

SAN GORGONIO PASS WATER AGENCY

FINANCIAL STATEMENTS

JUNE 30, 2007

SAN GORGONIO PASS WATER AGENCY

FINANCIAL STATEMENTS

JUNE 30, 2007

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 San Geronio Pass Water Agency
 Beaumont, California 92223

Independent Auditors' Report

We have audited the accompanying statement of net assets of the San Geronio Pass Water Agency as of June 30, 2007, and the related statements of revenues, expenses and changes in net assets, and cash flows for the year then ended. These financial statements are the responsibility of the Agency's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year's summarized comparative financial information has been derived from the Agency's 2006 financial statements which were audited by other auditors whose report dated September 8, 2006 expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the State Controller's Minimum Audit Requirements for California Special Districts. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the San Geronio Pass Water Agency as of June 30, 2007, and the respective changes in financial position and cash flows of the Agency for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The information identified in the accompanying table of contents as *management's discussion and analysis* is not a required part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Rogers, Anderson Malody & Scott, LLP

September 17, 2007

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SAN GORGONIO PASS WATER AGENCY MANAGEMENT'S DISCUSSION AND ANALYSIS

The Agency

The San Gorgonio Pass Water Agency is one of 29 state water contractors and was created by the Legislature of the State of California under Senate Bill Number 8, Chapter 40, which was signed into law by the Governor of California on April 19, 1962. The purpose of creating this public agency by special law was for the "planning, conservation, development, distribution, control and use of an adequate water supply for the public good and for the protection of life and property therein." As part of the act, the Agency was given taxing authority similar to the taxing power of other local governments.

The Agency has completed the East Branch Extension, Phase 1, of the State Water Project. The Agency is the last of the State Water Project contractors to receive water. The Agency has entered into a contract with the State Department of Water Resources to receive an annual allotment of 17,300 acre-feet from the State Water Project. The "Extension" delivers water to the Agency's service area, which extends from Calimesa to Cabazon through the San Gorgonio Pass area.

The Basic Financial Statements

San Gorgonio Pass Water Agency is a special purpose government (special District) engaged only in activities that support themselves through user and capacity fees and tax levies. Accordingly, the accompanying financial statements are presented in the format prescribed for proprietary funds by the Governmental Accounting Standards Board.

These financial statements consist of three interrelated statements designed to provide the reader with relevant, understandable data about the Agency's financial condition and operating results. They are the Statement of Net Assets, the Statement of Revenues, Expenses and Changes in Net Assets, and the Statement of Cash Flows.

The Statement of Net Assets presents the Agency's assets and liabilities and the difference, or net, between what is owned and what is owed as of the last day of the Agency's fiscal year. The Statement of Revenues, Expenses and Changes in Net Assets describes the financial results of the Agency's operations for the years reported. These results, or changes in net assets, are the increases or decreases in the bottom line of the Statement of Net Assets.

The Statement of Cash Flows conveys to financial statement users how the Agency managed cash resources during the year. This statement converts the Change in Net Assets presented on the Statement of Revenues, Expenses and Changes in Net Assets into actual cash provided by or used for operations. The Statement of Cash Flows also details how the Agency obtains cash through financing and investing activities and, conversely, how cash is spent for these purposes.

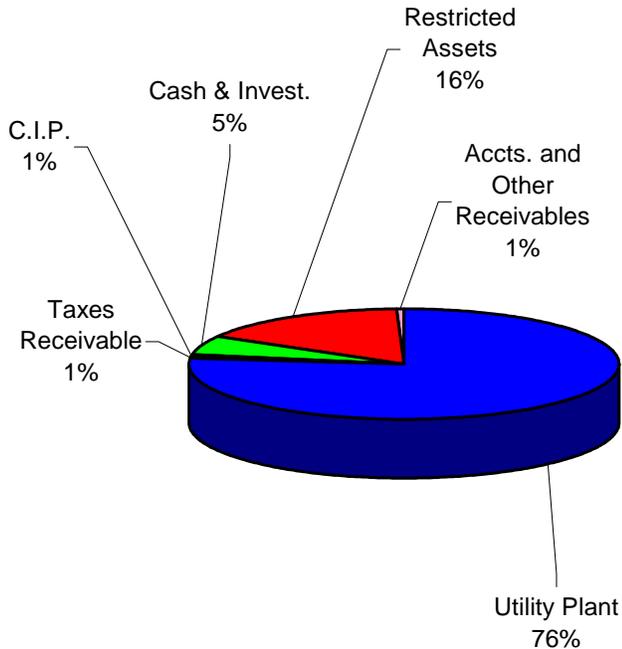
Summary Financial Information and Analysis

During the year ended June 30, 2007, the Agency's Total Assets increased by \$9.67 million and net assets increased by \$9.59 million. A majority of the increase in Total Assets resulted from payments to the Department of Water Resources (\$5.15 million) for Investment in State Water Rights in the State Water Project Transportation System.

**SAN GORGONIO PASS WATER AGENCY
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Assets Owned

June 30, 2007

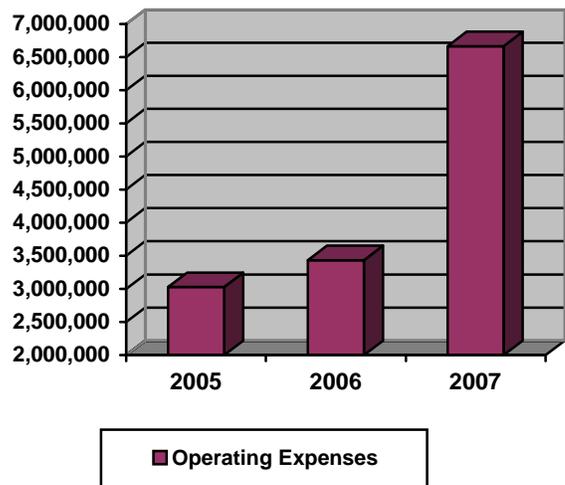


Total Cash in bank, Cash in Local Agency Investment Fund and Investments increased by \$6.76 million. The increase can be further divided into general unrestricted and restricted cash. Unrestricted cash increased \$2.40 million and restricted cash increased \$4.36 million. The \$2.86 million increase in Current Assets was due primarily to an increase in cash and investments from water sales, property taxes and interest. The increase in Restricted Assets is a result of an increase in the amount of property taxes collected for debt service pertaining to the state water project.

The \$9.59 million increase in Net Assets included non-operating revenue net of expenses of \$14.86 million, and contributions of \$.06 million. These amounts were reduced by a loss from operations of \$5.33 million.

Financial Statement Summary (In millions)

	6/30/07	6/30/06
Current Assets	\$ 6.89	\$ 4.02
Restricted Assets	16.56	11.60
Capital Assets	79.03	77.19
Total Assets	102.48	92.81
Total Liabilities	.26	.18
Net Assets	102.22	92.63
Oper. Revenues	1.33	.01
Oper. Expenses	(6.66)	(3.43)
Non Oper. Rev.:		
Interest	.75	.43
Property Taxes	14.03	9.46
Miscellaneous	.11	-
Non Oper. Exp.	(.04)	(.02)
Contributions	.06	.04
Change in Net Assets	\$ 9.58	\$ 6.49

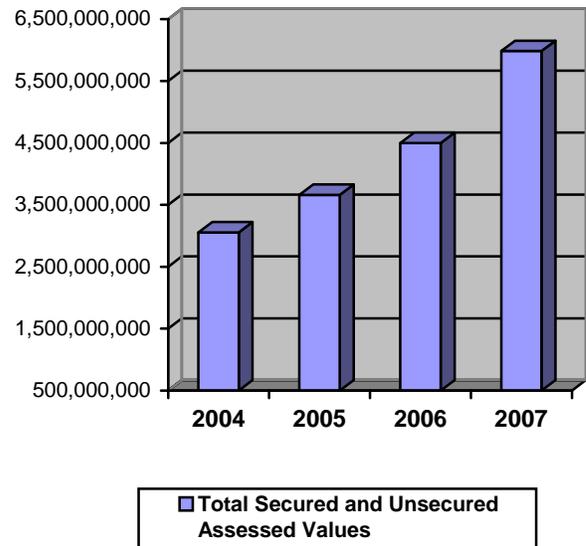


SAN GORGONIO PASS WATER AGENCY MANAGEMENT'S DISCUSSION AND ANALYSIS

Operating expenses increased \$3.23 million or 94% from the prior year. The increase in operating expenses is primarily attributable to costs associated with the increased purchase and delivery of water, amortization of the Investment in State Water Rights and legal and engineering fees. Purchased water increased \$624 thousand; transmission and distribution related costs increased \$99 thousand; amortization of State Water Rights increased \$2.46 million; legal and engineering costs increased \$199 thousand over the prior year.

Non-operating revenues increased over the prior year. Total property taxes received increased \$4.58 million. This increase was derived from a \$978 thousand increase from general-purpose property tax distribution and \$3.60 million increase from Debt Service property taxes. The service area within the Agency has experienced major growth which has attributed to the increase in property taxes received. In addition to growth, a portion of the general-purpose tax increase over the prior year was attributable to the restoration of \$502 thousand of property tax revenue previously shifted to the state's Education Revenue Augmentation Fund. Interest earned on reserves increased by \$324 thousand that was mainly attributable to an increase in reserves available and interest rates.

The following reflects the Agency's assessed property tax valuations. Assessed valuations have increased each of the four years ending on June 30, 2007. The percent increase in the current year was 33%.



Categories of Net Assets

The Agency is required to present its net assets in three categories: Invested in Capital Assets, Restricted and Unrestricted.

Invested in Capital Assets

At June 30, 2007, Invested in Capital Assets totaled \$79.03 million and consisted of Utility Plant in Service and Construction in Progress, net of Accumulated Depreciation and Amortization.

Restricted

The Agency had restricted Net Assets of \$16.56 million, which consisted of tax proceeds that were levied for State Water Project payments less actual State Water Project related expenditures.

Unrestricted

The Agency had unrestricted Net Assets of \$6.62 million at June 30, 2007.

**SAN GORGONIO PASS WATER AGENCY
MANAGEMENT'S DISCUSSION AND ANALYSIS**

Capital Asset activity for the year was as follows:

	Balance July 1, 2006	Additions	Deletions	Balance June 30, 2007
Capital Assets not being depreciated:				
Land	\$ 468,444	\$ -	\$ -	\$ 468,444
Construction in progress	492,590	28,959	-	521,549
Total Capital Assets, not being depreciated	961,034	28,959	-	989,993
Capital Assets being depreciated:				
Investment in State Water Rights	61,443,593	5,149,835	-	66,593,428
Source of supply	13,996,571	191,500	-	14,188,071
Transmission and distribution	1,351,614	-	-	1,351,614
Buildings	1,409,400	-	-	1,409,400
Furniture and fixtures	169,024	1,077	-	170,101
Technical equipment	39,333	10,742	-	50,075
Transportation equipment	21,954	-	-	21,954
Total Capital Assets, being depreciated	78,431,489	5,353,154	-	83,784,643
 Total Capital Assets	 \$ 79,392,523	 \$ 5,382,113	 \$ -	 \$ 84,774,636

Capital Assets

The Agency made payments to the Department of Water Resources during the year totaling \$6.08 million net of credits and refunds for participation rights in the State Water Project. The unit rate has been determined by dividing the total estimated capital costs to be charged to the Agency by total estimated water deliveries over the project repayment period. The resulting rate, which will be adjusted periodically to reflect changes in estimates, would then be applied to actual water deliveries in the current year.

Since water deliveries have commenced minimum operations, maintenance and power costs and variable operations, maintenance, power and replacement costs paid this year were expensed on the Statement of Revenues, Expenses and Changes in Net Assets. State Water Project deliveries through the East Branch Extension to the Little San Gorgonio Creek Recharge Facility were started in July 2003 and during the 2006-07 year 7,177 acre feet of water was delivered.

The Agency's future commitment for State Water Project costs over the years 2007 to 2035, according to a payment schedule dated June 30, 2007, is estimated to total \$279 million.

Construction in Progress (CIP)

Construction in Progress increased \$29 thousand to \$521 thousand between July 1, 2006 and June 30, 2007.

The remaining projects in Construction in Progress include the FERC project and an instream recharge project at Noble Creek.

Contacting the Agency's Financial Management

This financial report is designed to provide our customers, investors, and creditors with an overview of the Agency's financial operations and condition. If you have questions about this report or need additional information, you may contact the Agency's Finance Manager at 1210 Beaumont Ave., Beaumont, California 92223.

SAN GORGONIO PASS WATER AGENCY

STATEMENT OF NET ASSETS

JUNE 30, 2007 (with comparative data for 2006)

ASSETS	<u>2007</u>	<u>2006</u>
CURRENT ASSETS:		
Cash in bank and on hand	\$ 84,428	\$ 30,962
Cash in Local Agency Investment Fund	4,761,202	2,417,267
Investments	994,268	994,216
Accounts receivable	294,571	3,603
Taxes receivable	532,834	423,287
Interest receivable	214,359	122,535
Prepaid expenses	5,350	4,820
Other receivable	202	24,677
Total Current Assets	<u>6,887,214</u>	<u>4,021,367</u>
RESTRICTED ASSETS:		
Cash in Local Agency Investment Fund	14,814,386	10,451,061
Taxes receivable	1,745,129	1,147,677
	<u>16,559,515</u>	<u>11,598,738</u>
NONCURRENT ASSETS:		
Capital Assets:		
Investment in State Water Rights	66,593,428	61,443,593
Utility plant in service	17,191,215	16,987,896
Less: accumulated depreciation	1,806,653	1,239,603
accumulated amortization	3,934,320	962,359
	<u>78,043,670</u>	<u>76,229,527</u>
Land and rights of way	468,444	468,444
Construction in progress	521,549	492,590
Total Noncurrent Assets	<u>79,033,663</u>	<u>77,190,561</u>
TOTAL ASSETS	<u>102,480,392</u>	<u>92,810,666</u>

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

SAN GORGONIO PASS WATER AGENCY

STATEMENT OF NET ASSETS

JUNE 30, 2007 (with comparative data for 2006)

	<u>2007</u>	<u>2006</u>
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable	\$ 228,089	\$ 118,318
Accrued vacation and sick leave	35,290	29,315
Construction deposits	-	28,738
Total Current Liabilities	<u>263,379</u>	<u>176,371</u>
 NET ASSETS		
Invested in capital assets	79,033,663	77,190,561
Restricted for State Water Project	16,559,515	11,598,738
Unrestricted	<u>6,623,835</u>	<u>3,844,996</u>
 TOTAL NET ASSETS	 <u><u>\$ 102,217,013</u></u>	 <u><u>\$ 92,634,295</u></u>

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

SAN GORGONIO PASS WATER AGENCY

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

YEAR ENDED JUNE 30, 2007 (with comparative data for 2006)

	<u>2007</u>	<u>2006</u>
OPERATING REVENUES:		
Water sales - purveyors	\$ 1,329,304	\$ 11,048
OPERATING EXPENSES:		
Source of Supply		
Maintenance	997,890	1,313,878
Purchased water	896,100	272,372
	<u>1,893,990</u>	<u>1,586,250</u>
Transmission and Distribution		
Utilities	4,734	5,482
Maintenance	101,236	1,488
	<u>105,970</u>	<u>6,970</u>
General and Administrative Expenses		
Salaries	280,384	255,028
Director fees	75,695	69,002
Payroll taxes	19,080	18,799
Employee health benefits	65,485	51,387
Employee retirement benefits	103,748	96,022
Office supplies and expense	17,030	14,393
Travel expense	14,340	12,780
Automotive expense	4,658	5,107
Utilities and telephone	23,649	22,100
Rent	-	268
Repairs and maintenance	11,735	12,494
EBX operations and maintenance	-	45,225
Computer and telephone support and service	6,865	8,475
Insurance	19,579	16,623
Administration expense	1,309	1,060
Membership dues and assessments	24,497	22,965
Public relations	36,179	9,725
Legal services	136,635	86,171
Engineering services	188,166	39,445
Consulting services	4,655	5,261
Accounting and auditing	16,592	14,270
Outside professional services	8,090	20,625
Election expense	67,406	-
Depreciation	567,050	497,823
Amortization	2,971,961	514,903
	<u>4,664,788</u>	<u>1,839,951</u>
Total Operating Expenses	<u>6,664,748</u>	<u>3,433,171</u>
LOSS FROM OPERATIONS	<u>(5,335,444)</u>	<u>(3,422,123)</u>

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

SAN GORGONIO PASS WATER AGENCY

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

YEAR ENDED JUNE 30, 2007 (with comparative data for 2006)

	<u>2007</u>	<u>2006</u>
NON-OPERATING REVENUES (EXPENSES):		
Interest	\$ 756,185	\$ 432,203
Property taxes:		
General-purpose distribution	2,181,262	1,202,979
Debt service	11,854,138	8,255,318
Miscellaneous income	109,594	4,929
County collection charges	(38,617)	(25,175)
	<u>14,862,562</u>	<u>9,870,254</u>
Income Before Contributions	<u>9,527,118</u>	<u>6,448,131</u>
CONTRIBUTIONS:		
Local government - FERC Project	55,600	44,000
	<u>55,600</u>	<u>44,000</u>
Change in Net Assets	9,582,718	6,492,131
NET ASSETS, Beginning of year	<u>92,634,295</u>	<u>86,142,164</u>
NET ASSETS, End of year	<u>\$ 102,217,013</u>	<u>\$ 92,634,295</u>

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

SAN GORGONIO PASS WATER AGENCY

STATEMENT OF CASH FLOWS

YEAR ENDED JUNE 30, 2007 (with comparative data for 2006)

	<u>2007</u>	<u>2006</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from customers	\$ 1,040,211	\$ 39,529
Cash payments to suppliers for goods and services	(2,766,725)	(2,249,468)
Cash payments to employees for services	(274,409)	(245,738)
Other income received	109,392	4,929
Net Cash Used For Operating Activities	<u>(1,891,531)</u>	<u>(2,450,748)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
Property taxes received	<u>2,087,359</u>	<u>1,133,564</u>
Net Cash Provided By Noncapital Financing Activities	<u>2,087,359</u>	<u>1,133,564</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Property taxes received	11,227,102	8,062,481
Contributions received	55,600	94,660
Capital payments	<u>(5,382,113)</u>	<u>(5,051,276)</u>
Net Cash Provided By Capital and Related Financing Activities	<u>5,900,589</u>	<u>3,105,865</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Interest received	<u>664,309</u>	<u>377,668</u>
Net Cash Provided By Investing Activities	<u>664,309</u>	<u>377,668</u>
NET INCREASE IN CASH	6,760,726	2,166,349
CASH AT BEGINNING OF YEAR	<u>12,899,290</u>	<u>10,732,941</u>
CASH AT END OF YEAR	<u>\$ 19,660,016</u>	<u>\$ 12,899,290</u>
CASH AT END OF YEAR		
Current Assets:		
Cash in bank and on hand	\$ 84,428	\$ 30,962
Cash in Local Agency Investment Fund	4,761,202	2,417,267
Restricted Cash in Local Agency Investment Fund	<u>14,814,386</u>	<u>10,451,061</u>
	<u>\$ 19,660,016</u>	<u>\$ 12,899,290</u>

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

SAN GORGONIO PASS WATER AGENCY

STATEMENT OF CASH FLOWS

YEAR ENDED JUNE 30, 2007 (with comparative data for 2006)

	<u>2007</u>	<u>2006</u>
RECONCILIATION OF OPERATING LOSS TO NET CASH USED FOR OPERATING ACTIVITIES:		
Operating loss	\$ (5,335,444)	\$ (3,422,123)
Adjustments:		
Depreciation and amortization	3,539,011	1,012,726
Miscellaneous income	109,392	4,929
Change in Assets and Liabilities:		
(Increase) decrease in accounts receivable	(290,968)	(257)
(Increase) decrease in prepaid expenses	(530)	1,070
Increase (decrease) in accounts payable	109,771	(85,121)
Increase (decrease) in accrued vacation and sick leave	5,975	9,290
Increase (decrease) in construction deposits	<u>(28,738)</u>	<u>28,738</u>
Net Cash Used For Operating Activities	<u>\$ (1,891,531)</u>	<u>\$ (2,450,748)</u>
Non Cash Capital, Financing and Investing Activities:		
None to Report		

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

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 1: NATURE OF ACTIVITIES AND SIGNIFICANT ACCOUNTING POLICIES

The San Gorgonio Pass Water Agency is one of 29 state water contractors created by the state legislature. The Agency will ultimately manage water resources and supply water to local water districts. The Agency's service area extends from Calimesa to Cabazon through the Pass area.

Basis of Accounting and Measurement Focus

The Agency accounts for its operation in an enterprise fund using the economic resources measurement focus and the accrual basis of accounting in conformity with the Uniform System of Accounts for Water Utility Districts as prescribed by the Controller of the State of California. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

An enterprise fund distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Agency's principal ongoing operations. The principal operating revenues of the Agency will be charges for wholesale water sales to purveyors within the Agency. Operating expenses of the Agency include cost of sales, administrative expenses, depreciation and amortization on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The Agency has elected to follow Financial Accounting Standards Board pronouncements issued before November 30, 1989, and all pronouncements of the Governmental Accounting Standards Board.

On July 1, 2000, the Agency adopted the provisions of Governmental Accounting Standards Board Statement No. 34 "*Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments.*" Statement 34 established standards for external financial reporting for all state and local governmental entities, which includes a statement of net assets, a statement of revenues, expenses and changes in net assets, and a statement of cash flows. It requires the classification of net assets into three components – invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

- *Invested in capital assets, net of related debt* – This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation, reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 1: NATURE OF ACTIVITIES AND SIGNIFICANT ACCOUNTING POLICIES (continued)

- *Restricted* – This component of net assets consists of constraints placed on net assets use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.
- *Unrestricted net assets* – This component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

On July 1, 2000, the Agency also adopted the provisions of Governmental Accounting Standards Board Statement No. 33 “*Accounting and Financial Reporting for Nonexchange Transactions.*” This statement requires that capital contributions to the Agency be presented as a change in net assets.

Cash and Investments

Changes in fair value that occur during a fiscal year are recognized as *interest* reported for that fiscal year. *Interest* also includes interest earnings and any gains or losses realized upon the liquidation, maturity, or sale of investments. Investments are reported in the accompanying balance sheet at fair value except for certain investment contracts that are reported at cost because they are not transferable and they have terms that are not affected by changes in market interest rates.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Comparative Data

Prior year data has been included where practical for comparison purposes only. The prior year data does not represent a complete presentation in accordance with generally accepted accounting principles.

Capital Assets

Capital assets are stated at original cost. The capital cost component of the transportation charges and the Delta water charge the Agency pays for participation rights in the State Water Project are being capitalized as paid in accordance with instructions from the Controller of the State of California. Amortization of these water rights has been calculated based on the actual water delivery in the current fiscal year over the estimated total water delivery over the life of the State Water Project contract.

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 1: NATURE OF ACTIVITIES AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Capital assets include property, plant, equipment and infrastructure assets, and are defined by the Agency as assets with an initial cost of more than \$750 and an estimated useful life in excess of two years. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend the asset's life are not capitalized.

Property, plant and equipment of the Agency is depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Pipelines	20 - 40
Spreading Ground Facilities	20
Buildings	25
Furniture and Fixtures	5 - 10
Technical Equipment	5
Transportation	5

Investment in Water Rights is being amortized on a unit-rate basis. The unit rate has been determined by dividing the total estimated capital costs to be charged to the Agency by total estimated water deliveries over the project repayment period. The resulting rate, which will be adjusted periodically to reflect changes in estimates, would then be applied to actual water deliveries in the current year.

Property Taxes

Property tax in California is levied in accordance with Article XIII A of the State Constitution at 1% of countywide assessed valuations. The property taxes are placed in a pool and are then allocated to the local governmental units based upon complex formulas. Property tax revenue is recognized in the fiscal year in which taxes have been levied.

The property tax calendar is as follows:

Lien date:	January 1
Levy date:	July 1
Due date:	First installment – November 1 Second installment – February 1
Delinquent date:	First installment – December 11 Second installment – April 11

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 1: NATURE OF ACTIVITIES AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Accrued Vacation and Sick Leave

The Agency has a policy whereby an employee can accumulate unused sick leave and vacation. Sick leave is to be used for extended periods of sickness; however, upon termination or retirement, a portion will be paid as additional benefits to the employee. At retirement or termination, employees will be paid for 50% of the then unused sick leave up to the maximum of 480 hours at their regular payroll rates in effect at the date of termination. The Agency has provided for these future costs by accruing 50% of the earned and unused sick leave up to the maximum number of hours and 100% of the earned and unused vacation.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, deposits with financial institutions and deposits in the State of California Local Agency Investment Fund. Investments are carried at fair value and deposits in the Local Agency Investment Fund can be withdrawn at any time.

NOTE 2: CASH AND INVESTMENTS

Cash and investments as of June 30, 2007 are classified in the accompanying financial statements as follows:

Statement of Net Assets:

Current Assets:

Cash in bank and on hand	\$ 84,428
Cash in Local Agency Investment Fund	4,761,202
Investments	994,268

Restricted Funds:

Cash in Local Agency Investment Fund	<u>14,814,386</u>
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Total cash and investments	<u><u>\$ 20,654,284</u></u>
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Cash and investments as of June 30, 2007 consist of the following:

Cash on hand	\$ 100
Deposits with financial institutions	84,328
Investments	<u>20,569,856</u>

Total cash and investments	<u><u>\$ 20,654,284</u></u>
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SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 2: CASH AND INVESTMENTS (continued)

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

The following table identifies the investment types that are authorized for the Agency by the California Government Code and the Agency's investment policy. The table also identifies certain provisions of the California Government Code (or the Agency's investment policy, if more restrictive) that address interest rate risk and concentration of credit risk. This table does not address investments of debt proceeds held by bond trustee that are governed by the provisions of debt agreements of the Agency, rather than the general provisions of the California Government Code or the Agency's investment policy.

Investment Types Authorized by State Law	Authorized by Investment Policy	*Maximum Maturity	Maximum Percentage of Portfolio	Maximum Investment in One Issuer
Local Agency Bonds	No	5 years	None	None
U.S. Treasury Obligations	Yes	1 year	None	None
U.S. Agency Securities	No	5 years	None	None
Banker's Acceptances	No	180 days	None	None
Commercial Paper	No	270 days	None	None
Negotiable Certificates of Deposit	No	5 years	None	None
Repurchase Agreements	Yes	1 year	None	None
Reverse Repurchase Agreements	No	92 days	None	None
Medium-Term Notes	No	5 years	None	None
Mutual Funds	No	N/A	None	None
Money Market Mutual Funds	No	N/A	None	None
Mortgage Pass-Through Securities	No	5 years	None	None
County Pooled Investment Funds	No	N/A	None	None
Local Agency Investment Fund (LAIF)	Yes	N/A	None	None
JPA Pools (other investment pools)	No	N/A	None	None

* Based on state law requirements or investment policy requirements, whichever is more restrictive.

Disclosures Relating to Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the Agency manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 2: CASH AND INVESTMENTS (continued)

Information about the sensitivity of the fair values of the Agency's investments to market interest rate fluctuations is provided by the following table that shows the distribution of the Agency's investments by maturity:

Investment Type	Amount	Remaining Maturity (in Months)			
		12 Months or Less	13 to 24 Months	25 to 60 Months	More Than 60 Months
U.S. Treasury notes	\$ 994,268	\$ 994,268	\$ -	\$ -	\$ -
Local Agency Investment Fund	19,575,588	19,575,588	-	-	-
Total	<u>\$ 20,569,856</u>	<u>\$ 20,569,856</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

Investments with Fair Values Highly Sensitive to Interest Rate Fluctuations

The Agency does not hold investments that are highly sensitive to interest rate fluctuation beyond that already indicated in the information provided above.

Disclosures Relating to Credit Risk

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

Investment Type	Amount	Minimum Legal Rating	Exempt from Disclosure	Rating as of Year End		
				AAA	AA	Not Rated
U.S. Treasury notes	\$ 994,268	N/A	\$ 994,268	\$ -	\$ -	\$ -
Local Agency Investment Fund	19,575,588	N/A	-	-	-	19,575,588
Total	<u>\$20,569,856</u>		<u>\$ 994,268</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 19,575,588</u>

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 2: CASH AND INVESTMENTS (continued)

Concentration of Credit Risk

The investment policy of the Agency contains no limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code. The Agency did not hold any investments in any one issuer (other than U.S. Treasury securities and external investment pools) that represent 5% or more of total Agency investments.

Custodial Credit Risk

Custodial credit risk for *deposits* is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for *investments* is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code and the Agency's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. As of June 30, 2007, \$10,609 of the Agency's deposits with financial institutions in excess of federal depository insurance limits were held in uncollateralized accounts.

Investment in State Investment Pool

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

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 3: CAPITAL ASSETS

A summary of changes in capital assets follows:

	<u>Balance</u> <u>July 1, 2006</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance</u> <u>June 30, 2007</u>
Business-type activities:				
Capital assets, not being depreciated:				
Land and rights of way	\$ 468,444	\$ -	\$ -	\$ 468,444
Construction in progress	492,590	28,959	-	521,549
Total capital assets, not being depreciated	<u>961,034</u>	<u>28,959</u>	<u>-</u>	<u>989,993</u>
Capital assets, being depreciated/ amortized:				
Investment in State Water Rights	61,443,593	5,149,835	-	66,593,428
Source of supply	13,996,571	191,500	-	14,188,071
Transmission and distribution	1,351,614	-	-	1,351,614
Buildings	1,409,400	-	-	1,409,400
Furniture and fixtures	169,024	1,077	-	170,101
Technical equipment	39,333	10,742	-	50,075
Transportation equipment	21,954	-	-	21,954
Total capital assets, being depreciated / amortized	<u>78,431,489</u>	<u>5,353,154</u>	<u>-</u>	<u>83,784,643</u>
Less accumulated depreciation/amortization for:				
Investment in State Water Rights	962,359	2,971,961	-	3,934,320
Source of supply	773,332	422,397	-	1,195,729
Transmission and distribution	168,952	67,580	-	236,532
Buildings	140,940	56,376	-	197,316
Furniture and fixtures	106,807	13,602	-	120,409
Technical equipment	36,399	2,704	-	39,103
Transportation equipment	13,173	4,391	-	17,564
Total accumulated depreciation	<u>2,201,962</u>	<u>3,539,011</u>	<u>-</u>	<u>5,740,973</u>
Total capital assets, being depreciated / amortized, net	<u>76,229,527</u>	<u>1,814,143</u>	<u>-</u>	<u>78,043,670</u>
Total capital assets, net	<u>\$ 77,190,561</u>	<u>\$ 1,843,102</u>	<u>\$ -</u>	<u>\$ 79,033,663</u>

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 4: COMMITMENTS

STATE WATER PROJECT

The Agency has entered into a contract with the State Department of Water Resources to receive an annual entitlement for water from the State Water Project. The Agency assumed a proportionate share of capital costs and minimum operations, maintenance, power and replacement costs of the state facilities, in addition to paying variable operations, maintenance, power and replacement costs on a per-acre-foot charge for water deliveries when they are received. The Agency received delivery of 7,177 acre feet of State Project Water during the fiscal year ended June 30, 2007.

The Agency's future commitment for State Water Project costs over the years 2007 to 2035, according to a payment schedule dated June 30, 2007, is estimated as follows:

Transportation charge:		
Capital cost component:		
State Water Project	\$	15,422,226
East branch extension		123,153,351
Minimum operations, maintenance, power and replacement component		37,923,598
Variable operations, maintenance, power and replacement component		86,051,976
		<hr/> 262,551,151
Delta water charges		13,439,183
Water system revenue bond surcharge		<hr/> 2,712,564
		<hr/> <hr/>
Total	\$	<u><u>278,702,898</u></u>

NOTE 5: EMPLOYEES' RETIREMENT PLAN

Plan Description: San Gorgonio Pass Water Agency contributes to the California Public Employees' Retirement System (PERS), an agent multiple-employer public employee defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. PERS acts as a common investment and administrative agent for participating public entities within the State of California. Benefit provisions and all other requirements are established by state statute and Agency policy. Copies of PERS' annual financial report may be obtained from their executive office: 400 P Street, Sacramento, CA 95814.

All full-time Agency employees are eligible to participate in PERS with benefits vesting after five years of service. Agency employees who retire at age 60 with five years of credited service are entitled to an annual retirement benefit, payable monthly for life, in increasing percentage increments up to 3% of their average full-time monthly par rate for the highest 12 consecutive months for each year of credited service.

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 5: EMPLOYEES' RETIREMENT PLAN (continued)

Funding Policy: Agency employees are required to contribute 8% of their annual salary to PERS. The Agency makes the contributions required of Agency employees on their behalf and for their account. The Agency is required to contribute an amount necessary to fund the benefits of its members, using the actuarial basis recommended by the PERS actuaries and actuarial consultants and adopted by the Board of Administration. For the year ended June 30, 2007, the amount contributed by the Agency on behalf of the employees was \$103,748. The required employer contributions rate for fiscal year ended June 30, 2007 was 30.504%.

Annual Pension Cost: Under GASB 27, an employer reports an annual pension cost (APC) equal to the annual required contribution (ARC) plus an adjustment for cumulative difference between the APC and the employer's actual plan contributions for the year. The cumulative difference is called the net pension obligation (NPO). The ARC for the period July 1, 2006 to June 30, 2007 has been determined by an actuarial valuation of the plan as of June 30, 2004. The contribution rate for the indicated period is 30.504% of covered payroll. In order to calculate the dollar value of the ARC for inclusion in financial statements prepared as of June 30, 2007, this contribution rate, as modified by any amendments for the year, would be multiplied by the payroll of covered employees that was actually paid during the period July 1, 2006 to June 30, 2007.

A summary of principal assumptions and methods used to determine the ARC is shown below.

Valuation Date	June 30, 2004
Actuarial Cost Method	Entry Age Actuarial Cost Method
Amortization Method	Level Percent of Payroll
Average Remaining Period	17 Years as of the Valuation Date
Asset Valuation Method	15 Year Smoothed Market
Actuarial Assumptions	
Investment Rate of Return	7.75% (net of administrative expenses)
Projected Salary Increases	3.25% to 14.45% depending on Age, Service, and type of employment
Inflation	3.0%
Payroll Growth	3.25%
Individual Salary Growth	A merit scale varying by duration of employment coupled with an assumed annual inflation component of 3.0% and an annual production growth of 0.25%

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. Gains and losses that occur in the operation of the plan area amortized over a rolling period, which results in an amortization of 10% of unamortized gains and losses each year. If the plan's accrued liability exceeds the actuarial value of plan assets, then the amortization payment on the total unfunded liability may not be lower than the payment calculated over a 30 year amortization period.

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 5: EMPLOYEES' RETIREMENT PLAN (continued)

Assembly Bill 1974, which added Sections 20840-20842 to the California Government Code allowed PERS to create risk pools and mandate public agency participation in those pools. Commencing with the valuation of June 30, 2003, mandatory pooling was established for plans with less than 100 active members. Henceforth, the San Gorgonio Pass Water Agency was required to participate in a risk pool of plans with less than 100 employees.

At the time of joining the risk pool (valuation of June 30, 2003), a side fund was created to account for the differences between the funded status of the pool and funded status of the Agency's plan. The side fund will be credited, on an annual basis, with the actuarial investment return assumption. The side fund will also be subject to amortization on an annual basis.

A positive side fund meant that the employer will have to contribute less than the pool's required contribution rate while a negative side fund indicates the employer will have to contribute more than the pool's required contribution rate.

The total contribution paid to the PERS for 2007 and 2006 were \$103,748 and \$96,022, respectively. In 2007, the Agency paid \$103,748 and the employees paid \$0. In 2006, the Agency paid \$96,022 and the employees paid \$0. The contributions were made in accordance with actuarially determined requirements computed through an actuarial valuation performed prior to the beginning of each fiscal year by the PERS Actuarial Divisions. The combined employer and employee contribution consisted of 38.504% of current covered payroll and no amount to amortized unfunded actuarial accrued liability. In order to maintain a level of contributions, the Agency has chosen to amortize the overfunded actuarial liability for a period of 20 years.

Three Year Trend Information:

<u>Fiscal Year</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
June 30, 2005	\$ 105,978	100%	\$ 0
June 30, 2006	96,022	100	0
June 30, 2007	103,748	100	0

The Schedule of Funding Progress below shows the recent history of the actuarial value of assets, actuarial accrued liability, their relationship, and the relationship of the unfunded accrued liability to payroll.

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 5: EMPLOYEES' RETIREMENT PLAN (continued)

Risk Pool

Required Supplementary Information

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets</u>	<u>Actuarial Accrued Liability Entry Age</u>	<u>Unfunded AAL</u>	<u>Funded Ratio</u>	<u>Covered Payroll</u>	<u>UAAL as a % of Covered Payroll</u>
June 30, 2003	\$ 270,886,705	\$335,029,580	\$ 64,142,875	80.9%	\$ 75,357,937	85.1%
June 30, 2004	334,956,019	426,958,282	92,002,263	78.5%	90,667,029	101.5%
June 30, 2005	405,480,805	499,323,280	93,842,475	81.2%	108,618,321	86.4%

NOTE 6: JOINT VENTURE

The Agency participates in a joint venture under a joint powers agreement (JPA) with the Association of California Water Agencies Joint Powers Insurance Authority (Authority). The Authority is a risk-pooling self-insurance authority created under the provisions of California Government Code Section 6500 et. sec.

The Authority is governed by a board consisting of a representative from each member agency. The board controls the operations of the Authority including selection of management and approval of operating budgets. The relationship between the Agency and the Authority is such that the Authority is not a component unit of the Agency for financial reporting purposes.

The purpose of the Authority is to arrange and administer programs of insurance for the pooling of self-insured losses and to purchase excess insurance coverage. At June 30, 2007, the Agency participation in the self-insurance programs of the Authority was as follows:

Property Loss: Insured up to replacement value with \$1,000 deductible for building and personal property and \$0 for mobile licensed equipment per occurrence; the Authority is self-insured up to \$10,000 per occurrence and has purchased excess insurance coverage.

General Liability: Insured up to \$40,000,000 per occurrence with \$2,500 shared expense; the Authority is self-insured up to \$1,000,000 and excess insurance coverage has been purchased.

Crime Coverage - Public Employee Dishonesty, Forgery and Alteration, and Computer Fraud: Insured up to \$100,000 per occurrence with a \$1,000 deductible.

SAN GORGONIO PASS WATER AGENCY

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007 (with comparative data for 2006)

NOTE 6: JOINT VENTURE (continued)

Terrorism Coverage: Provides up to \$2,500,000 per occurrence for property damage caused by malicious or violent act declared by the U.S. government to involve terrorism.

Crisis Management Coverage by Public Response: Insured up to \$250,000 above the coverage limits.

Condensed financial information of the Authority for the year ended September 30, 2006 is as follows:

Total Assets	\$ 102,216,230
Total Liabilities	<u>73,348,877</u>
Net Assets	<u>\$ 28,867,353</u>
Total Revenues	\$ 20,068,101
Total Expenses	<u>16,228,461</u>
Increase in Net Assets	<u>\$ 3,839,640</u>

NOTE 7: POST-EMPLOYMENT MEDICAL HEALTH CARE BENEFITS

In addition to the pension benefits described in Note 5, the Agency provides post-employment medical benefits to eligible employees who retire from the Agency. The benefits provide retired employees with the same medical insurance coverage available to current employees. Pre-Medicare retirees, after attaining age 50 with 5 years service, will receive paid medical benefits up to a maximum dollar amount as set by board resolution.

At June 30, 2007, two retirees met these eligibility requirements. Expenditures for post-employment medical health care benefits are recognized as the premiums are paid. Expenditures of \$14,273 and \$11,724 were incurred by the Agency for post-employment medical health care benefits for the years ended June 30, 2007 and 2006, respectively.

NOTE 8: DEFERRED COMPENSATION PLAN

The Agency offers its employees a deferred compensation plan through the California Public Employees Deferred Compensation Plan and was created in accordance with Internal Revenue Code Section 457. The plan, available to all full-time Agency employees, permits them to defer a portion of their salary to be deposited in individual investment accounts. Funds may be withdrawn by participants upon termination, retirement, death or certified emergency. All assets and income of the deferred compensation plan are held in trust for the exclusive benefit of plan participants and their beneficiaries.