swap	-	(8,343)	211	(8,132)	(281)
Compensated absences	-	280	-	280	43
State revolving fund loan	5,576	774	-	6,350	125
Semitropic water storage agreement	8,512	-	(1,104)	7,408	-
<b>Total enterprise debt</b>	<b>\$ 111,404</b>	<b>\$ 126,345</b>	<b>\$ (3,557)</b>	<b>\$ 234,192</b>	<b>\$ 2,687</b>

The aggregate maturities of long-term debt are as follows (in thousands):

Year ending June 30:	Principal	Interest and amortization
2009	\$ 2,980	\$ 11,585
2010	5,294	11,535
2011	5,525	11,302
2012	5,631	11,066
2013	5,473	10,820
2014 - 2018	31,395	50,023
2019 - 2023	39,655	41,759
2024 - 2028	49,823	31,566
2029 - 2033	52,893	18,764
2034 - 2037	36,685	5,487
<b>Total Requirements</b>	<b>235,354</b>	<b>\$ 203,907</b>
Add: semitropic water storage agreement	7,408	
Add: unamortized premium on issuance	3,073	
Add: compensated absences	280	
Less: unamortized discount and deferred amount on refunding	(11,923)	
<b>Total principal outstanding at June 30, 2008</b>	<b>\$ 234,192</b>	

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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

The following provides a brief description of the Fund's outstanding debt as of June 30, 2008:

1963 Water Bonds

The Water Bonds are general obligations of the District. These bonds were issued pursuant to the provisions of Resolution No. W-1.8, adopted November 12, 1963. Proceeds from these bonds have been used for construction of a comprehensive water treatment and distribution system. Debt service payments are funded through ad valorem taxes on property.

2006 Water Enterprise Revenue Bonds

In December 2006, the District issued \$99,835,000 of Water Utility System Refunding Revenue Bonds, Series 2006A and Taxable Series 2006B. The proceeds of \$57,415,000 of the 2006A and 2006B Bonds were used to refinance \$55,265,000 of the remaining 2000A and 2000B Bonds and the proceeds of \$42,420,000 of 2006A and 2006B Bonds were used to repay approximately \$40.9 million of commercial paper notes. The District funded the 2006A Debt Service Reserve Fund with proceeds of the 2000A Debt Service Reserve Fund and purchased a surety bond to fund the 2006B Debt Service Reserve Fund. The District has pledged its net water utility revenues to secure the semi-annual debt service payments.

2007 Water Enterprise Revenue Certificates of Participation

In October 2007, the District issued \$131,000,000 of Water Utility Revenue Certificates of Participation Bonds, Series 2007A and Taxable Series 2007B. The proceeds of the 2007A and 2007B bonds will be used to finance capital construction projects in the Water Utility Enterprise. The District funded the 2007A Debt Reserve Fund by purchasing a surety. The 2007A issuance was \$77,270,000 fixed rate bonds with a 30 year maturity. The 2007B issuance of \$53,730,000 are floating rate notes based on the three month LIBOR rate plus 32 basis points with a 30 year maturity. The District has pledged its net water utility revenues to secure the semi-annual debt service payments for the 2007A issuance and quarterly debt service payments for the 2007B issuance.

The District entered into two interest rate locks in anticipation of the issuance of the 2007 Series A and B. The interest rate locks successfully locked in the interest rate the District had been projecting in its water rate financing models on a net present value basis. The interest rate locks were terminated at the time of bonds issuance in which the District paid the counterparties a termination fee in the amount of \$8.5 million.

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

Semitropic Water Storage Agreement

In December 1995, the Santa Clara Valley Water District entered into a water banking and exchange program with Semitropic Water Storage District and its Improvement Districts that entitles the District to storage, withdrawal, and exchange rights for the District's State Water Project supplies. The Santa Clara Valley Water District's share of the total program capital costs is \$46.9 million based on a 35 percent vesting in the program. The District pays the program capital costs when storing and recovering water. At June 30, 2008, the District has paid \$39.5 million towards the obligation of this agreement.

Compensated absences

Compensated absences are paid out of the general fund as an employee benefit expense in the year the expense is realized. At the end of the each year all funds reimburse the general fund on a pro-rata basis of salary expense cost for the payment of these payouts. In fiscal year 2008, the compensated absences liability for the year was recognized in the Fund.

Compliance with Bond Covenants

Resolutions associated with the District's bonds and certificates of participation contain a number of covenants, limitations, and restrictions. The District believes it is in compliance with all significant covenants, limitations, and restrictions. At June 30, 2008, the contingent arbitrage liability arising from interest earnings is \$447 thousand for governmental activities and \$537 thousand in the Water Enterprise Fund. At June 30, 2008, the legal debt margin for short term notes under was \$8.0 million. There were no short term notes outstanding as of June 30, 2008.

**(8) PROPERTY TAXES AND BENEFIT ASSESSMENTS**

The Fund derives certain revenues from the assessment of property tax parcel levies. The property tax levy is composed of three categories: (1) a 1 percent tax allocation; (2) voter approved levy to service the 1963 Water General Obligation bonds (G.O. bonds); and (3) voter approved levy to repay capital and operating costs related to State Water Projects.

Property tax revenues recorded for the year ended June 30, 2008 are as follows (in thousands):

Property taxes:	
1% tax allocation	\$ 4,216
Voter approved indebtedness:	
State water	17,853
G.O. bonds	876
Total property taxes	<u>\$ 22,945</u>

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

The County is responsible for the assessment, collection, and apportionment of property taxes for the District. The amount of property tax levies is restricted by Article 13A of the California State Constitution (commonly referred to as Proposition 13). The District is responsible for determining the amount of benefit assessment, special parcel tax, and State Water Project debt service. Secured property taxes and benefit assessments are each payable in equal installments, November 1 and February 1, and become delinquent on December 10 and April 10, respectively. The lien date is January 1 of each year. The Fund records property taxes as they are levied. Property taxes on the unsecured roll are due on the March 1 lien date and become delinquent if still unpaid on August 31.

The District has elected to participate in the "Teeter Plan" offered by the County whereby the District receives 100 percent of secured property and supplemental property taxes levied in exchange for foregoing any interest and penalties collected on the related delinquent taxes.

**(9) NET ASSETS/FUND BALANCES**

The Fund financial statements utilize a net assets presentation. Net assets are categorized as invested capital assets (net of related debt), restricted and unrestricted.

*Invested In Capital Assets, Net of Related Debt* - This category groups all capital assets, including infrastructure, into one component of net assets. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction or improvement of these assets reduce the balance in this category.

*Restricted Net Assets* – This category presents external restrictions imposed by creditors, grantors, contributors, laws, or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.

*Unrestricted Net Assets* – This category represents net assets of the District, not restricted for any project or other purpose.

Portions of unrestricted fund balance may be designated to indicate tentative plans for financial resource utilization in a future period, such as for general contingencies or capital projects. Such plans or intent are subject to change, require further legal authorization and may not result in expenditures or expenses. The Fund's unrestricted net asset as of June 30, 2008 is \$101.5 million.

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

The Fund's restricted and designated net assets as of June 30, 2008 are represented below (in thousands):

<b>Restricted Net Assets</b>	
Restricted for Debt Service	\$ 6,691
Restricted for State Revolving Fund Loan	401
Restricted for Operating Reserve	11,987
Restricted for San Felipe Operations	3,637
Restricted for Rate Stabilization	1,295
Sub-total for Restricted Net Assets	<u>24,011</u>
<b>Designated for Operations &amp; Contingencies</b>	
Designated for Encumbrances	39,965
Designated for Market Valuation	527
Designated for Operating and Capital Reserves	14,039
Designated for Supplemental Water Supply	6,791
Designated for Rate Debt Payment Stabilization	303
Sub-total for Designated for Operations & Contingencies	<u>61,625</u>
<b>Designated for Capital Projects</b>	
Designated for Current Authorized Projects	<u>39,903</u>
<b>Investment in Non-current Assets</b>	<u>500,821</u>
<b>Net Assets</b>	<u><u>\$ 626,360</u></u>

**(10) EMPLOYEES' RETIREMENT PLAN**

**Plan Description**

All permanent employees are eligible to participate in the miscellaneous plan with the California Public Employees' Retirement System (CalPERS), an agent multiple-employer public employee defined benefit pension plan. CalPERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries based on member's years of service, age and final compensation. District employees vest after five years of service and are eligible to receive retirement benefits at age fifty. CalPERS acts as a common investment and administrative agent for participating public entities within the State of California. Benefit provisions and all other requirements are established by State statute and District's ordinance. CalPERS issues a separate comprehensive annual financial report. Copies of the CalPERS' annual financial report may be obtained from the CalPERS Executive Office, 400 P Street, Sacramento, CA 95814

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**Funding Status and Progress**

District employees are required to contribute 8.0 percent of their annual covered salary to CalPERS. The District makes the contributions required of District employees on their behalf and for their account. The District is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The actuarial methods and assumptions used are those adopted by the CalPERS Board of Administration. The required employer contribution rate for the District for fiscal year 2007/08 was 13.798 percent. In January 2003, the District amended its contract with CalPERS to include the enhanced retirement formula of 2.5% at 55. District employees pay 2.5% of their salaries towards the District's cost of this amended retirement plan. The contribution requirements of plan members are established by State statute and employer contribution rate is established and may be amended by CalPERS.

**Annual Pension Cost**

For fiscal year 2007/08, the District's annual pension cost of \$11,024,583 for CalPERS was equal to the District's required and actual contributions. The required contribution was determined as part of the June 30, 2007 actuarial valuation using the entry age normal actuarial cost method with the contributions determined as a percent of pay. The actuarial assumptions included (a) 7.75 percent investment rate of return (net of administrative expenses) and (b) projected annual salary increases that vary by duration of service. Both (a) and (b) included an inflation component of 3.0 percent. The actuarial value of CalPERS assets was determined using a technique that smoothes the effects of short-term volatility in the market value of investments over a three-year period. Initial unfunded liabilities are amortized over a closed period that depends on the plan's date of entry into CalPERS. Subsequent plan amendments are amortized as a level percentage of pay over a closed 20-year period. All annual pension costs are paid upon receipt of invoices.

**THREE-YEAR TREND INFORMATION FOR CalPERS**  
(Dollars in Thousands)

Fiscal Year	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
6/30/2006	\$11,293	100%	\$0
6/30/2007	10,425	100%	0
6/30/2008	11,025	100%	0

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**FUNDED STATUS OF PLAN**

(Dollars in Thousands)

Actuarial Valuation Date	Entry Age Normal Accrued Liability (a)	Actuarial Value of Assets (b)	Unfunded Liability/ (Excess Assets) (a)-(b)	Funded Ratio (b)/(a)	Annual Covered Payroll (c)	Unfunded (Overfunded) Actuarial Accrued Liability As a % of Payroll [(a)-(b)]/(c)
6/30/2005	\$306,652	\$257,849	\$48,803	84.1%	\$73,793	66.1%
6/30/2006	331,605	285,793	\$45,812	86.2%	72,982	62.8%
6/30/2007	365,735	318,839	\$46,896	87.2%	76,696	61.1%

**(11) POST-EMPLOYMENT BENEFITS**

The District provides post-employment healthcare benefits, in accordance with negotiated memoranda of understanding with employee groups and adoption by the Board of Directors, for retired employees and/or their surviving spouses who meet the eligibility requirements and elect the option. For employees who retired prior to June 30, 1988 with at least 10 years of service, the District provides reimbursement of medical premiums of \$165 per month payable quarterly.

For employees who retired after June 30, 1988, the District pays 100 percent of medical premiums provided the employee has 10 years of service with the District, the employee retires from the District at minimum age 50, and the employee is receiving a monthly allowance from PERS. For employees who retired after June 30, 1990, the District provides additional medical coverage for one dependent provided the employee has 15 years of service with the District and their dependent does not have coverage from a current employer. For employees who were hired after March 1, 2007, the District pays 100 percent of the medical premiums provided the employee has 15 years of continuous service. An employee retiring with 20 years or more of continuous service will receive medical coverage with the premium paid by the District for the employee plus one eligible dependent.

As of March 1, 2007, all current retirees not yet 65 years of age and Medicare eligible and all future retirees who are Medicare eligible must enroll themselves in Medicare when they reach the eligibility date for Medicare. Their Medicare eligible dependents, who are enrolled in the District's health plan, must also enroll in Medicare upon their eligibility date. The District reimburses the ongoing Medicare Part B cost incurred by the retiree and/or dependent.

Employees retiring from the unclassified group are eligible for dental, vision, and life insurance benefits. The District pays for 100 percent dental and vision premiums to those that retire with at least 10 years of service. The District provides full benefit to one dependent for those that retire with at least 15 years of service. The District provides \$50,000 life insurance amount upon retirement, decreasing by \$10,000 per year after retirement.

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

As of June 30, 2008, there were 272 retirees and 284 active employees eligible for the post employment benefits. The benefit allowance was not established in conjunction with an irrevocable trust or equivalent arrangement in accordance with the parameters of GASB Statement 45. Accordingly, there is no publicly available financial report.

**Funding Policy**

As of June 30, 2008, the District has not established an irrevocable trust fund in accordance with the parameters of GASB Statement 45 and therefore, amounts contributed of \$4,143,981 and \$3,378,861 represent the pay-as-you go amount for the years ended June 30, 2008 and 2007, respectively.

Subsequent to June 30, 2008, the District entered into a trust agreement with California Public Employees' Retirement System (CALPERS) to participate in its Prefunding Plan through California Employer's Retiree Benefit Trust (CERBT) that will administer other post employment benefits obligations on behalf of the District. Additional information on the establishment of a trust account is included in Note 18 – Subsequent Event.

**Annual OPEB Cost and Net OPEB Obligation**

The District's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC), and the amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The following table shows the components of the District's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the District's net OPEB obligation to the Plan:

Annual Required Contribution	\$ 14,212,000
Interest on net OPEB obligation	-
Adjustment to annual required contribution	-
Annual OPEB cost (expense)	14,212,000
Contributions made	<u>4,143,981</u>
Increase in Net OPEB obligation	10,068,019
Net OPEB obligation, beginning of year	-
Net OPEB obligation, end of year	<u>\$ 10,068,019</u>



**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

The annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the net OPEB obligation is as follows:

<u>Year Ended June 30</u>	<u>Annual Required Contribution</u>	<u>Amount Contributed</u>	<u>Percentage Contributed</u>	<u>NET OPEB Obligation</u>
2008	\$14,212,000	\$4,143,981	29.16%	\$10,068,019

**Funded Status and Funding Progress**

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the health cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made in the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the accrued liabilities for benefits.

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets (a)</u>	<u>Actuarial Accrued Liability (AAL) - Entry Age Normal (b)</u>	<u>Unfunded AAL (UAAL) (b-a)</u>	<u>Funded Ratio (a/b)</u>	<u>Covered Payroll (c)</u>
June 30, 2007	\$ -	\$141,459,000	\$141,459,000	-	\$78,300,000

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

The June 30, 2007 actuarial valuation used the Entry Age Normal (EAN) cost method. The actuarial assumptions included a discount rate of 7.75% and a 3% inflation rate. Healthcare cost trend rates ranged from an initial rate range of 11 to 5 percent after eight years. The unfunded liability is being amortized as a percent of payroll over 30 years. The remaining amortization period at June 30, 2008 was 29 years.

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**(12) RISK MANAGEMENT**

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District reports all of its risk management activities in its Risk Management Internal Service Fund.

The District's deductibles and maximum coverage are as follows (in thousands):

<u>Coverage Descriptions</u>	<u>Deductibles</u>	Commercial Insurance <u>Coverage</u>
General liability	\$2,000	\$50,000
Workers' compensation	1,000	Statutory
Property damage (subject to policy sub-limits)	100	125,000
Fidelity (Crime) - Directors	5	1,000
Fidelity (Crime) – Non-Directors	10	2,000
Non-owned aircraft liability	-	5,000
Boiler and machinery	50	500,000

Claims expenses and liabilities are reported for self-insured deductibles when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported, allocated and unallocated claims adjustment expenses and incremental claim expense. Claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors. At June 30, 2008, the liability for self-insurance claims was \$8,566,000. This liability is the District's best estimate based on available information. Settled claims have not exceeded commercial insurance coverage in any of the past three fiscal years.

Changes in the reported liability since June 30, 2006 are as follows (in thousands):

	<u>General Liability</u>	<u>Workers' Compensation</u>	<u>Total</u>
Claims payable at June 30, 2006	\$ 3,840	\$ 5,714	\$ 9,554
Current year premiums, incurred claims and changes in estimates	(703)	529	(174)
Net payments	(35)	(598)	(633)
Claims payable at June 30, 2007	<u>3,102</u>	<u>5,645</u>	<u>8,747</u>
Current year premiums, incurred claims and changes in estimates	870	(461)	409
Net payments	(160)	(430)	(590)
Claims payable at June 30, 2008	<u>\$ 3,812</u>	<u>\$ 4,754</u>	<u>\$ 8,566</u>

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

**(13) TRANSFERS IN AND OUT**

Transfers are used to 1) move revenues from the fund that statute or budget requires to collect them to the fund that statute or budget requires to expend them, 2) move receipts to debt service from the funds collecting the receipts to the debt service fund as debt service payments become due, and 3) move debt proceeds held in the construction fund to the funds incurring the construction expense.

In the year ended June 30, 2008, the Fund transferred \$882 thousand to General Fund and \$516 thousand to Clean, Safe Creek & Natural Flood Protection Program Fund for its share in information technology and capital projects relevant to water operations.

Interfund transfers for the year ended June 30, 2008, is as follows (in thousands):

Fund Receiving Transfers	Fund Making Transfers	Amount Transferred
General Fund	Water Enterprise	\$ 882
Clean Safe Creek & Natural Flood	Water Enterprise	516
Total interfund transfers		\$ 1,398

**(14) COMMITMENTS**

**(a) Contract and Purchase Commitments**

As of June 30, 2008, the Fund had open purchase commitments of approximately \$41.5 million related to new or existing contracts and agreements. These encumbrances represent commitments for the expenditure of funds and do not represent expenditures or liabilities.

**(b) State Water Project Water Deliveries**

The District has contracted with the State for water deliveries from the State Water Project. Under the terms of the contract, the District secured rights to obtain 6,510,783 acre-feet of water, of which, 3,560,783 acre-feet of water have been allotted through June 30, 2006. The contract requires the District to reimburse the State for capital costs (including interest thereon) and minimum operating, maintenance, power, and replacement costs of the State Water Project transportation and conservation facilities. The State annually reestimates the District's total commitment for reimbursement of such costs.

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

A summary of the currently estimated remaining commitment to the State through 2035 is as follows (in thousands):

Transportation Charges:

Capital cost component, including principal and interest	\$80,418
Operations and maintenance	246,598
Delta water charges	76,700
Water revenue bond surcharges	32,793
Total State Water Project Commitment	<u>\$436,509</u>

**(c) San Felipe Project Water Deliveries**

The District has also contracted with the U.S. Department of the Interior for water deliveries from the San Felipe Project. Under the terms of the contract, the District secured Rights to a minimum of 4,022,900 acre-feet of water, of which 2,005,402 acre-feet of water have been received through June 30, 2006. The contract requires the District to operate and maintain its share of the facilities.

During Fiscal Year 2007, the District amended this contract. The amended contract provided for compliance with the Central Valley Project Improvement Act and converted the repayment of the San Felipe Division facilities from a water service contract to a repayment contract with fixed semi-annual payments. The semi-annual payments for January 2007 through July 2016 are \$7,466,867. The amended contract preserved the attributes of a water service contract for other Central Valley Project costs.

The estimated commitment for the payment of allocated capital and capital interest charges of the contracted water service component as of June 30, 2008 was \$26,728,938. The total commitment, including applicable interest, of the repayment contract was \$439,261,342. The remaining commitment as of June 30, 2008 was \$416,860,742.

**(d) Participation Rights in Storage Facilities**

In December 1995, the District entered into a water banking and exchange program with Semitropic Water Storage District and its Improvement Districts that entitles the District to storage, withdrawal, and exchange rights for the District's water supplies. The District's share of the total program capital costs is \$46.9 million based on a 35 percent vesting in the program. The District pays the program capital costs when storing and recovering Tier 1 water. The agreement terminates in December 2035.

The District pays the program capital costs when storing and recovering Tier 1 water. As of June 30, 2008, the District has paid \$39.5 million towards the obligation of this agreement. During the first 10 years, the District had a reservation for the full 35 percent allocation; by January 1, 2006, if the District's contributions towards the program capital

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

costs did not equal \$46.9 million, the District's permanent storage allocation would have been reduced.

The District decided to utilize its total allowable storage rights at 35 percent on January 1, 2006.

The District currently has a storage allocation of 350,000 acre-feet. As of June 30, 2008, the District has 241,108 acre-feet of water in storage. The participation rights are amortized using the straight-line method over the life of the agreement. Amortization of \$14,656,000 has been recorded through fiscal year 2008.

**(15) CONTINGENCIES**

**(a) Litigation**

The District is a defendant or co-defendant in a number of lawsuits for property damages and/or personal injuries. Although the outcome of the lawsuits is not presently determinable, counsel for the District has indicated that material losses, if any, arising from these lawsuits are adequately provided for under indemnification agreements or insurance coverage and therefore would not have a material effect on the June 30, 2008 basic financial statements.

**(b) Grants and Subventions**

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

**(c) Central Valley Project**

On June 7, 1977, the District entered into a contract with the U.S. Bureau of Reclamation for water service from the San Felipe Division of the Federal Central Valley Project (CVP). The CVP water service provides for both agricultural operation and maintenance (O&M) and municipal and industrial (M&I) water deliveries to the District up to a total maximum annual entitlement of 152,500 acre-feet per year. The contract specified initial water rates for O&M and M&I water service and provided for periodic adjustments for the respective water rates in accordance with prevailing CVP water rate policies commencing in the year 1993 for the in-basin M&I rate component; 1996 for the agricultural O&M rate component; 2001 for the full agricultural water rate; and 2008 for the out-of-basin M&I rate component. The methodology of CVP water rate setting has historically recovered current year operating costs and the applicable construction costs over 50 years.

The District's initial CVP water rates were determined based on a November 1974 CVP water rate policy and estimated construction costs of the San Felipe Division. The actual construction costs of the San Felipe Division were significantly higher than the estimates

**WATER UTILITY ENTERPRISE FUND  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2008

used in the initial rate calculation, and changes in the Federal Reclamation Law during the 1980's led to development of new CVP water rate policies. These policies, coupled with the terms of the original contract, resulted in the District facing significant rate increases for repayment of the San Felipe Division.

In compliance with the Central Valley Improvement Act (CVPIA) the District entered into negotiations, along with all other CVP contractors, with the U.S. Bureau of Reclamation for contract renewal. Because of concerns related to litigation challenging the renewal process, the District entered into an amended contract. The amendment maintained the basic provisions of the original contract, implemented provisions of CVPIA, and allowed the establishment of a fixed repayment for the San Felipe Division facilities.

In past years, to minimize the potential adverse effects of possible future CVP water rate increases, the District collected additional revenue through its water rates. The District has designated the related incremental portion of net assets of the Water Enterprise Fund as Designated for CVP. However, the District recently determined that the risk of being required to fund a future liability associated with the original contract with the U.S. Bureau of Reclamation had been substantially eliminated. Consequently, \$16.1 million was reallocated from Designated for CVP to the Supplemental Water Supply and Operating and Capital Reserves.

**(d) Perchlorate**

In 2003, an investigation performed under the direction of state water officials detected a chemical called perchlorate in several water wells in South County. Although the contamination is under the jurisdiction of the Central Coast Regional Water Quality Control Board, the District applied its significant resources to assess the extent of the perchlorate contamination. In addition to offering free well testing within the initial study area, the District's groundwater experts continue to provide technical assistance to the investigation. The responsibility for assessing the problem and cleaning up the contamination resided with the Olin Corporation. The District's involvement is supporting local, state, and federal efforts to ensure a safe water supply and groundwater cleanup.

**(16) SUBSEQUENT EVENT**

**a. OPEB funding**

On June 24, 2008, the Board of Directors adopted a resolution approving the agreement and election of the Santa Clara Valley Water District to prefund other post employment benefits

through California Public Employees' Retirement System (CALPERS) under its California Employer's Retiree Benefit Trust (CERBT) Program. The Board of Directors approved the transfer of \$17.7 million from the Compensated Absences Reserve to CERBT for the initial funding of OPEB. The agreement between the District and CERBT was signed on September 9, 2008. The initial contribution of \$19.6 million was wired to CALPERS/CERBT Trust Fund on September 16, 2008, that includes the \$17.7 million

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from Compensated Absences Reserve plus the fiscal year 2009 contribution of \$1.9 million.

**b. Recent financial market volatility and its impact to the District**

The recent financial market volatility signaled economic and financial turmoil. On September 7, 2008, the Federal Housing Finance Agency (FHFA), in conjunction with the U.S. Treasury placed government sponsored enterprises Fannie Mae (Federal National Mortgage Association) and Freddie Mac (Federal Home Loan Mortgage Corporation) into conservatorship as part of a four-part plan to strengthen the housing agencies. The U. S. Treasury committed as much as \$100 billion to each company if needed to maintain a positive net worth, provide unlimited short term liquidity if needed, and purchase mortgage-backed securities in the open market. In addition, Lehman Brothers Holdings, Inc. (the fourth largest Wall Street investment bank) declared bankruptcy; Merrill Lynch (the third largest Wall Street firm) agreed to be purchased by Bank of America; American International Group (AIG), once the largest insurance company in the United States, received an \$85 billion emergency loan from the federal government to prevent AIG's bankruptcy; Goldman Sachs and Morgan Stanley changed their regulatory status in order to become commercial banks; Washington Mutual, Inc. was seized by government regulators and sold to JP Morgan Chase & Co.; and the banking operations of Wachovia Bank were purchased by Wells Fargo Bank. On October 3, 2008, the President of the United States signed into law the \$700 billion Emergency Economic Stabilization Act of 2008 in an effort to stabilize the economy.

The District's investment policy adheres to the provisions of California Government Code 53601 and further limitations on the authorized investments, maturities, and maximum portfolio and issuer limits at the time of purchase. The portfolio is invested with the following objectives in specific order: maintenance of safety, liquidity, and yield. As of September 30, 2008, the District's investment portfolio did not include Lehman Brothers Holdings, Inc., AIG, Washington Mutual, Inc. or Wachovia Bank.

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## INDEPENDENT ACCOUNTANTS' REPORT ON APPLYING AGREED-UPON PROCEDURES

The Honorable Members of the Board of Directors of the  
Santa Clara Valley Water District

We have performed the agreed-upon procedures, which were agreed to by the management of the Santa Clara Valley Water District (the District), to review allocation of revenues and expenses between the North and the South Zone of the Water Enterprise service area for the year ended June 30, 2008, for the purpose of determining the rate charges between the two zones. We used the allocation methodologies used by the District's management which involve estimates based on actual revenues and both actual and encumbered expenses between the two zones. Management of the District is responsible for the compliance with District resolutions. The sufficiency of these procedures is solely the responsibility of those specified parties in this report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

### **Agreed Upon Procedures Performed**

1. Verify that the revenues and expenses of the Water Enterprise Fund were properly allocated between the North and South zones consistently between the current and prior years.
2. Verify the reasonableness of the allocation of the budgeted revenues and budgeted expenses by observing the methodologies used by management and by examining the reasonableness of the assumptions behind those allocations.

### **Results of Procedures**

1. The revenues and expenses were allocated between the North and the South zone consistently in the current year compared to the prior year.

2. The allocation of revenues and expenses based on procedures used by management appear to be reasonable. Management has chosen to estimate revenues and expenses based on elements that combine budgetary basis and actual amounts as opposed to actual amounts because management believes that these elements that include budgetary basis and actual amounts will provide a better link for projecting future funds available for determining water rate charges.

We were not engaged to and did not conduct an examination, the objective of which would be the expression of an opinion on compliance. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

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

*Vavrinek, Trine, Day & Co. LLP*

Palo Alto, California  
June 25, 2009