

**CITY OF LAKEPORT MUNICIPAL**  
**SEWER DISTRICT NO. 1**

**BASIC FINANCIAL STATEMENTS**

**JUNE 30, 2011**

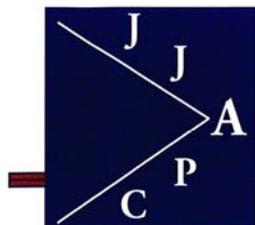
**City of Lakeport Municipal Sewer District No. 1**  
**Basic Financial Statements**  
**For the year ended June 30, 2011**

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JJACPA, Inc.

A Professional Accounting Services Corp.

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INDEPENDENT AUDITORS' REPORT

The Board of Directors  
City of Lakeport Municipal Sewer District No. 1  
Lakeport, California

We have audited the accompanying basic financial statements of the City of Lakeport Municipal Sewer District No. 1 (District) as of and for the year ended June 30, 2011, as listed in the foregoing table of contents. These basic financial statements are the responsibility of the management of the District. Our responsibility is to express an opinion on these basic financial statements based on our audit. The prior year summarized comparative information has been derived from the District's June 30, 2010, financial statements in which an unqualified opinion was expressed by other auditors 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 basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall basic financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the City of Lakeport Municipal Sewer District No. 1 as of June 30, 2011, and the results of its operations and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis (MD&A) on pages three to ten are not required parts of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the basic financial statements of the City of Lakeport Municipal Sewer District No. 1 taken as a whole. The accompanying supplementary schedule is presented for purposes of additional analysis and is not a required part of the basic financial statements. The information presented in this supplementary schedule has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

February 1, 2012

*JJACPA, Inc.*  
J JACPA, Inc.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Management's Discussion and Analysis**

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This section of City of Lakeport Municipal Sewer District No. 1's (District) basic financial statements presents management's discussion and analysis of the District's financial performance during the fiscal year ended June 30, 2011. Since this management's discussion and analysis is designed to focus on current activities, resulting change and current known facts, please read it in conjunction with the District's basic financial statements (pages 12 - 14) and the footnotes (pages 15 - 21).

**Financial Highlights**

At June 30, 2011, the District's net assets decreased to \$8,552,716 from \$8,724,240 in 2010 or \$171,524 as can be seen on Page 12. Operating revenues decreased by \$14,104 and non-operating revenues increased by \$55,103 as can be seen on Page 13. Operating expenses decreased by \$189,956 as can be seen on Page 7. Depreciation expense increased by \$18,471.

**Using This Report**

In December 1998, the Governmental Accounting Standards Board (GASB) released statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, which revised the reporting of property tax revenue. In June 1999, GASB released statement No. 34, *Basic Financial Statements -- and Management's Discussion and Analysis -- for State and Local Governments*. Changes in Statement No. 34 require a comprehensive one-line look at the entity as a whole and capitalization of assets and depreciation for agencies not reporting on the accrual basis of accounting. Since the District has historically reported all activities in enterprise funds in a manner similar to business activities and followed the accrual basis of accounting, the District merely has been required to reclassify certain balances to utilize the new Statement No. 34 terminology. There were no major reconciling items necessary or elimination of balances due to the implementation of Statement No. 34.

The annual financial statements include the Independent Auditors' Report, this management's discussion and analysis, the basic financial statements, and notes to basic financial statements.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Management's Discussion and Analysis, Continued**

**Financial Analysis of the District as a Whole**

	Net Assets		Increase (Decrease)	Percent Change
	As of June 30, 2011 and 2010			
	2011	2010		
<b>Assets:</b>				
Current assets	\$2,092,355	\$1,717,111	\$375,244	21.9%
Non-current assets	13,629,980	14,264,159	(634,179)	(4.4)%
<b>Total assets</b>	<b>15,722,335</b>	<b>15,981,270</b>	<b>(258,935)</b>	<b>(1.6)%</b>
<b>Liabilities:</b>				
Current liabilities	189,029	151,960	37,069	24.4%
Non-current liabilities	6,980,590	7,105,070	(124,480)	(1.8)%
<b>Total liabilities</b>	<b>7,169,619</b>	<b>7,257,030</b>	<b>(87,411)</b>	<b>(1.2)%</b>
<b>Net assets:</b>				
Investment in capital assets, net of related debt	6,532,659	7,635,928	(1,103,269)	(14.4)%
Restricted	796,958	60,919	736,039	1208.2%
Unrestricted	1,223,099	1,027,393	195,706	19.0%
<b>Total net assets</b>	<b>\$8,552,716</b>	<b>\$8,724,240</b>	<b>\$(171,524)</b>	<b>(2.0)%</b>

This schedule is prepared from the District's Statement of Net Assets (page 12), which is presented on the accrual basis of accounting whereby assets are capitalized and depreciated.

As can be seen from the table above, net assets at June 30, 2011, decreased to \$8,552,716 from \$8,724,240 in 2010 or \$171,524. This was a result of decreased operating revenue, which continued to be lower than operating expenses and the inclusion of depreciation and amortization, which are a non-cash expense. Restricted net assets represents amounts restricted for use in Assessment District 91-1.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Management's Discussion and Analysis, Continued**

**Financial Analysis of the District as a Whole, Continued**

**Operating Results**  
**For the years ended June 30, 2011 and 2010**

	<u>2011</u>	<u>2010</u>	<u>Increase (Decrease)</u>	<u>Percent Change</u>
<b>Operating revenues</b>	\$ 1,702,012	\$ 1,716,116	\$ (14,104)	(0.8)%
<b>Operating expenses</b>	<u>1,950,925</u>	<u>2,140,881</u>	<u>(189,956)</u>	<u>(8.9)%</u>
<b>Operating loss</b>	(248,913)	(424,765)	175,852	(41.4)%
<b>Non-operating revenues</b>	415,025	359,922	55,103	15.3%
<b>Non-operating expenses</b>	<u>(337,636)</u>	<u>(334,861)</u>	<u>(2,775)</u>	<u>0.0%</u>
<b>Net income (loss)</b>	(171,524)	(399,704)	228,180	(57.1)%
<b>Net assets:</b>				
Beginning of year	<u>8,724,240</u>	<u>9,123,944</u>	<u>(399,704)</u>	<u>(4.4)%</u>
End of year	<u>\$ 8,552,716</u>	<u>\$ 8,724,240</u>	<u>\$ (171,524)</u>	<u>(2.0)%</u>

While the Statement of Net Assets shows the change in financial position of net assets, the operating results are reflected in the Statement of Revenues, Expenses, and Changes in Net Assets (page 13). This statement provides answers to the nature and source of the change in financial position of net assets.

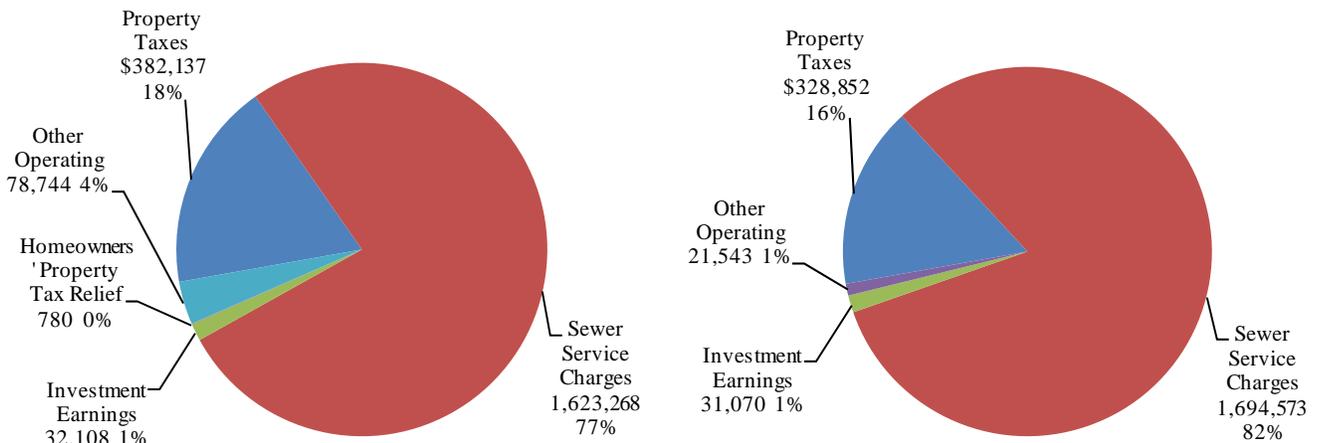
**City of Lakeport Municipal Sewer District No. 1  
Financial Statements  
For the year ended June 30, 2011**

**Management's Discussion and Analysis, Continued**

**Financial Analysis of the District as a Whole, Continued**

The following is a graphic illustration of revenues by source:

**Revenues By Source  
Both Operating & Non-Operating**



<u>FY 2010-2011</u>			<u>FY 2009-2010</u>		<u>Increase (Decrease)</u>
\$ 382,137	18.1%	<b>Property Taxes</b>	\$ 328,852	15.8%	\$ 53,285
1,623,268	76.7%	<b>Sewer Service Charges</b>	1,694,573	81.6%	(71,305)
32,108	1.5%	<b>Investment Earnings</b>	31,070	1.5%	1,038
780	0.0%	<b>Homeowners' Property Tax Relief</b>	-	0.0%	780
78,744	3.7%	<b>Other Operating</b>	21,543	1.0%	57,201
<u>\$ 2,117,037</u>	<u>100.0%</u>	<b>Totals</b>	<u>\$ 2,076,038</u>	<u>100.0%</u>	<u>\$ 40,999</u>

Property Taxes increased by \$53,285 due to County apportionments being slightly higher. Sewer user service charges decreased by \$71,305 as described on page 9. Investment Earnings increased by \$1,038 due to interest received on higher cash balances. Other revenues increased by \$57,201 primarily the result of connection fees, which can fluctuate dramatically from year to year.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Management’s Discussion and Analysis, Continued**

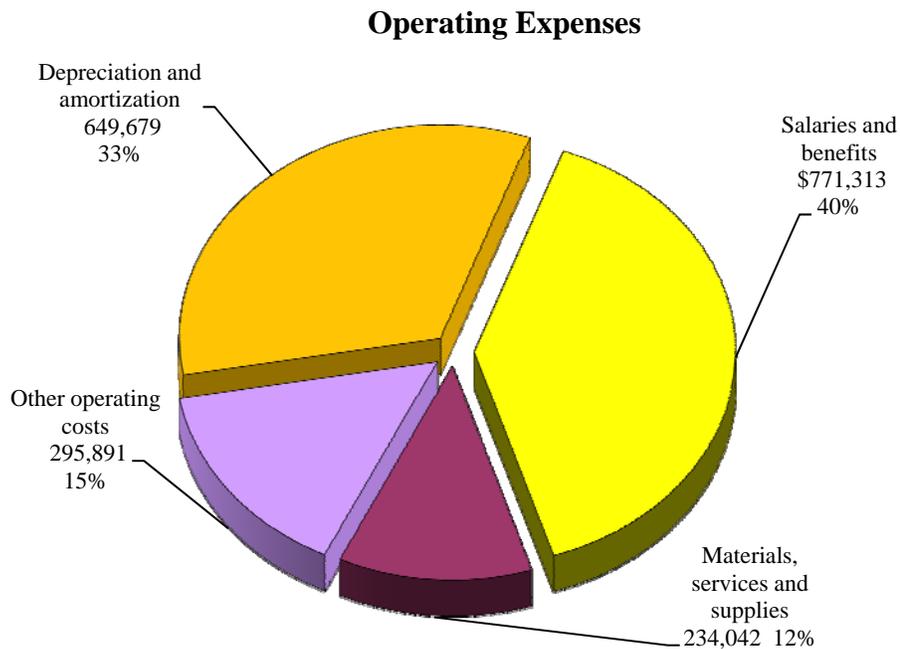
**Financial Analysis of the District as a Whole, Continued**

Operating Expenses decreased by \$189,956 as detailed below:

**Operating Expenses**  
**For the years ended June 30, 2011 and 2010**

	<u>2011</u>	<u>2010</u>	<u>Increase (Decrease)</u>	<u>Percent Change</u>
<b>Operating expenses:</b>				
Salaries and benefits	\$ 771,313	\$ 836,804	\$ (65,491)	(7.8)%
Materials, services and supplies	234,042	540,787	(306,745)	(56.7)%
Other operating costs	295,891	132,082	163,809	124.0%
Depreciation and amortization	649,679	631,208	18,471	2.9%
<b>Total</b>	<u>\$ 1,950,925</u>	<u>\$ 2,140,881</u>	<u>\$ (189,956)</u>	<u>(8.9)%</u>
<b>Net capital assets</b>	<u>\$ 13,464,659</u>	<u>\$ 14,075,711</u>	<u>\$ (611,052)</u>	<u>(4.3)%</u>

The following is a graphic illustration of operating expenses:



**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Management’s Discussion and Analysis, Continued**

**Financial Analysis of the District as a Whole, Continued**

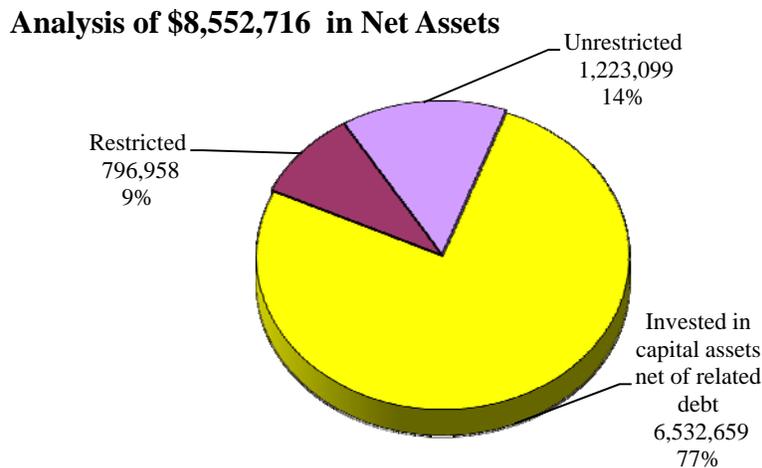
**Analysis of Net Assets**  
**As of June 30, 2011 and 2010**

	<u>2011</u>	<u>2010</u>	<u>Increase (Decrease)</u>	<u>Percent Change</u>
<b>Net assets:</b>				
Invested in capital assets	\$ 6,532,659	\$ 7,635,928	\$ (1,103,269)	(14.4)%
Restricted	796,958	60,919	736,039	1208.2%
Unrestricted	2,020,057	1,027,393	992,664	96.6%
<b>Total</b>	<u>\$ 9,349,674</u>	<u>\$ 8,724,240</u>	<u>\$ 625,434</u>	<u>7.2%</u>

The change in net assets is a decrease of \$171,524, primarily the result of decreased operating revenue, which was lower than operating expenses by \$248,913, but was offset by increased non-operating revenues, which exceeded non-operating expenses by \$77,389. Current charges for service and non-operating revenues, as compared with the year ended 2010, continue to be sufficient to fund operations, excluding depreciation and amortization, which are considered non-cash expenses. The District reported a net cash increase in 2011 of \$390,552.

The District’s revenue to expense ratio, excluding depreciation and amortization, was 1.70 at June 30, 2011. This ratio is illustrated further in the Schedule of Debt Service Coverage, included as a Supplementary Schedule at the end of this document.

The following is a graphic illustration of net assets:



**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Management's Discussion and Analysis, Continued**

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**Economic Factors and Potential Future Results**

The District completed a Sewer System Master Plan in June 2008. In 2008, the Plan identified most of the sanitary sewer system as being over 30 years old. The Master Plan provides guidance on system upgrades and refurbishments. Over the next 20 years (FY 2008-2009 through FY 2028-2029), capital investment was estimated at \$5,006,000. Since the Plan was completed, some construction projects far exceeded the Plan's estimates.

Using the Plan as a guide, the District continues to plan a program of repair and replacement of the sanitary infrastructure. To finance this effort, as well as on-going operations and maintenance, the sewer user service charge likely will be increased and outside funding will be sought, most likely through the United States Department of Agriculture (USDA), Rural Development.

The District is in the fourth year of a five-year rate increase plan, which began in 2007. That increase was the result of imposed regulatory requirements by the Central Valley State Water Resource Control Board under a cease and desist order. That order required the District to design and construct a wastewater irrigation field near the current treatment facility. It has proven insufficient, however, in meeting the short, medium, and long-term capital improvement goals of the District as well as adequately funding basic operations.

Since the 2008 plan was completed, the State and Regional Water Boards have implemented a system of requirements for wastewater collection agencies known as a Sewer System Management Plan (SSMP) that sets out additional parameters for master plans that were not addressed in the 2008 plan.

Asset Management refers to the establishment of levels of services for the District. These levels of service, similar to roles or the function of the sewer system, are:

1. Maintain sewer service to customers.
2. Maintain regulatory compliance.
3. Minimize inflow and infiltration (I/I).
4. Fund and implement an aggressive capital improvement program.

The costs associated with maintaining adequate levels of service are highly dependent on the age of the system, I/I issues, and the topography of the District. Wastewater flow from individual dwelling units is a relatively minor component when determining projects and their associated costs. It is important to note that the rehabilitation/replacement of sewer mains and laterals is as much (if not more so) a result of changes in design requirements as it is a result of deteriorated and undersized pipes.

Over the next 20 years major capital investment is estimated at \$10,000,000. Staff continues to evaluate a second 5-year stepped increase in the sewer user service charge and low interest, long-term loans/bonds to finance the effort, as well as on-going operations and maintenance.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Management's Discussion and Analysis, Continued**

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**Contacting the District's Financial Management**

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the District's finances and to show the District's accountability for the money it receives. If you have questions about this report, contact City of Lakeport Municipal Sewer District No. 1 in care of the City of Lakeport, 225 Park Street, Lakeport, CA, (707) 263-5615.

## **BASIC FINANCIAL STATEMENTS**

# City of Lakeport Municipal Sewer District No. 1

## Statement of Net Assets

June 30, 2011

(with comparative balances for June 30, 2010)

	<u>2011</u>	<u>2010</u>
<b>ASSETS</b>		
Current assets:		
Cash equivalents and investments - pooled	\$ 1,931,497	\$ 1,540,945
Accounts receivable	119,016	127,239
Taxes receivable	11,218	-
Interest receivable	175	-
Inventory	30,449	48,927
Total current assets	<u>2,092,355</u>	<u>1,717,111</u>
Property, plant and equipment:		
Non-depreciable	1,735,233	1,735,233
Depreciable	22,039,363	22,023,863
Less accumulated depreciation	<u>(10,309,937)</u>	<u>(9,683,385)</u>
Net property, plant and equipment	<u>13,464,659</u>	<u>14,075,711</u>
Deferred charges	<u>165,321</u>	<u>188,448</u>
<b>Total assets</b>	<u><u>\$ 15,722,335</u></u>	<u><u>\$ 15,981,270</u></u>
<b>LIABILITIES AND NET ASSETS</b>		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 50,671	\$ 50,352
Compensated absences	4,806	4,600
Interest payable	133,552	97,008
Total current liabilities	<u>189,029</u>	<u>151,960</u>
Long-term liabilities:		
Compensated absences	48,590	15,070
Due within one year	160,000	155,000
Due after one year	6,772,000	6,935,000
Total long-term liabilities	<u>6,980,590</u>	<u>7,105,070</u>
Total liabilities	<u>7,169,619</u>	<u>7,257,030</u>
Net assets:		
Invested in capital assets, net of related debt	6,532,659	7,635,928
Restricted	796,958	60,919
Unrestricted	1,223,099	1,027,393
Total net assets	<u>8,552,716</u>	<u>8,724,240</u>
<b>Total liabilities and net assets</b>	<u><u>\$ 15,722,335</u></u>	<u><u>\$ 15,981,270</u></u>

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

**City of Lakeport Municipal Sewer District No. 1**  
**Statement of Revenues, Expenses, and Changes in Net Assets**  
**For the year ended June 30, 2011**  
**(with comparative balances for the year ended June 30, 2010)**

	<u>2011</u>	<u>2010</u>
<b>OPERATING REVENUES:</b>		
Charges for services:		
Sewer service charges	\$ 1,623,268	\$ 1,694,573
Other	78,744	21,543
<b>Total operating revenues</b>	<u>1,702,012</u>	<u>1,716,116</u>
<b>OPERATING EXPENSES:</b>		
Salaries and benefits	771,313	836,804
Materials, services and supplies	234,042	540,787
Other operating costs	295,891	132,082
Depreciation and amortization expense	649,679	631,208
<b>Total operating expenses</b>	<u>1,950,925</u>	<u>2,140,881</u>
<b>OPERATING LOSS</b>	<u>(248,913)</u>	<u>(424,765)</u>
<b>NON-OPERATING REVENUES (EXPENSES):</b>		
Property taxes	382,137	328,852
Homeowners' property tax relief	780	-
Investment earnings	32,108	31,070
Interest and debt service expenses	(337,636)	(334,861)
<b>Total non-operating revenues (expenses)</b>	<u>77,389</u>	<u>25,061</u>
<b>Net income</b>	<u>(171,524)</u>	<u>(399,704)</u>
<b>NET ASSETS:</b>		
Beginning of year	<u>8,724,240</u>	<u>9,123,944</u>
End of year	<u>\$ 8,552,716</u>	<u>\$ 8,724,240</u>

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

**City of Lakeport Municipal Sewer District No. 1**  
**Statement of Cash Flows**  
**For the year ended June 30, 2011**  
**(with comparative balances for the year ended June 30, 2010)**

	<u>2011</u>	<u>2010</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Receipts from customers	\$ 1,710,235	\$ 1,715,778
Payments to vendors for services and supplies	(511,774)	(713,395)
Payments to City of Lakeport employees	(737,587)	(812,710)
<b>Net cash provided(used) by operating activities</b>	<u>460,874</u>	<u>189,673</u>
<b>CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES:</b>		
Property taxes and apportioned amounts	394,135	328,852
<b>Net cash provided by non-capital financing activities</b>	<u>394,135</u>	<u>328,852</u>
<b>CASH FLOW FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>		
Acquisition and construction of capital assets	(15,500)	(24,439)
Principal payments on long-term debt	(158,000)	(145,000)
Interest paid on long-term financing	(322,890)	(358,566)
<b>Net cash used by capital and related financing activities</b>	<u>(496,390)</u>	<u>(528,005)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Investment income received	31,933	31,070
<b>Net increase(decrease) in cash</b>	390,552	21,590
<b>CASH AND INVESTMENTS:</b>		
Beginning of year	1,540,945	1,519,355
End of year	<u>\$ 1,931,497</u>	<u>\$ 1,540,945</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Reconciliation of operating income (loss) to net cash provided (used) by operating activities:		
Operating loss	\$ (248,913)	\$ (424,765)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities		
Depreciation and amortization	649,679	631,208
Changes in current assets and liabilities:		
Accounts receivable	8,223	(338)
Inventory	18,478	(8,827)
Accounts payable and accrued liabilities	(319)	(20,057)
Compensated absences	33,726	12,452
<b>Net cash provided(used) by operating activities</b>	<u>\$ 460,874</u>	<u>\$ 189,673</u>

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

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Notes to Basic Financial Statements**

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**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The financial statements of City of Lakeport Municipal Sewer District No. 1 (District) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental enterprises classified as proprietary fund types. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The reports are based on all applicable GASB pronouncements as well as applicable Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Review Boards of the Committee on Accounting Procedure issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The more significant of the District's accounting policies are described below.

**A. Description of the Reporting Entity**

City of Lakeport Municipal Sewer District No. 1 is a component unit of the City of Lakeport. The District provides sewage collection services for the City, limited areas of the surrounding communities referred to as North Lakeport and certain unincorporated land within Lake County. The District's collection system consists of approximately 135,400 feet of collector mains and 13,500 feet of interceptor sewers. The District is an integral part of the City and is included in the City's June 30, 2011, and 2010, basic financial statements. City personnel provide all engineering, management, and operational services to the wastewater collection system, including management and operational services for sewage collection pump station maintenance. A large portion of the funding of the District's sewage facilities was funded by federal and state sources, with the remainder of the funding by the District's users.

**B. Fund Accounting Classification and Basis of Accounting**

On the Statement of Net Assets and the Statement of Revenues, Expenses, and Changes in Net Assets, business-like activities are presented using the economic resources measurement focus. The accounting objectives of this measurement focus are the determination of net income, financial position, and cash flows. All assets and liabilities (whether current or noncurrent) associated with their activities are reported. Fund equity is classified as net assets.

Enterprise funds account for operations that are financed and operated in a manner similar to private business enterprises where the intent is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges. The acquisition and capital improvement of the physical plant facilities required to provide these goods and services are financed from existing cash resources, the issuance of bonds, and cash flow from operations.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Notes to Basic Financial Statements, Continued**

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**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued**

**B. Fund Accounting Classification and Basis of Accounting, continued**

The District's operations are funded almost entirely by user fees imposed as a rate based on type of usage (e.g. commercial, residential, etc.). The bulk of that rate is a flat amount charged primarily to residential users. Commercial accounts are charged a tiered rate based on water usage. The District collects a small maintenance and operations user fee (applied to operations) and a special assessment, which is applied to the repayment of a bond issued to construct the current treatment facility in 1993.

**C. Cash Equivalents and Investments**

For the purposes of the Statement of Net Assets and Statement of Cash Flows, "cash equivalents and investments" includes all demand, savings accounts, and certificates of deposits or short-term investments with an original maturity of three months or less.

The District, through the City of Lakeport, pools cash and investments from all funds for the purpose of increasing income through investment activities. Highly liquid money market investments with maturities of one year or less at time of purchase are stated at amortized cost. All other investments are stated at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Market value is used as fair value for those securities for which market quotations are readily available.

The District indirectly, through the City of Lakeport, participates in an investment pool managed by the State of California titled Local Agency Investment Fund (LAIF) which has invested a portion of the pool funds in Structured Notes and Asset-Backed Securities. LAIF's investments are subject to credit risk with the full faith and credit of the State of California collateralizing these investments. In addition, these Structured Notes and Asset-Backed Securities are subject to market risk as to changes in interest rates.

**D. Fixed Assets**

Purchased fixed assets are valued at cost where historical records are available and at an estimated historical cost where no historical records exist. Donated fixed assets are valued at their estimated fair value on the date received.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. Improvements are capitalized. Depreciation is provided on a straight-line basis over estimated useful lives ranging from 5 to 40 years.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Notes to Basic Financial Statements, Continued**

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**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued**

**E. Compensated Absences**

The liability for vested vacation pay is recorded as an expense when the vacation is taken. Unused balances of vacation and sick time are accrued by employees when earned and may be subject to maximum accrual limits. Sick time accrued is paid in full to the employee when employment is terminated. There is no maximum accrual amount for sick time. Vacation time has a maximum accrual of 400 hours, dependent on the accrual rate of that employee, which is based on years of service. Upon termination of employment, vacation is paid out at a maximum of 50% of the accrued time available, depending on years of service. Compensatory time accrued is paid in full at the end of employment. The District estimates that 9% of accrued time would be used within the next operating period (twelve months).

**F. Comparative Data**

Comparative data for the prior year has been presented in the accompanying financial statements in order to provide an understanding of changes in the District's financial position and operations.

**G. Reclassifications**

Certain amounts from the prior year have been reclassified to conform to the current year's presentation.

**2. CASH AND INVESTMENTS**

**A. Cash Deposits**

The District pools cash from all sources. The District invests excess cash in the City of Lakeport, an unrated investment pool, which at June 30, 2011, approximated fair value of \$6,433,021.

The California Government Code requires California banks and savings and loan associations to secure government cash deposits by pledging securities as collateral. This Code states that collateral pledged in this manner shall have the effect of perfecting a security interest in such collateral superior to those of a general creditor. Thus, collateral is considered to be held in the government's name.

According to California law, the market value of pledged securities with banking institutions must equal at least 110% of the government's cash deposits. California law also allows institutions to secure government deposits by pledging first trust deed mortgage notes having a value of 150% of the government's total cash deposits. The government can waive collateral requirements for cash deposits, which are fully insured up to \$250,000 by the Federal Deposit Insurance Corporation.

The City Treasurer maintains the cash and investment pool, on behalf of the District, as their custodian, which includes cash balances and authorized investments for all District funds, which is invested to enhance interest earnings. The pooled interest earned is allocated monthly to the District based on average daily cash and investment balance.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Notes to Basic Financial Statements, Continued**

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**2. CASH AND INVESTMENTS, Continued**

**B. Authorized Investments**

Under provisions of the District/City's Investment Policy and in accordance with California Government Code Section 53601 & 53635 (a-n), the District/City may invest or deposit in the following types of investments:

- Local District Bonds
- US Treasury Obligations
- US Agencies
- Time Deposits
- Negotiable Certificates of Deposit
- Bankers' Acceptances
- Commercial Paper
- Local Agency Investment Funds (LAIF) of California State Treasurer's Office (State Pool)
- State of California Obligations
- CA Local District Obligations
- Repurchase Agreements (Repos)
- Reverse Repurchase Agreements
- Medium-Term Notes (Corporate Debt Investment Grade)
- Mutual Funds
- Money Market Funds
- Collateralized Bank Deposits

Criteria for selecting investments and the order of priority are:

- *Safety* - The safety and risk associated with an investment refers to the potential loss of principal, interest, or a combination of these amounts. The District/City only invests in those investments that they consider very safe.
- *Liquidity* - This refers to the ability to "cash in" at any moment in time with a minimal possibility of losing some portion of principal or interest. Liquidity is an important investment quality especially when the need for unexpected funds occurs occasionally.
- *Yield* - This refers to the rate of return and is the least important of the criteria. Safe, liquid investments do not enjoy the yields of investments not having those characteristics.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Notes to Basic Financial Statements, Continued**

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**2. CASH AND INVESTMENTS, Continued**

**C. Safekeeping**

Securities purchased from broker-dealers are held in third party safekeeping by the trust department of the broker-dealer or other designated third party trust in the District/City's name and control, whenever possible.

**D. Investments in External Investment Pools**

The District's investments with the City at June 30, 2011, included a portion of the pool funds invested in structured notes and asset backed securities and similar transactions through the Local Agency Investment Fund (LAIF). These investments may include the following:

*Structured Notes* are debt securities (other than asset-backed securities) whose cash-flow characteristics (coupon rate, redemption amount, or stated maturity) depends on one or more indices and/or that have embedded forwards or options.

*Asset-backed Securities*, the bulk of which are mortgage-backed securities, entitle their purchaser to receive a share of the cash flows from a pool of assets such as principal and interest repayments from a pool of mortgages (such as CMOs) or credit card receivables.

As of June 30, 2011, LAIF had invested 1.91% of its pooled assets in structured notes and asset-backed securities and similar transactions.

**3. PROPERTY TAXES**

Property taxes attach as an enforceable lien as of March 1. Taxes are levied on July 1 and payable in two installments on December 10 and April 10. All general property taxes are then allocated by the County Auditor's office utilizing the Teeter System of allocation in which levied amounts are directly allocated to the various taxing entities per the legislation-implementing Proposition 13 and the County retains any interest and penalties on delinquent taxes. The method of allocation used by the County is subject to review by the State of California.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Notes to Basic Financial Statements, Continued**

**4. CAPITAL ASSETS**

The following is a summary of changes in property, plant and equipment during the fiscal year:

	Balance June 30, 2010	Additions	Deletions	Balance June 30, 2011
Land	\$1,735,233	\$ -	\$ -	\$1,735,233
Buildings, improvements and infrastructure	21,574,244	147,558	-	21,721,802
Equipment	449,619	-	(132,058)	317,561
Total depreciable property, at cost	22,023,863	147,558	(132,058)	22,039,363
Accumulated depreciation	(9,683,385)	(626,552)	-	(10,309,937)
Total depreciable property, net	12,340,478	(478,994)	(132,058)	11,729,426
Total	<u>\$14,075,711</u>	<u>\$(478,994)</u>	<u>\$(132,058)</u>	<u>\$13,464,659</u>

These assets are being depreciated on a straight-line basis over their estimated useful lives ranging from 5 to 40 years.

**5. LONG-TERM LIABILITIES**

The District generally incurs debt to finance projects or purchase assets, which will have useful lives equal to or greater than the related debt. The District's debt issues and transactions related to District activities are summarized below and discussed in detail subsequently:

	Balance July 1, 2010	Additions	Retirements	Balance June 30, 2011	Due Within One Year
2007 Series A Sewer Revenue Bonds	\$3,010,000	\$ -	\$ (55,000)	\$ 2,955,000	\$ 55,000
Sewer District Improvement Bonds	4,110,000	-	(100,000)	4,010,000	105,000
Compensated absences	19,670	53,396	(19,670)	53,396	4,806
Total	<u>\$ 7,139,670</u>	<u>\$ 53,396</u>	<u>\$ (174,670)</u>	<u>\$ 7,018,396</u>	<u>\$ 164,806</u>

**2007 Sewer Revenue Bonds Series A** – 2007 Series A, total issue \$3,060,000. Annual principal and interest payments are due September 1<sup>st</sup>, with semiannual interest payments due March 1<sup>st</sup>, interest at 5.31% per annum, secured by wastewater fund revenue, maturing in year 2037.

**Sewer District Improvement Bonds** – Series 1993-1, USDA Rural Development, total issue 5,196,270. Annual principal and interest payments are due September 1<sup>st</sup>, with semi-annual interest payments due March 1<sup>st</sup>, interest at 5% per annum, secured by property assessment revenue from the South Assessment District 91-1, maturing in year 2032.

**City of Lakeport Municipal Sewer District No. 1**  
**Financial Statements**  
**For the year ended June 30, 2011**

**Notes to Basic Financial Statements, Continued**

**5. LONG-TERM LIABILITIES, Continued**

Future debt service at June 30, 2011, is as follows for the Bonds:

Year Ending June 30,	2007 Sewer Revenue Bonds		Sewer District		Total	
	Series A		Improvement Bonds			
	Principal	Interest	Principal	Interest	Principal	Interest
2012	\$ 55,000	\$ 132,260	\$ 105,000	\$ 199,875	\$ 160,000	\$ 332,135
2013	60,000	129,960	110,000	192,500	170,000	322,460
2014	60,000	127,560	115,000	186,875	175,000	314,435
2015	65,000	125,060	120,000	3,000	185,000	128,060
2016	65,000	122,460	125,000	174,875	190,000	297,335
2017-2021	375,000	569,300	735,000	770,125	1,110,000	1,339,425
2022-2026	460,000	478,625	935,000	562,375	1,395,000	1,041,000
2027-2031	575,000	362,377	1,200,000	297,250	1,775,000	659,627
2032-2036	720,000	212,248	565,000	28,625	1,285,000	240,873
2037-2041	520,000	37,763	-	-	520,000	37,763
Total	\$ 2,955,000	\$ 2,297,613	\$ 4,010,000	\$ 2,415,500	\$ 6,965,000	\$ 4,713,113
Due within one year	\$ 55,000	\$ 132,260	\$ 105,000	\$ 199,875	\$ 160,000	\$ 332,135
Due after one year	2,900,000	2,165,353	3,905,000	2,215,625	6,805,000	4,380,978
Total	\$ 2,955,000	\$ 2,297,613	\$ 4,010,000	\$ 2,415,500	\$ 6,965,000	\$ 4,713,113

**6. RISK MANAGEMENT**

The District is insured under the City and 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 City's insurance coverage and the respective coverage providers are as follows:

Amount	Coverage Provider	Payment Source
<b>Liability Claim:</b>		
\$0 - \$5,000	Self-insured	Banking layer
\$5,001 - \$10,000,000	Redwood Empire Municipal Insurance Fund	Shared risk
<b>Workers' Compensation:</b>		
\$0 - \$5,000	Self-insured	Banking layer
\$5,001 - Statutory	Redwood Empire Municipal Insurance Fund	Shared risk

The City purchases insurance through the Redwood Empire Municipal Insurance Fund (REMIF) for all other risks of loss. The City also participates in insurance programs through REMIF for employee dental and vision claims. There have been no significant reductions in insurance coverage from coverage in the prior fiscal year.

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**SUPPLEMENTARY SCHEDULES**

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**City of Lakeport Municipal Sewer District No. 1**  
**Schedule of Debt Service Coverage**  
**June 30, 2011 and 2010**

In conjunction with the 2007 Series A Sewer Revenue Bonds, the District has covenanted to fix, prescribe and collect rates and charges for the sewer service which will be sufficient to yield during the year net revenues equal to 110% of the debt service paid during the year. For purposes of this calculation, net revenues equals net income plus depreciation and amortization expenses. The debt service requirement for 2011 and 2010 is as follows:

	2011	2010
Operating loss	\$ (248,913)	\$ (424,765)
Add:		
Depreciation and amortization	649,679	631,208
Interest revenue	32,108	31,070
Property taxes	382,137	328,852
Homeowners' property tax relief	780	-
Net revenue	<u>\$ 815,791</u>	<u>\$ 566,365</u>
Debt service:		
Principal	\$ 158,000	\$ 145,000
Interest	<u>322,890</u>	<u>358,566</u>
Total debt service	<u>\$ 480,890</u>	<u>\$ 503,566</u>
Calculated coverage	<u>1.70</u>	<u>1.12</u>

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