

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

Basic Financial Statements
For the Fiscal Year Ended June 30, 2012

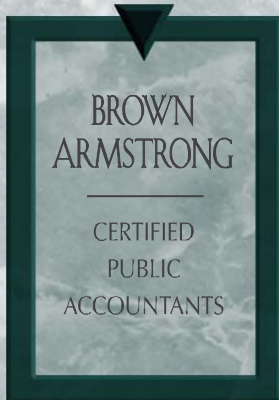
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**WATER UTILITY ENTERPRISE FUND
OF THE
SANTA CLARA VALLEY WATER DISTRICT
Basic Financial Statements
For the Year Ended June 30, 2012**

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BROWN ARMSTRONG
Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

To the Honorable Members of the Board of Directors
Santa Clara Valley Water District
San Jose, California

We have audited the accompanying financial statements of the Water Utility Enterprise Fund of the Santa Clara Valley Water District (the District), as of and for the year ended June 30, 2012, as listed in the table of contents. 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 audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Water Utility Enterprise Fund and do not purport to, and do not, present fairly the financial position of the District as of June 30, 2012, and the changes in its financial position or, where applicable, its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to previously present fairly, in all material respects, the financial position of the Water Utility Enterprise Fund of the District, as of June 30, 2012, and the changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that management's discussion and analysis and the Schedule of Funding Progress - Other Post Employment Benefit Plan as listed in table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

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REGISTERED with the Public Company Accounting Oversight Board and MEMBER of the American Institute of Certified Public Accountants

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Water Utility Enterprise Fund's financial statements. The Schedule of Revenues and Expenses – Budgetary Basis, as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the financial statements. The Schedule of Revenues and Expenses – Budgetary Basis are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 31, 2013, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

*Brown Armstrong
Accountancy Corporation*

Bakersfield, California
May 31, 2013

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

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, 2012. 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. The Fund is comprised of two funds – Water Enterprise Fund and State Water Project Fund. The Water Enterprise Fund accounts for ongoing water utility operations and with revenues comprised primarily of charges to the District's groundwater and treated water customers. The State Water Project Fund accounts specifically for state water project tax revenue and state water project contractual costs.

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 Brown Armstrong Accountancy Corporation to conduct an audit of the District's Water Utility Enterprise Fund for the fiscal year ended June 30, 2012. 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:

Management Discussion and Analysis (continued)

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 Fund is improving or deteriorating.

The Statement of Revenues, Expenses and Changes in Net Assets provides information about the Fund's revenues and expenses on an 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)

	2012	2011
Current and other assets	\$ 157,759	\$ 165,312
Capital assets	785,448	736,627
Total assets	943,207	901,939
Current liabilities	46,541	22,460
Litigation - claim	6,738	6,414
Long-term liabilities outstanding	217,301	224,935
Total liabilities	270,580	253,809
Net assets:		
Investment in capital assets, net of related debt	554,316	524,557
Restricted	28,082	26,824
Unrestricted	90,229	96,749
Total net assets	\$ 672,627	\$ 648,130

Management Discussion and Analysis (continued)

- The total net assets of the Fund exceeded its liabilities by \$672.6 million. Of this amount, \$90.2 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 (82.4 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.
- The net increase in the investment in capital assets, net of related debt was \$29.8 million. Major projects contributing to this increase, less any related debts, included Silicon Valley Advanced Water Purification Center of \$36.0 million, Pacheco Pumping Plant Adjustable Speed Drive Replacement of \$5.6 million, Rinconada Water Treatment Plant Facility Renewal Program Primary Electrical System of \$4.0 million and the ongoing major improvements to the water treatment plants.

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

	2012	2011
Revenues:		
Ground water charges	\$ 48,030	\$ 50,384
Treated water charges	92,904	70,135
Surface and recycled water charges	849	828
Operating grants	1,111	1,458
Capital grants and contributions	11,803	10,443
Property taxes	22,327	23,181
Investment income	1,082	1,779
Miscellaneous	2,573	1,575
Total revenues	180,679	159,783
Expenses:		
Operating expenses	150,605	147,338
Nonoperating and other expenses	8,858	8,790
Total expenses	159,463	156,128
Increase in net assets before transfers	21,216	3,655
Transfers	3,281	2,811
Increase in net assets	24,497	6,466
Net assets, beginning	648,130	641,664
Net assets, ending	\$ 672,627	\$ 648,130

Management Discussion and Analysis (continued)

- The net assets of the Fund increased by \$24.5 million. Compared to the previous fiscal year, key elements of the changes are as follows:
 - a. Revenues from ground water charges decreased by \$2.4 million or 4.7 percent due to the reduction in the total acre feet of ground water usage. Compared to prior fiscal year 2011, the total acre feet of ground water usage of major customers decreased by approximately 11.6 thousand or 11.2 percent.
 - b. Receipts of treated water charges were higher by \$22.8 million or 32.5 percent primarily due to higher acre feet deliveries of treated water as well as increase in treated water rate of 8 percent. The total acre feet deliveries of treated water were up by approximately 25.6 thousand or approximately 22.7 percent, if compared to prior fiscal year 2011.
 - c. Operating grants decreased by \$347 thousand or 23.8 percent. The decrease was caused by lower operating grants received from the County of Alameda for the Residential Water Conservation Program and from the San Benito Water District from reimbursement associated with the operation and maintenance of certain San Felipe Division facilities.
 - d. Capital grants and contributions increased by \$1.4 million or 13.0 percent due to the \$3.8 million increase in the reimbursement from the City of San Jose for the Recycled Water Facilities and Program Integration agreement, offset by decreases in reimbursements from the following agencies: United States Department of Interior for the Recycled Water Treatment Program by \$1.3 million, San Benito County Water District on San Felipe Division capital projects by \$113 thousand, United States Department of Water Resources on the San Luis Bypass Feasibility Study Program for Safe Drinking Water and Flood Protection by \$829 thousand, and County of Santa Clara for the Grant Jacques Gulch Project by \$237 thousand.
 - e. Property taxes decreased by \$854 thousand or 3.7 percent due to the decrease in the property tax received for the State Water Project.
 - f. Investment earnings decreased by \$697 thousand or 39.2 percent due to lower interest rates and net negative impact from the GASB 31 fair market value adjustment of \$363 thousand.
 - g. Miscellaneous revenues increased by \$998 thousand or 63.4 percent due to one-time purchase of imported water by the United States Bureau of Reclamation in the amount of \$750 thousand and a \$130 thousand Power Cost Reconciliation refund received from the Power and Water Resources Pooling Authority.
 - h. Total operating expenses increased by \$3.3 million or 2.2 percent due to the \$3.1 increase in the cost of water purchases as a result of higher volume of water deliveries. In addition, there has been an increase in the price of chemicals used to treat the water.

Management Discussion and Analysis (continued)

- i. Non-operating and other expenses increased by \$68 thousand due to costs of implementing the commercial paper program that was offset by lower interest on long-term debts.

Water Utility Enterprise Fund's Schedule of Revenues and Expenses

(Budgetary Basis)
(Dollars in Thousands)

	<u>North County</u>		<u>South County</u>		<u>Total</u>	
	<u>2012</u>	<u>2011¹</u>	<u>2012</u>	<u>2011¹</u>	<u>2012</u>	<u>2011¹</u>
Operating Revenues:						
Ground water charges	\$ 38,817	\$ 41,750	\$ 9,213	\$ 8,634	\$ 48,030	\$ 50,384
Treated water charges	92,904	70,135	-	-	92,904	70,135
Surface and recycled water charges	471	512	378	316	849	828
Total water charges	<u>132,192</u>	<u>112,397</u>	<u>9,591</u>	<u>8,950</u>	<u>141,783</u>	<u>121,347</u>
Operating grants	1,032	1,360	79	98	1,111	1,458
Other	123	14	-	-	123	14
Total Operating revenues	<u>133,347</u>	<u>113,771</u>	<u>9,670</u>	<u>9,048</u>	<u>143,017</u>	<u>122,819</u>
Operating Expenses:						
Source of supply	59,895	60,524	6,850	6,304	66,745	66,828
Water treatment	27,735	24,869	19	15	27,754	24,884
Transmission and distribution:						
Raw water	6,597	6,805	1,810	1,652	8,407	8,457
Treated water	<u>1,818</u>	<u>2,872</u>	<u>24</u>	<u>62</u>	<u>1,842</u>	<u>2,934</u>
Cost of goods sold	96,045	95,070	8,703	8,033	104,748	103,103
Administration and general	14,202	13,976	2,677	2,757	16,879	16,733
Capital cost recovery	<u>(2,859)</u>	<u>(2,777)</u>	<u>2,859</u>	<u>2,777</u>	<u>-</u>	<u>-</u>
Total operating expenses	<u>107,388</u>	<u>106,269</u>	<u>14,239</u>	<u>13,567</u>	<u>121,627</u>	<u>119,836</u>
Operating income (loss)	25,959	7,502	(4,569)	(4,519)	21,390	2,983
Non-operating income (expenses):						
Property taxes	20,341	21,169	1,986	2,012	22,327	23,181
Investment income	1,446	2,325	-	-	1,446	2,325
Rental income	63	59	30	31	93	90
Other	2,298	1,401	59	71	2,357	1,472
Interest/fiscal agent fees	(8,858)	(8,790)	-	-	(8,858)	(8,790)
Open space credit transfer	(6,401)	(6,146)	6,401	6,146	-	-
Interest earned credit	58	195	(58)	(195)	-	-
Perchlorate response costs	<u>2,243</u>	<u>2,404</u>	<u>(2,243)</u>	<u>(2,404)</u>	<u>-</u>	<u>-</u>
Net non-operating income	<u>11,190</u>	<u>12,617</u>	<u>6,175</u>	<u>5,661</u>	<u>17,365</u>	<u>18,278</u>
Income (loss)	<u>\$ 37,149</u>	<u>\$ 20,119</u>	<u>\$ 1,606</u>	<u>\$ 1,142</u>	<u>\$ 38,755</u>	<u>\$ 21,261</u>

¹Fiscal year 2010-11 property taxes, open space credit transfer, and interest earned credit allocations between North and South County were restated to reflect corrections resulting in a decrease in North County income and an increase in South County income of \$153 thousand.

Management Discussion and Analysis (continued)

- The Fund's total revenues from water charges were \$141.8 million in fiscal year 2011-12. Ninety-three percent of those revenues, or \$132.2 million were collected from customers in the North County, while the remaining seven percent or \$9.6 million were collected from South County customers.
- Operating grants applied for and received were \$1.0 million to augment North County revenue and \$79 thousand in the South County. These grants helped to fund water conservation, desalination, and recycled/reclaimed water programs.
- Operating expenses for the North County include \$96.0 million in cost of goods sold, or 72 percent of its total operating revenues. Whereas, for the South County, cost of goods sold is \$8.7 million or 90 percent of its total operating revenues.
- Administration and general expenses make up 11 percent of total operating revenues in the North County and 28 percent of total operating revenues in the South County.
- Total operating revenues of \$143.0 million less total operating expenses of \$121.6 million results in a \$21.4 million gain from operations. The gain from North County operations is \$26.0 million, while the loss from South County operations is \$4.6 million.

Operations is supplemented with property tax and investment earnings of \$23.8 million overall.

- Property taxes collected in the North County amounted to \$20.3 million while \$2.0 million were collected in South County for a total of \$22.3 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.
- \$1.4 million of investment earnings resulted from an average return of 0.85 percent on average monthly cash balances of \$111.9 million was allocated to the North County.

Overall net income was \$38.7 million. A total of \$37.1 million income was allocated to North County and \$1.6 million gain was allocated to South County.

Management Discussion and Analysis (continued)

The following table shows the rates for water services for fiscal year 2010-12:

*Water Utility Enterprise Fund's Rate Summary
Adopted 2011-12*

	Rate
<u>Groundwater</u>	
North County – Agricultural	\$ 17.10
North County – Non-Agricultural	569.00
South County – Agricultural	17.10
South County – Non-Agricultural	285.00
<u>Treated Water</u>	
Contract (Scheduled)	669.00
Non-Contract	619.00
<u>Untreated Water</u>	
North County – Agricultural	17.10
North County – Non-Agricultural	569.00
South County – Agricultural	17.10
South County – Non-Agricultural	285.00
<u>Water Master</u>	12.17
<u>Minimum Charge</u>	
North County	426.75
South County	213.75
<u>Reclaimed Water</u>	
Gilroy Reclamation Facility – Agricultural	41.50
Gilroy Reclamation Facility – Non-Agricultural	275.00

Note: The surface water charge is the sum of the basic user charge plus the water master charge.

Capital Assets

The Fund's investment in capital assets as of June 30, 2012, amounts to \$785.4 million (net of accumulated depreciation). The investment in capital assets includes intangible rights, land, construction in progress, buildings, structures and improvements, machinery and equipment. During fiscal year 2011-12, the total increase in the Fund's investment in capital assets for the current year was \$48.8 million.

Major capital projects expenses during the current fiscal year include the following (in millions):

- Silicon Valley Advanced Water Purification Center - \$36.0
- Pacheco Pumping Plant Adjustable Speed Drives Replacement - \$5.6
- Rinconada Water Treatment Plant Facility Renewal Program Primary Electrical System - \$4.0

Management Discussion and Analysis (continued)

- Recycled Water Master Plan Short Term - \$2.4
- Anderson Dam Seismic Retrofit - \$2.0
- Lower Berryessa Creek Lower Penitencia Calaveras - \$2.0
- Dam Safety Seismic Stability - \$2.0
- Santa Teresa Water Treatment Plant Incompatible Study Materials - \$1.6
- Santa Teresa Water Treatment Plant Standby Power System Upgrade - \$1.4

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

	<u>2012</u>	<u>2011</u>
Land	\$ 17,594	\$ 17,594
Contract water and storage rights	57,872	60,294
Buildings	2,759	2,819
Structures and improvements	405,166	395,986
Equipment	7,409	7,222
Construction in progress	<u>294,648</u>	<u>252,712</u>
Total	<u>\$ 785,448</u>	<u>\$ 736,627</u>

Information on the Fund's capital assets activity for fiscal year 2011-12 can be found in Note 6 on page 31-32 of this report.

Management Discussion and Analysis (continued)

Debt Administration

On December 17, 2002, the District Board of Directors authorized a commercial paper program. On May 15, 2012, the execution and delivery of certain agreements in connection with the District's commercial paper program in an aggregate amount not to exceed \$100 million was approved by the District Board of Directors.

As of June 30, 2012, the Fund had \$16.7 million outstanding short-term debt consisting of non-taxable commercial paper for \$13.0 million and taxable commercial paper for \$3.7 million.

At the end of the current fiscal year, the Fund had total long term debt outstanding of \$230.3 million. This Fund's long-term obligations outstanding as of June 30, 2012 consisted of the following:

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

	2012	2011
General obligation bonds	\$ -	\$ 405
Revenue bonds	210,480	215,440
Compensated absences	4,722	7,706
Semitropic water banking	6,045	6,045
State revolving fund	5,445	5,711
Other post employment benefits	4,425	3,872
Litigation claim	6,738	6,414
Bond discount	(829)	(868)
Deferred amount on refunding	(2,319)	(2,442)
Deferred interest swap	(7,007)	(7,289)
Premium on bond issue	2,648	2,755
Total	\$ 230,348	\$ 237,749

The Fund's outstanding long-term obligations as of the end of the current fiscal year decreased by a net of \$7.4 million. The decreases in obligations were from the normal repayment of principal on existing outstanding debts.

The bond rating of the revenue bonds of the Fund from is Aa1 from Moody's and AA from Standard & Poor's.

Additional information on the Fund's long-term debt can be found in note 7 on pages 32 to 37 of this report.

Management Discussion and Analysis (continued)

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 for current and future generations"

In considering the District's budget for fiscal year 2012-13, the Board of Directors and District management issued the following directions:

- Reduce the FY2012-13 budget by \$27.4 million from FY2011-12 for a total Operating and Capital budget of \$285.2 million.
- \$2.2 million savings from reduced staffing over FY2011-12.
- 12 scheduled capital construction projects expected to create 800-1600 local jobs.
- \$41.4 million expected in external funding.

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 95118, or call (408) 265-2600.

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

Statement of Net Assets

June 30, 2012

(Dollars in Thousands)

	Water Enterprise Fund	State Water Project Fund	Total
ASSETS			
Current assets:			
Cash and investments (Note 3)	\$ 116,353	\$ 4,727	\$ 121,080
Restricted cash and investments (Note 3)	6,801	-	6,801
Receivables:			
Accounts	24,461	-	24,461
Taxes	29	71	100
Due from other governments (Note 9)	354	-	354
Due from other funds (Note 14)	989	-	989
Deferred charge	1,165	-	1,165
Deposits and other assets	2,809	-	2,809
Total current assets	152,961	4,798	157,759
Non current assets:			
Capital assets: (Note 6)			
Contract water rights, net	35,206	22,666	57,872
Nondepreciable	312,242	-	312,242
Depreciable, net	415,334	-	415,334
Total non current assets	762,782	22,666	785,448
Total assets	915,743	27,464	943,207
LIABILITIES			
Current liabilities:			
Accounts payable	13,836	364	14,200
Accrued liabilities	6,050	88	6,138
Commercial paper, net of discount (Note 7)	16,670	-	16,670
Deposits payable	2,451	-	2,451
Accrued interest payable	760	-	760
Deferred revenue	13	-	13
Claims payable (Note 13)	-	-	-
Revenue bonds - current (Note 7)	4,864	-	4,864
Other Debt (Note 7)	1,445	-	1,445
Total current liabilities	46,089	452	46,541
Non current liabilities:			
Litigation claim (Note 17)	6,738	-	6,738
Long-term debt: (Note 7)			
Revenue bonds (net of unamortized discount and deferred amount on refunding)	198,108	-	198,108
Claims payable (Note 13)	-	-	-
Other post employment benefits payable (Note 12)	4,425	-	4,425
Other debt	14,768	-	14,768
Total long-term debt	217,301	-	217,301
Total non current liabilities	224,039	-	224,039
Total liabilities	270,128	452	270,580
NET ASSETS (Note 10)			
Investment in capital assets, net of related debts	531,650	22,666	554,316
Restricted	23,736	4,346	28,082
Unrestricted	90,229	-	90,229
Total net assets	\$ 645,615	\$ 27,012	\$ 672,627

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, 2012
(Dollars in Thousands)

	Water Enterprise Fund	State Water Fund	Total
Operating revenues:			
Ground water production charges	\$ 48,030	\$ -	\$ 48,030
Treated water charges	92,904	-	92,904
Surface and recycled water revenue	849	-	849
Operating grants	1,111	-	1,111
Charges for services	-	-	-
Other	123	-	123
Total operating revenues	<u>143,017</u>	<u>-</u>	<u>143,017</u>
Operating expenses:			
Sources of supply	51,371	18,941	70,312
Water treatment	28,281	-	28,281
Transmission and distribution:			
Raw water	9,777	-	9,777
Treated water	1,998	-	1,998
Administration and general	17,648	-	17,648
Claims and Adjustments	325	-	325
Equipment maintenance	-	-	-
Insurance	-	-	-
Depreciation and amortization	21,320	944	22,264
Total operating expenses	<u>130,720</u>	<u>19,885</u>	<u>150,605</u>
Operating income (loss)	<u>12,297</u>	<u>(19,885)</u>	<u>(7,588)</u>
Nonoperating revenues (expenses):			
Property taxes (Note 8)	4,491	17,836	22,327
Investment income (Note 5)	1,082	-	1,082
Rental income	93	-	93
Other	1,117	1,240	2,357
Interest and fiscal agent fees	(8,858)	-	(8,858)
Net nonoperating revenues	<u>(2,075)</u>	<u>19,076</u>	<u>17,001</u>
Income before capital contributions and transfers	10,222	(809)	9,413
Capital contributions (Note 4)	11,803	-	11,803
Transfers in (Note 15)	3,281	-	3,281
Change in net assets	25,306	(809)	24,497
Net assets, beginning of year	620,309	27,821	648,130
Net assets, end of year	<u>\$ 645,615</u>	<u>\$ 27,012</u>	<u>\$ 672,627</u>

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, 2012

(Dollars in Thousands)

	Water Enterprise Fund	State Water Fund	Total
Cash flows from operating activities:			
Receipts from customers and users	\$ 143,103		\$ 143,103
Payments to suppliers	(40,141)	(18,211)	(58,352)
Payments to employees	(53,994)	-	(53,994)
Payments for internal services used	(3,513)	-	(3,513)
Other receipts	1,117	1,240	2,357
Net cash provided (used) by operating activities	<u>46,572</u>	<u>(16,971)</u>	<u>29,601</u>
Cash flows from noncapital financing activities:			
Property taxes received	4,491	17,860	22,351
Transfers in from other funds	3,281	-	3,281
Net cash provided by noncapital financing activities	<u>7,772</u>	<u>17,860</u>	<u>25,632</u>
Cash flows from capital and related financing activities:			
Principal payments on general obligation bonds	(405)	-	(405)
Principal payments on revenue bonds	(4,960)	-	(4,960)
Principal payments on other loans	(266)	-	(266)
Proceeds from issuance of commercial paper	16,670	-	16,670
Capital contributions received	11,803	-	11,803
Interest and fiscal agent fees paid	(8,472)	-	(8,472)
Acquisition of contract water rights	(7,137)	-	(7,137)
Acquisition and construction of capital assets	(63,948)	-	(63,948)
Net cash used by capital and related financing activities	<u>(56,715)</u>	<u>-</u>	<u>(56,715)</u>
Cash flows from investing activities:			
(Decrease) in restricted investments	(1,532)	-	(1,532)
Rental income received	93	-	93
Interest received on cash and investments	1,082	-	1,082
Net cash used by investing activities	<u>(357)</u>	<u>-</u>	<u>(357)</u>
Net (decrease) in cash and cash equivalents	(2,728)	889	(1,839)
Cash and cash equivalents, beginning of year	119,085	3,838	122,923
Cash and cash equivalents, end of year	<u>\$ 116,357</u>	<u>\$ 4,727</u>	<u>\$ 121,084</u>
Cash and cash equivalents are reported on the Statement of Net Assets as follows:			
Cash and investments	\$ 116,353	\$ 4,727	\$ 121,080
Restricted cash and investments	6,801	-	6,801
Less cash and investments not meeting the definition of cash equivalents	(6,797)	-	(6,797)
Cash and cash equivalents, end of year	<u>\$ 116,357</u>	<u>\$ 4,727</u>	<u>\$ 121,084</u>
Reconciliation of operating income (loss) to net cash provided by operating activities:			
Operating income (loss)	\$ 12,297	\$ (19,885)	\$ (7,588)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:			
Depreciation and amortization	21,320	944	22,264
Other receipts	1,117	1,240	2,357
Change in operating assets and liabilities:			
Decrease in deposits and other assets	6,801	278	7,079
(Increase)/decrease in accounts receivable	1,070	-	1,070
Increase in due to due from other funds	(989)	-	(989)
(Increase)/decrease in property tax receivable	5	-	5
Decrease in prepaid asset	-	-	-
Decrease in inventory	5	-	5
Decrease in accounts payable	5,996	364	6,360
Increase/(decrease) in accrued liabilities	377	88	465
Increase/(decrease) in deferred revenue	13	-	13
Decrease in deposits payable	666	-	666
Increase in claims payable	-	-	-
Increase in litigation claim	325	-	325
Increase in other post employment benefits & compensated absences	(2,431)	-	(2,431)
Net cash provided (used) by operating activities	<u>\$ 46,572</u>	<u>\$ (16,971)</u>	<u>\$ 29,601</u>

See accompanying notes to basic financial statements.

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

Notes to Basic Financial Statements
For the Year Ended June 30, 2012

(1) THE FINANCIAL REPORTING ENTITY

(a) Description of the Reporting Entity

Santa Clara Valley Water District (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 supervisorial 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.

On October 12, 2009, Assembly Bill 466 was signed by the Governor of California revising the composition of the board of the District by requiring the board to transition to an all-elected board that, on or after noon on December 3, 2010, consists of seven directors who are elected pursuant to specified requirements. The board also would be required to adopt a resolution establishing boundaries of the seven electoral districts. On May 14, 2010, the Board of Directors adopted a resolution that officially set the boundaries of the seven electoral districts. In November, 2010, two directors were elected to represent the new electoral districts constituting a new board of seven members. As required by state law, the District must redraw its boundaries to reflect 2010 Census results. On October 11, 2011, the Board of Directors adopted Resolution No. 11-63 selecting the Redistricting Plan, known as the Current Adjusted Map.

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. The Fund is comprised of two funds – Water Enterprise Fund and State Water Project Fund. The Water Enterprise Fund accounts for ongoing water utility operations and with revenues comprised primarily of charges to the District's groundwater and treated water customers. The State Water Project Fund accounts specifically for state water project tax revenue and state water project contractual costs.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of Presentation

Fund Financial Statements

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.

(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.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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. *Non-operating* revenues, such as subsidies and investment earnings, result from non-exchange 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 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 Fund 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.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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	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 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.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

(j) Due from Other Governments

Amounts due from other governments represent amounts due from various government agencies for reimbursement of the District's expenditures/expenses in association with construction projects.

(k) 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, up to 480 hours of accrued sick leave shall be paid to the eligible employee at the rate of 50% of the equivalent cash value. Upon resignation with ten or more years of service or upon separation by layoff regardless of service, up to 480 hours of accrued sick leave shall be paid off at the rate of 25% of the cash value.

(l) 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 Revenue Bond and Certificate of Participation premiums, 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. Issuance costs are reported as deferred charges.

(m) 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.

(n) 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.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

(o) New Pronouncements

Recently Released Standards by GASB

Following is the list of recently released stands by the Governmental Accounting Standard Board which may or may not affect the District's future fiscal years financial reporting.

GASB Statement No. 60 – *Accounting and Financial Reporting for Service Concession Arrangements* addresses accounting and financial reporting issues related to public-private and public-public partnerships. The statement is effective for periods beginning after December 15, 2011. The District has not fully judged the effect of the implementation of GASB Statement No. 60 as of the date of the basic financial statements.

GASB Statement No. 61 – *The Financial Reporting Entity: Omnibus, an amendment of GASB Statements No. 14 and 34* modifies a number of provisions with regard to reporting of component units within a financial reporting entity. The statement is effective for periods beginning after June 15, 2012. As of the date of the basic financial statements, the District has not made an assessment of any changes that occur upon this statement's implementation.

GASB Statement No. 62 – *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989, FASB and AICPA Pronouncements* incorporates into the GASB's authoritative literature certain accounting and financial guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements: FASB Statements and Interpretations, APB Opinions, and ARBs of the American Institute of Certified Public Accountants' (AICPA) Committee on Accounting Procedure. The statement is effective for periods beginning after December 15, 2011. However, as the statement codifies what is in current practice, there is no effect on the District's accounting or financial reporting upon the statement's implementation.

GASB Statement No. 63 – *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* modifies current financial reporting of those elements. The largest change will be the replacement of the current Statement of Net (Plan if retirement entity) Assets with a Statement of Net (Plan) Position and a Statement of Changes in Net Position instead of the current Statement of Changes in (Plan) Net Assets upon implementation for periods beginning after December 15, 2011. The District will implement this change for the fiscal year ended June 30, 2013.

GASB Statement No. 64 – *Derivative Instruments: Application of Hedge Accounting Termination Provisions* amends current accounting and financial reporting related to termination of swap agreements due to default or other termination events. In certain instances where swap counterparties or credit support providers are replaced, hedge accounting may continue, rather than cease. The provisions of GASB Statement No. 64 are effective for financial statements beginning after June 15, 2011. As of the date of the basic financial statements, the District has not made an assessment of any changes that will occur upon this statement's implementation.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

GASB Statement No. 65 – *Items Previously Reported as Assets and Liabilities.* The provisions of GASB Statement No. 65 are effective for financial statements beginning after December 15, 2012. The District will implement this change for the fiscal year ended June 30, 2013.

GASB Statement No. 66 – *Items Technical Corrections – 2012 – an amendment of GASB Statements No. 10 and No. 62.* The provisions of GASB Statement No. 66 are effective for financial statements beginning after December 15, 2012. As of the date of the basic financial statements, the District has not made an assessment of any changes that will occur upon this statement's implementation.

GASB Statement No. 67 – *Financial Reporting for Pension Plans – an amendment of GASB Statement No. 25.* The provisions of GASB Statement No. 67 are effective for financial statements beginning after June 15, 2013. The District has not fully judged the effect of the implementation of GASB Statement No. 67 as of the date of the basic financial statements.

(3) CASH AND INVESTMENTS

Total Fund cash and investments at June 30, 2012 are as follows (in thousands):

Statement of Net Assets:	
Cash and investments	\$ 121,080
Restricted cash and investments	6,801
	<u>\$ 127,881</u>

Investments

At June 30, 2012, cash and investments consist of the following (in thousands):

Guaranteed Investment Contracts	\$ 4,745
Money Market Funds	125
Cash	15
US Treasury Notes	399
Mutual Funds	<u>1,513</u>
Total Investments Held by Fiscal Agent	6,797
Santa Clara County Investment Pool	4
District's Pooled Cash and Investment	<u>121,080</u>
Total cash and investments	<u>\$ 127,881</u>

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

As of June 30, 2012, the District's investment in the State investment pool (LAIF) is \$50,061,000. The total amount invested by all public agencies in LAIF at that date is \$60,502,186,000. Of that amount, 96.53 percent is invested in non-derivative financial products and 3.47 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, 2012, the Fund's investment in the Santa Clara County Investment Pool (Pool) is \$4,120 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 District shares in the Pool is determined on an amortized cost basis, which is different than the fair value of the District's position in the Pool. The District'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 table 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
SANTA CLARA VALLEY WATER DISTRICT**

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

<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. Government 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%
Nonnegotiable Time Certificates of Deposit	1 year	N/A	5%	\$250,000 & FDIC 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	12.0%
California Local Agency Investment Fund (B)	N/A	N/A	(B)	(B)
Mutual Funds	N/A	AAA	10%	10.0%
Money Market Account with Union Bank	N/A	N/A	None	12.0%

(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.

(B) District's investment policy is still in process of being revised to match the FDIC limit of \$250,000.

(C) LAIF will accept no more than \$50 million of an agency's unrestricted funds while placing no constraints on funds.

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 2007B Water Utility Revenue Certificates of Participation (COP) and 2006A & 2006B Water Utility Revenue and Refunding Bonds, 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, 2012, the amount invested in assets held by fiscal agent amounted to \$6.370 million and was equal to or in excess of the amount required at that date. A total of \$416 thousand restricted cash and investment is also held by the fiscal agents for payments of the State Revolving Fund Loan and the 1963 Water Utility Bond.

Restricted Cash and Investments for Capital Projects

The Fund has issued commercial paper to provide for any District purposes, including but not limited to, capital expenditure, investment and reinvestment, and the discharge of any obligation or indebtedness of the District. At June 30, 2012, the balance of this fund is \$15,000.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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 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 (G)	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; 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.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

(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.

(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, unsecured and 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. if 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.

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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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):

	<u>Total</u>	<u>12 Months or less</u>	<u>13 to 24 Months</u>	<u>25 to 60 Months</u>	<u>More than 60 Months</u>
U.S. Government Agencies	310,371	152,516	124,162	33,693	-
U.S. Government Agencies - Callable	64,363	-	10,010	54,353	-
U.S. Treasury Obligations	399	-	-	-	399
Local Agency Investment Fund	50,061	50,061	-	-	-
Guaranteed Investment Contracts	4,745	-	-	-	4,745
Santa Clara County Investment Pool	4	4	-	-	-
Mutual Funds	33,549	33,549	-	-	-
Money Market Funds	430	430	-	-	-
	<u>\$ 463,922</u>	<u>\$ 236,560</u>	<u>\$ 134,172</u>	<u>\$ 88,046</u>	<u>\$ 5,144</u>
Fund's Investment in District's Pooled Cash and Investment	<u>\$ 121,080</u>				

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.

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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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, 2012 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	Not Rated
U.S. Government Agencies	\$ 374,734	AA-	\$ -	\$ -	\$ 374,734	\$ -	\$ -
U.S. Treasury Obligations	399	AA-	399	-	-	-	-
Local Agency Investment Fund	50,061	N/A	-	-	-	-	50,061
Guaranteed Investment Contracts	4,745	N/A	-	-	-	-	4,745
Santa Clara County Investment Pool	4	N/A	-	-	-	-	4
Mutual Funds	33,549	AAA	-	33,549	-	-	-
Money Market Funds	430	N/A	-	-	-	-	430
Total Investments	\$ 463,922		\$ 399	\$ 33,549	\$ 374,734	\$ -	\$ 55,240
Fund's Investment in District's Pooled Cash and Investment	<u>\$ 121,080</u>						

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, 2012, those investments consisted of (in thousands):

Issuer	Investment Type	Reported Amount
District-Wide		
Federal Home Loan Mortgage Corp.	U.S. Government Agency	\$46,256
Federal National Mortgage Association	U.S. Government Agency	158,716
Federal Home Loan Bank	U.S. Government Agency	121,575
Federal Farm Credit Bank	U.S. Government Agency	48,187
Fund Level		
FSA Capital Management Services LLC	Guaranteed Investment Contract	4,745

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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 the trust department of the financial institutions in the District's name.

(4) REIMBURSEMENT OF CAPITAL COSTS

The Fund 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 2011-12 (in thousands):

Agencies	Amount
City of San Jose	\$ 6,132
South County Regional Wastewater	103
San Benito County Water District	1,523
US Corps of Engineer	<u>4,045</u>
Total	<u>\$ 11,803</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 Statement of Net Assets. 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.

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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, 2012 (in thousands):

	Interest as Reported	FY 2012 GASB 31 Fair Value Adjustment	Interest Earned Before Adjustment
Water Enterprise	1,082	(363)	1,445

(6) CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2012 was as follows (in thousands):

	Balance July 1, 2011	Additions	Deletions	Transfers / Reclassified	Balance June 30, 2012
Nondepreciable capital assets:					
Land	\$ 17,594	\$ -	\$ -	\$ -	\$ 17,594
Construction in progress	252,712	63,296	-	(21,360)	294,648
Total nondepreciable capital assets	270,306	63,296	-	(21,360)	312,242
Depreciable capital assets:					
Contract water and storage rights	150,537	7,137	-	-	157,674
Buildings	2,992	-	-	-	2,992
Structures and improvements	593,039	-	-	20,429	613,468
Equipment	20,089	652	-	931	21,672
Total depreciable capital assets	766,657	7,789	-	21,360	795,806
Less accumulated depreciation and amortization					
Contract water and storage rights	(90,243)	(9,559)	-	-	(99,802)
Buildings	(173)	(60)	-	-	(233)
Structures and improvements	(197,053)	(11,249)	-	-	(208,302)
Equipment:	(12,867)	(1,396)	-	-	(14,263)
Total accumulated depreciation and amortization	(300,336)	(22,264)	-	-	(322,600)
Net depreciable capital assets	466,321	(14,475)	-	21,360	473,206
Total capital assets, net	\$736,627	\$ 48,821	\$ -	\$ -	\$ 785,448

During fiscal year 2011-12, new construction in progress increased in the Fund by \$63.3 million. Fifty-one projects were in progress during the fiscal year with the major projects listed below (in millions):

- Silicon Valley Advanced Water Purification Center - \$36.0
- Pacheco Pumping Plant Adjustable Speed Drives Replacement - \$5.6
- Rinconada Water Treatment Plant Facility Renewal Program Primary Electrical System - \$4.0

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

- Recycled Water Master Plan Short Term - \$2.4
- Anderson Dam Seismic Retrofit - \$2.0
- Lower Berryessa Creek Lower Penitencia Calaveras - \$2.0
- Dam Safety Seismic Stability - \$2.0
- Santa Teresa Water Treatment Plant Incompatible Study Materials - \$1.6
- Santa Teresa Water Treatment Plant Standby Power System Upgrade - \$1.4

Depreciation expense was charged to projects of the Fund as follows (in thousands):

Total depreciation and amortization expenses	<u>\$22,264</u>
--	-----------------

(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.

On May 15, 2012, the District Board of Directors authorized the execution and delivery of certain agreements in connection with the District's commercial paper program in an aggregate principal amount not to exceed \$100 million. The proceeds of the commercial paper may be used for any District purposes, including but not limited to, capital expenditure, investment and re-investment, and the discharge of any obligation or indebtedness of the District.

As of June 30, 2012, the outstanding non-taxable commercial paper issued was \$12,975,000 with an interest rate of 0.15% to 0.18%, maturing on September 26, 2012, while the outstanding taxable commercial paper was \$3,695,000 with interest rate of 0.19%, maturing on September 26, 2012. The new maturity date of both the taxable and non-taxable commercial papers is December 5, 2012, with interest rate of 0.16% to 0.19%.

The District's short-term outstanding consists of the following, as of June 30, 2012 (in million):

	<u>Authorized</u>	<u>Issued</u>	<u>Available</u>
Commercial Paper Program	\$100	\$16.7	\$83.3

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

(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, 2012</u>	<u>Due Within One Year</u>
2006A Water revenue bond	2035	3.5% - 5%	74,265	63,665	2,055
2006B Water revenue bond	2035	5.15%-5.31%	25,570	22,850	575
2007A Water revenue COP bond	2037	4% - 5.0%	77,270	73,155	1,505
2007B Water revenue COP bond	2037	5.50%-floating	53,730	50,810	1,065
Bond discount				(829)	(38)
Deferred amount on refunding				(2,319)	(123)
Deferrend interest rate swap				(7,007)	(281)
Premium on debt issuance				2,648	106
Compensated absences				4,722	1,172
Other post employment benefits				4,425	-
Semitropic water banking agreement	2035		46,900	6,045	-
State revolving fund loan	2027		6,350	5,445	273
Litigation claim				6,738	-
Total Fund debt				<u>\$ 230,348</u>	<u>\$ 6,309</u>

The following is a summary of changes in long-term liabilities as of June 30, 2012 (in thousands):

	<u>Balance 7/1/2011</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance 6/30/2012</u>	<u>Due Withn One Year</u>
1963 Water Utility bonds	\$ 405	\$ -	\$ (405)	\$ -	\$ -
2006A revenue bonds	65,635	-	(1,970)	63,665	2,055
2006B revenue bonds	23,390	-	(540)	22,850	575
2007A COP revenue bonds	74,585	-	(1,430)	73,155	1,505
2007B COP revenue bonds	51,830	-	(1,020)	50,810	1,065
Bond discount on refunding	(868)	-	39	(829)	(38)
Deferred amount on refunding	(2,442)	-	123	(2,319)	(123)
Deferred interest rate swap	(7,289)	-	282	(7,007)	(281)
Premium on debt issuance	2,755	-	(107)	2,648	106
Compensated absences	7,706	3,439	(6,423)	4,722	1,172
Other post employment benefits	3,872	553	-	4,425	-
Semitropic water banking agreement	6,045	-	-	6,045	-
State revolving fund loan	5,711	-	(266)	5,445	273
Litigation claim	6,414	324	-	6,738	-
Total Fund debt	<u>\$ 237,749</u>	<u>\$ 4,316</u>	<u>\$ (11,717)</u>	<u>\$ 230,348</u>	<u>\$ 6,309</u>

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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

Year Ending June 30:	<u>Principal</u>	<u>Interest and amortization</u>
2013	\$ 5,473	\$ 10,821
2014	5,714	10,567
2015	5,971	10,313
2016	6,268	10,021
2017	6,565	9,717
2018 - 2022	37,841	43,572
2023 - 2027	47,655	33,746
2028 - 2032	54,433	21,571
2033 - 2037	46,005	8,090
Total requirements	<u>215,925</u>	<u>\$ 158,418</u>
Add: unamortized premium on issuance	2,648	
Less: unamortized discount and deferred amount on refunding	(3,148)	
Less: deferred interest swap	(7,007)	
Add: compensated absences	4,722	
Add: other post employment benefits	4,425	
Add: semitropic water banking agreement	6,045	
Add: litigation claim	6,738	
Total principal outstanding at June 30, 2012	<u>\$ 230,348</u>	

The following provides a brief description of the Fund's debt outstanding as of June 30, 2012:

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

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

system. Debt service payments are funded through ad valorem taxes on property. Final debt service payment for this bond was made by the District on March 1, 2012 and the bond is fully paid as of June 30, 2012.

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 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. Additionally, the District used funds accumulated in the 2000A and 2000B Debt Service Reserve Funds, and other 2000A and 2000B Bonds accounts to reduce the size of the 2006A and 2006B Bonds issuance. As a result, the 2000A and 2000B Bonds are considered defeased and the liabilities have been removed from the Statement of Net Assets. 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.

Semitropic Water Banking 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, 2012, the District has paid \$40.5 million towards the obligation of this agreement.

State Revolving Fund Loan

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

In November 2004, the District entered into a loan agreement with the State of California Department of Water Resources, on behalf of State of California Department of Health Services, under the Safe Drinking Water State Revolving Fund Law of 1997 for \$6.3 million. The loan was used to fund the construction of filter-to-waste and wash water clarification projects at the Santa Teresa Water Treatment Plant. At June 30, 2012, the District has paid \$905 thousand towards the principal balance of this obligation.

Litigation Claim

In fiscal year 2009, the District recorded a liability of \$5.9 million, which was the potential judgment amount from the tentative ruling on the case Great Oaks Water Company vs. Santa Clara Valley Water District. On February 3, 2010, the judge issued Judgment After Trial and ordered the District to pay Great Oaks Water Company \$5.9 million plus post judgment interest of \$886.62 per day. The District recorded post judgment interest of \$160 thousand in fiscal year 2009-10, \$324 thousand in fiscal year 2010-11, and \$324 thousand in fiscal year 2011-12. Additional information regarding this litigation is disclosed in Note 17 (a), Contingencies.

Compensated Absences

Compensated absences are paid out of the general fund as an employee benefit expense in the year the expense is realized. Prior to fiscal year 2009, all funds reimbursed the general fund on a pro-rata basis of salary expense cost for the payment of these payouts at the end of each year and the funds were held in the reserve as designated for compensated absences. On June 24, 2008, the Board authorized the transfer of \$17.7 million from the compensated absences reserve to a trust fund to prefund other post employment benefits. Effective fiscal year 2008, the compensated absences liability for the year has been recognized in the District's enterprise funds.

Other Post-Employment Benefits (OPEB)

The District provides post-employment healthcare benefits to retired employees and/or their surviving spouses in accordance with negotiated memoranda of understanding with employee groups and adoption by the Board of Directors. The District implemented the provisions of Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions* during fiscal year 2007-08. OPEB expense and obligation are recognized in the proprietary funds in full accrual basis while governmental funds are in modified accrual basis. OPEB expense and obligation reported in government wide financial statements are recognized in full accrual basis. Additional information on OPEB is disclosed in Note 12, Post-Employment Benefits.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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.

(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 imported water from the State Water Project.

Property tax revenues recorded for the year ended June 30, 2012 are as follow (in thousands):

	Water Enterprise Fund
Property taxes:	
1% tax allocation	\$ 4,256
Voter approved indebtedness:	
State water	17,836
G.O. bonds	235
Total property taxes	\$ 22,327

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. Property taxes are accounted for as collected and remitted by the District within the governmental fund revenues. The proprietary 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.

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

(9) PROPOSITION 1A BORROWING BY THE STATE OF CALIFORNIA

Under the provisions of Proposition 1A and as part of the 2009-10 budget package passed by the California state legislature on July 28, 2009, the State of California borrowed 8% of the amount of property tax revenue, including those property taxes associated with the in-lieu motor vehicle license fee, the triple flip in lieu sales tax, supplemental property tax, apportioned to cities, counties and special districts (excluding redevelopment agencies). The state is required to repay this borrowing plus interest by June 30, 2013. After repayment of this initial borrowing, the California legislature may consider only one additional borrowing within a ten-year period. The amount of this borrowing pertaining to the District was \$4.8 million.

This borrowing by the State of California was recognized as a receivable in the accompanying financial statements. The Fund recognized \$354 thousand as revenues in its financial statement in fiscal year 2009-10.

(10) NET ASSETS

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 represents amounts that are subject to limitations imposed by either a) creditors, grantors, contributors or laws and regulations of other governments, or b) 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.

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

Below is the detailed schedule of the Fund's net assets as of June 30, 2012 (in thousands):

	Water Enterprise Fund	State Projects Fund	Total
Restricted Net Assets			
Debt Service	\$ 6,041	\$ -	\$ 6,041
State Revolving Fund Loan Requirement	401	-	401
San Felipe Emergency Reserve	3,958	-	3,958
Operating Reserve	11,757	-	11,757
Rate Stabilization	1,579	-	1,579
State Water Projects	-	4,346	4,346
Total Restricted Net Assets	23,736	4,346	28,082
Unrestricted Net Assets			
Committed			
Operating & Capital Contingencies	4,895	-	4,895
Currently Authorized Projects	31,742	-	31,742
Floating Rate Debt Payment Stabilization	475	-	475
Supplemental Water Supply	8,658	-	8,658
Total Committed	45,770	-	45,770
Assigned			
Encumbrances	44,150	-	44,150
Market Valuation	309	-	309
Total Assigned	44,459	-	44,459
Total Unrestricted Net Assets	90,229	-	90,229
Investment in capital assets, net of related debt	531,650	22,666	554,316
Net Assets	\$ 645,615	\$ 27,012	\$ 672,627

(11) 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

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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 Q Street, Sacramento, CA 95811.

Funding Status and Progress

District employees are required to contribute 8.0% 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 2011-12 was 16.675%.

In January 2003, the District amended its contract with CalPERS to include the enhanced retirement formula of 2.5% at 55. In December, 2011, the District and its bargaining units agreed on new three-year Memorandum of Understanding (MOU), January 1, 2012 to December 31, 2014. The current MOUs implemented a contract amendment with CALPERS to add a second-tier retirement formula of 2.0 percent at 60. District employees hired on or after March 19, 2012 are covered under this formula with a required contribution of 7.0 percent of their annual covered salary to CALPERS. In addition, the current MOUs require all District employees to contributed 3.0 percent of their salary to reimburse the District's annual required employer contribution. 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 2011-12, the District's annual pension cost of \$14,379,193 for CalPERS was the prepayment contribution. The District elected the Annual Lump Sum Prepayment Option from the June 30, 2009 actuarial valuation and was based on the budgeted salaries for fiscal year 2011-12. The required contribution was determined as part of the June 30, 2009 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.

The required and actual contribution based on the percentage of pay for fiscal year 2011-12 was \$1,266,000 less that the prepayment option due lower cost of salaries. The unused contribution will be used to mitigate the District's long term total unfunded CALPERS retirement liability. The District has decided not to exercise the prepayment option for fiscal year 2012-13 and will utilize the percentage of pay method that provides more savings and less cash flow.

**WATER UTILITY ENTERPRISE FUND
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Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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

Fiscal Year	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
6/30/2010	10,962	100%	\$ -
6/30/2011	11,325	100%	-
6/30/2012	14,379	100%	-

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)
6/30/2009	458,952	375,014	83,938	81.7%	81,324	103.2%
6/30/2010	487,009	400,422	86,587	82.2%	81,624	106.1%
6/30/2011	528,826	429,944	98,882	81.3%	80,604	122.7%

(12) POST-EMPLOYMENT BENEFITS

The District provides post-employment health care 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, and to certain employees who retire due to disability who meet the eligibility requirements and elect the option. The District must be the employee's last CALPERS employer, and the retiree must be receiving a monthly CALPERS retirement pay. As of June 30, 2012, there were 358 retirees and surviving spouses receiving these health care benefits.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

	Hire/Retirement Date	Eligibility Rule (Years of Continuous Service)	District's Required Contribution
<u>Classified</u>	Retired prior to July 1, 1988		Fixed amount of \$165 per month
	Retired from July 1, 1988 through June 30, 1990	10 years	100% medical premium for retiree
	Retired from July 1, 1990 or later and hired prior to December 31, 2006	10 years 15 years	100% medical premium for retiree 100% medical premium for retiree plus one eligible dependent
	Employee Association (AFSCME – Local 101)	10 years	Retiree is covered for medical. Medical premium cost sharing is required with the same contribution percentage as active employees and based on medical premium applicable to active employees or retirees, whichever is less.
	Engineers Society (IFPTE-Local 21) Professional Managers Association (IFPTE – Local 21)	15 years	Retiree plus one eligible dependent are covered for medical. Medical premium cost sharing is required with the same contribution percentage as active employees and based on medical premium applicable to active employees or retirees, whichever is less.
	Hired on or after March 1, 2007	15 years 20 years	Retiree is covered for medical. Medical premium cost sharing is required with the same contribution percentage as active employees and based on medical premium applicable to active employees or retirees, whichever is less. Retiree plus one eligible dependent are covered for medical. Medical premium cost sharing is required with the same contribution percentage as active employees and based on medical premium applicable to active employees or retirees, whichever is less

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

	Hire/Retirement Date	Eligibility Rule (Years of Continuous Service)	District's Required Contribution
Unclassified At Will	Retired prior to July 1, 1988		Fixed amount of \$165 per month
	Retired from July 1, 1988 through June 30, 1990	10 years	100% medical premium for retiree
	Retired from July 1, 1990 through June 18, 1995	10 years	100% medical premium for retiree
		15 years	100% medical premium for retiree plus one eligible dependent
	Retired from June 19, 1995 through October 21, 1996	10 years	100% medical premium for retiree
		15 years	100% medical premium for retiree plus one eligible dependent
25 years		100% medical, dental, and vision coverages for the retiree plus two or more eligible dependents	
Retired from October 22, 1996 or later and hired prior to December 30, 2006	10 years	100% medical premium for retiree	
	15 years	100% medical, dental, and vision coverages for the retiree plus one eligible dependent	
	25 years	100% medical, dental, and vision coverages for the retiree plus two or more eligible dependents	
Hired on or after December 30, 2006 and prior to March 1, 2007	10 years	Medical coverage is provided for retiree. Medical premium cost sharing is required with the same contribution percentage as active employees and based on the medical premium amount applicable to active employees or retirees, whichever is less.	
	15 years	Medical, dental, and vision coverages are provided for retiree and one eligible dependent. Medical premium	

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

	Hire/Retirement Date	Eligibility Rule (Years of Continuous Service)	District's Required Contribution
<u>Unclassified</u> At Will	Hired on or after December 30, 2006 and prior to March 1, 2007	15 years (con't) 25 years	cost sharing is required with the same contribution percentage as active employees and based on the medical premium amount applicable to active employees or retirees, whichever is less. Medical, dental, and vision coverages are provided for retiree plus two or more eligible dependents. Medical premium cost sharing is required with the same contribution percentage as active employees and based on the medical premium amount applicable to active employees or retirees, whichever is less.
	Hired on or after March 1, 2007	15 years 20 years	Retiree is covered for medical. Medical premium cost sharing is required with the same contribution percentage as active employees and based on medical premium applicable to active employees or retirees, whichever is less. Retiree plus one eligible dependent are covered for medical. Medical premium cost sharing is required with the same contribution percentage as active employees and based on medical premium applicable to active employees or retirees, whichever is less.

As of August 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 payable quarterly.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

After an evaluation of the cost savings realized in implementing the Medicare enrollment plan since August 2007, the District decided to expand the Medicare enrollment requirement to all retirees and their eligible dependents that are enrolled in the District's medical plan. As of July 1, 2009, all Medicare eligible retirees and their eligible dependents were required to enroll in Medicare. The District reimburses the Medicare Part B penalty charged by the Social Security Administration to the retirees/dependents due to late enrollment.

The District provides the unclassified group of retiree \$50,000 life insurance upon retirement with a five-year phase out in declining increments of \$10,000 per year after retirement.

During fiscal year 2007-08, the District implemented the provisions of Government Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers of Postemployment Benefits Other than Pensions*. This Statement establishes standards for the measurement, recognition, and financial reporting for employers providing postemployment benefits other than pensions (OPEB). The provisions of this Statement are implemented prospectively and do not affect prior year's financial statements.

On June 24, 2008, the District's Board of Directors adopted a resolution approving the agreement and election of the District to prefund OPEB through CalPERS under its California Employer's Retiree Benefit Trust (CERBT) Program. On September 9, 2008, the District joined CERBT, an agent multiple-employer plan consisting of an aggregation of single-employer plans. The CERBT issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained from the California Employees' Retirement System, P. O. Box 942703, Sacramento, CA 94229-2703.

Funding Policy

The District's policy is to prefund these benefits as part of its multi-year financial planning strategy. On June 24, 2008, the Board of Directors approved the reallocation of \$17.7 million from its existing reserve for the initial prefunding of the unfunded liability for the first year of reporting. Subsequent years' funding, pursuant to the annual budget approved by the Board of Directors, would be phased in to gradually reach full funding by the sixth year in order to limit its immediate impact on groundwater charge increases and the funding of core services within limited available revenues.

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.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

The following table shows the components of the District's annual OPEB cost for fiscal year 2011-12, the amount actually contributed to the plan, and changes in the District's net OPEB obligation to the Plan:

Annual required contribution	\$ 10,979,100
Interest on net OPEB obligation	730,300
Adjustment to annual required contribution	<u>(614,400)</u>
Annual OPEB cost (expense)	11,095,000
Contributions made	<u>(9,694,498)</u>
Increase (decrease) in Net OPEB obligation	1,400,502
Net OPEB obligation, June 30, 2011	<u>9,927,690</u>
 Net OPEB obligation, June 30, 2012	 <u>\$ 11,328,192</u>

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

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation	
			WUE Enterprise Fund	Governmental/ Internal Service Funds
6/30/2010	13,306,561	58.51%	2,388,932	3,781,341
6/30/2011	13,930,369	73.03%	3,871,707	6,055,983
6/30/2012	11,095,000	87.38%	4,425,137	6,903,055

Funded Status and Funding Progress

As of June 30, 2011, the latest valuation date, the funded status of the OPEB plan was as follows:

Actuarial accrued liability (AAL)	\$ 156,061,200
Actuarial value of plan assets	\$ 32,273,200
Unfunded actuarial accrued liability (UAAL)	\$ 123,788,000
Funded ratio (actuarial value of plan assets/AAL)	21.0%
Covered payroll	\$ 81,761,500
UAAL as a percentage of covered payroll	151.0%

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

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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.

Actuarial Methods and Assumptions

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, 2011 actuarial valuation used the Entry Age Normal (EAN) cost method. The actuarial assumptions included a discount rate of 7.5% and a 3.25% inflation rate. Healthcare cost trend rates ranged from an initial rate range of 8% to 4.5 percent. The unfunded liability is being amortized as a percent of payroll over 30 years on a closed basis. The remaining years in amortization period at June 30, 2012 was 26 years.

(13) 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)	50	250,000
Fidelity (Crime) - Directors	5	1,000
Fidelity (Crime) – Non-Directors	10	2,000
Non-owned aircraft liability	-	5,000
Boiler and machinery	50	250,000

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

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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, 2012, the liability for self-insurance claims was \$6,130,000. 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, 2010 are as follows (in thousands):

	<u>General Liability</u>	<u>Workers' Compensation</u>	<u>Total</u>
Claims payable at June 30, 2010	\$ 3,027	\$ 4,579	\$ 7,606
Current year premiums, incurred claims and changes in estimates	(571)	169	(402)
Claim payments	<u>(25)</u>	<u>(360)</u>	<u>(385)</u>
Claims payable at June 30, 2011	<u>2,431</u>	<u>4,388</u>	<u>6,819</u>
Current year premiums, incurred claims and changes in estimates	(339)	221	(118)
Claim payments	<u>(233)</u>	<u>(338)</u>	<u>(571)</u>
Claims payable at June 30, 2012	<u><u>\$ 1,859</u></u>	<u><u>\$ 4,271</u></u>	<u><u>\$ 6,130</u></u>

The total claims payable in the amount of \$6.13 million is recorded in the District's Risk Management Internal Service Fund under current liabilities – claims payable (\$476 thousand) and non-current liabilities – claims payable (\$5,654 thousand). No portion of this amount is recorded in the Water Utility Enterprise Fund.

(14) DUE TO AND FROM OTHER FUNDS

The summary of current due to/from other funds, as of June 30, 2012, follows (in thousands):

<u>Due to other funds</u>	<u>Due from other funds</u>	<u>Amount</u>	<u>Due Within one year</u>
General Fund	Water Utility Enterprise Fund	<u>\$ 989</u>	<u>\$ 989</u>

(15) 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.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

In the year ended June 30, 2012, the Fund received \$3.3 million for the Open Space credit on property tax receipts.

Interfund transfer for the year ended June 30, 2012, is as follows (in thousands):

<u>Fund Receiving Transfers</u>	<u>Fund Making Transfers</u>	Amount Transferred
Water Utility Enterprise Fund	General Fund	\$ 1,751
Water Utility Enterprise Fund	Watershed & Stream Stewardship	1,530
Total		<u>\$ 3,281</u>

(16) COMMITMENTS

(a) Contract and Purchase Commitments

As of June 30, 2012, the Fund had open purchase commitments of approximately \$44.2 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) San Felipe Project Water Deliveries

The District has contracted with the U.S. Department of the Interior for water deliveries from the Central Valley Project through the San Felipe Division. The contract requires the District to operate and maintain Reach 1, Reach 2, and Reach 3 of the facilities.

During fiscal year 2006-07, 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 September 30, 2010 was \$25,762,669. The total commitment, including applicable interest, of the repayment contract was \$439,261,342. The remaining commitment as of June 30, 2012 was \$357,125,807.67.

(c) 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 State Water Project supplies. The District's share of the total program capital costs is \$46.9 million based on a 35 percent

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

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, 2012, the District has paid \$40.5 million towards the obligation of this agreement. During the first 10 years the District has a reservation for the full 35 percent allocation; by January 1, 2006, if the District's contributions towards the program capital costs did not equal \$46.9 million, the District's permanent storage allocation will be 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, 2012, the District has 324,665 acre-feet of water in storage. The participation rights are amortized using the straight-line method over the life of the agreement. Amortization of \$19,346,000 has been recorded through fiscal year 2012.

(17) CONTINGENCIES

(a) Litigation

As a public entity and due to its size and its activities, at virtually all times, the District is a defendant, co-defendant, or cross-defendant in various court cases in which money damages are sought. The largest case in which the District is involved in currently is Great Oaks Water Company v. Santa Clara Valley Water District.

On February 3, 2010, the Honorable Kevin Murphy issued Judgment After Trial and decided that the District owes Great Oaks Water Company a refund of groundwater charges in the amount of \$4,623,096 plus interest at 7% per annum. The award of pre-judgment interest as of December 1, 2009 amounts to \$1,285,524. Judge Murphy also awarded post-judgment interest at the rate of \$886.62 per day until the date of the entry of judgment. Judge Murphy also decided that the District owes Great Oaks Water Company damages in the amount of \$1,306,830. Recovery of this damages amount is in the alternative to the award of refund described above, and is not subject to application of any interest.

The District does not believe that the decision regarding its 2005-06 groundwater production charges is supported by the record. The District has timely appealed the trial court's decision and a decision by the Sixth District Court of Appeal is anticipated in 2013.

In accordance with the requirements of the *Financial Accounting Standards Board Accounting Standards Codification 450-20-25-2 – Contingencies – Loss Contingencies - Recognition*, the District has recorded a liability in the amount of \$5.93 million, which includes the Judgment After Trial decision amount plus interest in fiscal year 2008-09. The District recorded \$160 thousand in fiscal year 2009-10 and \$324 thousand in fiscal year 2010-11, and \$325 thousand in fiscal year 2011-12 as liability for the post-judgment interest from January 1, 2010 through June 30, 2012 at the rate of \$886.62 per day. The accrual was presented under the caption "Litigation Claim" in the Statement of Net Assets, and "Claims and Adjustments" in the Statement of Revenues, Expenses, and Changes in Net Assets.

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

Other than the case noted above, the outcome of other 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 material effect on June 30, 2012 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 used in the initial rate calculation, and changes in the Federal Reclamation Law during the 1980's have led to the development of new CVP water rate policies. These policies, coupled with the terms of the original contract, resulted in the District facing significant 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.

(d) Perchlorate

In 2003, perchlorate was discovered at the Olin Corporation facility and over a wide area in the Llagas subbasin in South County, impacting a number of water supply wells. The investigation and clean-up of the contamination are under the jurisdiction of the Central Coast Regional Water

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

Notes to Basic Financial Statements (Continued)
For the Year Ended June 30, 2012

Quality Control Board. As of November 2011, perchlorate is still present above the Maximum Contaminant Level in a few South County water supply wells and over a wide area of the subbasin. Olin's remedial efforts to date have been focused on clean-up of the site, including soil removal and groundwater treatment. Olin is in the process of beginning the clean-up of contaminated groundwater beyond the Olin site.

(18) SUBSEQUENT EVENTS

The District has evaluated subsequent events through May 31, 2013, the date on which the financial statements were available to be issued. The following subsequent events have occurred since June 30, 2012:

(a) Safe, Clean Water Measure

On July 24, 2012, the Board of Directors voted unanimously to place a measure on the November 6, 2012 ballot to renew an expiring parcel tax and help ensure the quality, safety and supply to the county's local water resources. On November 6, 2012, voters of Santa Clara County overwhelmingly supported Measure B. Measure B renews an existing special parcel tax assessed by the District on each parcel of land within the District. This tax will remain in effect for 15 years (July 1, 2013 through June 30, 2028).

(b) 2012A Certificate of Participation

On October 23, 2012, the Board of Directors authorized the execution and delivery of aggregate principal amount not to exceed \$60 million Refunding and Improvement Certificates of Participation, Series 2012A (2012A COPs). The Series 2012A COPs was sold on November 13, 2012 to J.P. Morgan Securities LLC on a competitive basis with an expected closing date on November 2012. The proceeds of the sale will be used to (i) refinance all or a portion of the outstanding 2003A COPs; (ii) finance the cost of certain flood protection improvement projects; (iii) fund a reserve fund; and (iv) pay the cost of issuing the 2012A COPs. This certificate of participation has been assigned "AAA" rating by Fitch and "AA+" rating by Standard and Poor's.

**Required
Supplementary
Information**

**WATER UTILITY ENTERPRISE FUND
OF THE
SANTA CLARA VALLEY WATER DISTRICT**
Schedule of Funding Progress - Other Post Retirement Benefit Plan
June 30, 2012

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL) Entry Age	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	Percentage of Covered Payroll
(a)	(b)	(b-a)	(a/b)	(c)	([b-a]/c)	
6/30/2007	\$ -	\$ 141,459,000	\$ 141,459,000	0.0%	\$78,300,000	180.7%
12/31/2008	\$ 19,580,319	\$ 150,156,794	\$ 130,576,475	13.0%	\$76,369,316	171.0%
6/30/2011	\$ 32,273,200	\$ 156,061,200	\$ 123,788,000	20.7%	\$81,761,500	151.4%

Other Information

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BROWN
ARMSTRONG

CERTIFIED
PUBLIC
ACCOUNTANTS

BROWN ARMSTRONG

Certified Public Accountants

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Honorable Members of the Board of Directors
Santa Clara Valley Water District
San Jose, California

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We have audited the financial statements of the Water Utility Enterprise Fund of the Santa Clara Valley Water District (the District), as of and for the year ended June 30, 2012, and have issued our report thereon dated May 31, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

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



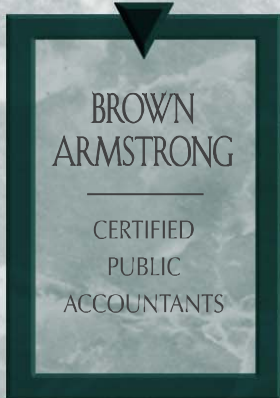
REGISTERED with the Public Company
Accounting Oversight Board and
MEMBER of the American Institute of
Certified Public Accountants

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

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

*Brown Armstrong
Accountancy Corporation*

Bakersfield, California
May 31, 2013



BROWN ARMSTRONG

Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT ON APPLYING AGREED UPON PROCEDURES

To the Honorable Members of the Board of Directors
Santa Clara Valley Water District
San Jose, California

We have performed the procedures enumerated below, which were agreed to by the Santa Clara Valley Water District (the District), to review allocation of revenues and expenses between the North and South Zone of the Water Utility Enterprise Fund service area for the year ended June 30, 2012, for the purpose of determining the rate charges between the two zones. We used the allocation methodologies used by the District's management which involves 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 Utility 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 determined allocations based on water usage, labor costs, and estimated benefits to the North and South Zones.

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.

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REGISTERED with the Public Company
Accounting Oversight Board and
MEMBER of the American Institute of
Certified Public Accountants

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

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

*Brown Armstrong
Accountancy Corporation*

Bakersfield, California
May 31, 2013

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

Schedule of Revenues and Expenses
(Budgetary Basis)
For the Year Ended June 30, 2012
(Dollars in Thousands)

	<u>North County</u>	<u>South County</u>	<u>Total</u>
Operating Revenues:			
Ground Water Charges	\$ 38,817	\$ 9,213	\$ 48,030
Treated Water Charges	92,904	-	92,904
Surface and recycled water charges	471	378	849
Operating Grants	1,032	79	1,111
	<u>123</u>	<u>-</u>	<u>123</u>
Total Operating revenues	133,347	9,670	143,017
Operating Expenses			
Sources of Supply	59,895	6,850	66,745
Water Treatment	27,735	19	27,754
Transmission and distribution:			
Raw Water	6,597	1,810	8,407
Treated Water	1,818	24	1,842
Administration and general	14,202	2,677	16,879
Capital Cost Recovery	<u>(2,859)</u>	<u>2,859</u>	<u>-</u>
Total Operating Expenses	<u>107,388</u>	<u>14,239</u>	<u>121,627</u>
Operating income (loss)	25,959	(4,569)	21,390
Nonoperating revenues (expenses):			
Property Taxes	20,341	1,986	22,327
Investment Income	1,446	-	1,446
Rental Income	63	30	93
Other	2,298	59	2,357
Interest and fiscal agent fees	(8,858)	-	(8,858)
Open Space Credit Transfer	(6,401)	6,401	-
Interest earned credit	58	(58)	-
Perchlorate response costs	<u>2,243</u>	<u>(2,243)</u>	<u>-</u>
Net Operating revenues	<u>11,190</u>	<u>6,175</u>	<u>17,365</u>
Income (loss)	<u>\$ 37,149</u>	<u>\$ 1,606</u>	<u>\$ 38,755</u>

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

Income (Loss)	\$ 38,755
Less: Depreciation and amortization expenses not allocated between Zones	(22,264)
Less: Transfers out	-
Less: Prior years' budget expenditures	(4,050)
Less: GAAP basis expenses and other liabilities	(894)
Less: Increase in Reserve for Market Valuation	(363)
Less: Incr in Oper Exp due to Reduction of Capitalized Cost	(12,390)
Add back: Capital cost recovery expense allocated to South County	-
Add back: Capital cost reimbursements	11,803
Add back: Encumbrances included in total Water Utility expenses	3,482
Add back: Reduction in program expenditures due to capitalized expenses	7,137
Add back: Transfers In	<u>3,281</u>
Total Income (Loss) per Statement of Revenues, Expenses and Changes in Net Assets	<u>\$ 24,497</u>

See accompanying notes to basic financial statements