

**PINE-STRAWBERRY
WATER IMPROVEMENT DISTRICT
REPORT ON AUDIT OF FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2010**

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
JUNE 30, 2010**

<u>CONTENTS</u>	<u>PAGE</u>
Report on Audit of Financial Statements	
Independent Auditors' Report	1
Management's Discussion and Analysis (MD&A) (Required Supplementary Information)	4
Statement of Net Assets	9
Statement of Revenues, Expenses and Changes in Net Assets	10
Statement of Cash Flows	11
Notes to Financial Statements	12

REPORT ON AUDIT OF FINANCIAL STATEMENTS



HEINFELD, MEECH & CO., P.C.
CERTIFIED PUBLIC ACCOUNTANTS



INDEPENDENT AUDITORS' REPORT

Governing Board
Pine-Strawberry Water Improvement District

We have audited the accompanying financial statements of Pine-Strawberry Water Improvement District (District), as of and for the year ended June 30, 2010, 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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 the 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 respective financial position of Pine-Strawberry Water Improvement District, as of June 30, 2010, and 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.

Without qualifying our opinion, we draw attention to Note 9 to the financial statements. The District has entered into a note agreement with a balloon payment due on September 30, 2012. Current cash flows are not sufficient to make the payment. The ultimate outcome of the District's efforts to refinance the note is not presently determinable.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 22, 2011, on our consideration of Pine-Strawberry Water Improvement 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.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 8 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audit of the 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.

Heinfeld, Meech & Co., P.C.

HEINFELD, MEECH & CO., P.C.
Certified Public Accountants

March 22, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
(Required Supplementary Information)

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
YEAR ENDED JUNE 30, 2010**

As management of the Pine-Strawberry Water Improvement District (District), we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2010. The District will be providing one year of information as this is the first year the District has undergone an audit.

FINANCIAL HIGHLIGHTS

- The District's total net assets decreased \$425,165, which represents a 370 percent decrease from the prior fiscal year as a result of the District acquiring a water utility company during the fiscal year.
- Operating revenues accounted for \$1.1 million in revenue, or 100 percent of all current fiscal year revenues an increase of 1,100 percent from the prior year.
- The District had approximately \$1.2 million in operating expenses, an increase of 226 percent from the prior fiscal year. The increase is due to the District acquiring a water utility company during the fiscal year.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the District's financial statements. The District's financial statements comprise two components: 1) proprietary financial statements, and 2) notes to the financial statements.

The *statement of net assets* presents information on all the District's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The *statement of revenues, expenses, and changes in net assets* presents information showing how the District's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The *statement of cash flows* outlines the cash inflows and outflows related to the operation of the District for the year ended June 30, 2010.

As discussed more thoroughly in Note 1 to the financial statements, the operations of the District are accounted for in a single proprietary fund. As a result, only the financial statements required for a proprietary fund are presented.

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
YEAR ENDED JUNE 30, 2010**

OVERVIEW OF FINANCIAL STATEMENTS (Concl'd)

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes to the financial statements can be found immediately following the basic financial statements.

FINANCIAL ANALYSIS

Net assets may serve over time as a useful indicator of a government's financial position. In the case of the District, liabilities exceeded assets by \$310,283 at the current fiscal year end.

At the fiscal year end the District carried negative net assets. In addition, a portion of the District's net assets are restricted by statute for the specified purpose of debt service repayment.

The following table presents a summary of the District's net assets for the fiscal year ended June 30, 2010.

	As of June 30, 2010
Current and other assets	\$ 2,267,802
Capital assets, net	2,302,510
Total assets, net	4,570,312
Current and other liabilities	116,696
Long-term liabilities	4,763,899
Total liabilities	4,880,595
Net assets:	
Invested in capital assets, net of related debt	(2,461,389)
Restricted	386,956
Unrestricted	1,764,150
Total net assets	\$ (310,283)

The District's financial position is the product of several financial transactions including the net result of activities, the acquisition of debt, the acquisition and disposal of capital assets, and the depreciation of capital assets. The following are significant current year transactions that had an impact on the Statement of Net Assets.

- The addition of \$2.7 million in capital assets through the acquisition of a water utility company.
- The addition of \$4.2 million in notes to purchase a water utility company.

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
YEAR ENDED JUNE 30, 2010**

FINANCIAL ANALYSIS (Concl'd)

Changes in net assets. The District's total revenues for the current fiscal year were \$1.1 million. The total expenses were \$1.5 million. The following table presents a summary of the changes in net assets for the fiscal year ended June 30, 2010.

	Fiscal Year Ended June 30, 2010
Revenues:	
Operating revenues:	
Other local	\$ 1,582
Property taxes	312,916
Water fees	777,905
Nonoperating revenues:	
Investment income	1,076
Total revenues	1,093,479
 Expenses:	
Operating expenses:	
Operations	449,464
Administration	314,186
Board of directors	83,438
Depreciation	349,144
Amortization – goodwill	31,439
Nonoperating expenses:	
Interest expense and loan fees	290,973
Total expenses	1,518,644
Change in net assets	\$ (425,165)

The following is a significant current year transaction that had an impact on the change in net assets.

- The District acquired a water utility company.

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
YEAR ENDED JUNE 30, 2010**

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets. At year end, the District had invested \$2.7 million in capital assets, including wells, distribution piping, fire hydrants, vehicles, computers, and other equipment. This amount represents a net increase prior to depreciation of \$2.7 million from the prior fiscal year, primarily due to the District acquiring a water utility company. Total depreciation expense for the current fiscal year was \$349,144.

The following schedule presents a summary of capital asset balances for the fiscal year ended June 30, 2010.

	As of June 30, 2010
Capital assets – non-depreciable	\$ 293,300
Capital assets – depreciable, net	<u>2,009,210</u>
Total	<u>\$ 2,302,510</u>

The estimated cost to complete current construction projects is \$685,000.

Additional information on the District's capital assets can be found in Note 6.

Debt Administration. At year end, the District had \$4.8 million in long-term debt outstanding. This represents a net increase of \$4.8 million due to the issuance of \$4.8 million in notes.

Additional information on the District's long-term debt can be found in Notes 9 and 10.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

Many factors were considered by the District's administration during the process of developing the fiscal year 2010-11 budget. Among them:

- Fiscal year 2009-10 budget balance carry forward (estimated \$160,080).
- Employee salaries.

Also considered in the development of the budget is the local economy and inflation of the surrounding area.

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
YEAR ENDED JUNE 30, 2010**

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, and investors and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the resources it receives. If you have questions about this report or need additional information, contact the Business and Finance Department, Pine-Strawberry Water Improvement District, P.O. Box 134, Pine, AZ 85544-0134.

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
STATEMENT OF NET ASSETS
PROPRIETARY FUND
JUNE 30, 2010**

ASSETS

Current assets:

Cash and investments	\$ 541,349
Property taxes receivable	10,026
Accounts receivable	41,186
Prepaid items	3,967
Inventory, at cost	58,486
Total current assets	655,014

Noncurrent assets:

Deferred charges	386,675
Land	91,239
Infrastructure	2,183,737
Leasehold improvements	5,665
Buildings and improvements	83,705
Vehicles, furniture and equipment	85,247
Construction in progress	202,061
Accumulated depreciation	(349,144)
Goodwill - net of amortization	1,226,113
Total noncurrent assets	3,915,298
Total assets	4,570,312

LIABILITIES

Current liabilities:

Accounts payable	34,540
Deposits held for others	82,156
Total current liabilities	116,696

Noncurrent liabilities:

Non-current portion of long-term obligations	4,763,899
Total non-current liabilities	4,763,899
Total liabilities	4,880,595

NET ASSETS

Invested in capital assets, net of related debt	(2,461,389)
Restricted for:	
Debt service	386,956
Unrestricted	1,764,150
Total net assets	\$ (310,283)

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2010**

Operating revenues:	
Other local	\$ 1,582
Property taxes	312,916
Water fees	777,905
Total operating revenues	<u>1,092,403</u>
Operating expenses:	
Operations	449,464
Administration	314,186
Board of Directors	83,438
Depreciation	349,144
Amortization - goodwill	31,439
Total operating expenses	<u>1,227,671</u>
Operating loss	<u>(135,268)</u>
Nonoperating revenues (expenses):	
Investment income	1,076
Interest expense and loan fees	<u>(290,973)</u>
Total nonoperating revenues (expenses)	<u>(289,897)</u>
Changes in net assets	<u>(425,165)</u>
Total net assets, beginning of year	114,882
Total net assets, end of year	<u><u>\$ (310,283)</u></u>

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2010**

Increase in Cash and Cash Equivalents

Cash flows from operating activities:

Cash received from customers, service fees	\$ 713,999
Cash received from customers, capacity fees and other	106,458
Cash received from property taxes	302,890
Cash paid to suppliers	<u>(966,025)</u>

Net cash provided by operating activities 157,322

Cash flows from capital and related financing activities:

Interest paid	(34,319)
Purchase of capital assets, including related goodwill	(3,909,206)
Costs of water utility acquisition	(515,002)
Proceeds from bank loan	<u>4,164,000</u>

Net cash used for capital and related financing activities (294,527)

Cash flows from noncapital financing activities:

Proceeds from line of credit	<u>599,899</u>
------------------------------	----------------

Net cash provided by noncapital financing activities: 599,899

Cash flows from investing activities:

Interest on investments	<u>1,076</u>
-------------------------	--------------

Net cash provided by investing activities 1,076

Net increase in cash and cash equivalents 463,770

Cash and cash equivalents, beginning of year 77,579

Cash and cash equivalents, end of year \$ 541,349

Reconciliation of Operating Loss to Net Cash Provided By Operating Activities:

Operating loss \$ (263,595)

Adjustments to reconcile operating loss to net cash provided by operating activities:

Depreciation	349,144
Amortization	31,439
Changes in assets and liabilities:	
Decrease in other assets	37,303
Increase in property taxes receivable	(10,026)
Increase in accounts receivable	(41,186)
Increase in prepaid items	(3,967)
Increase in inventory	(58,486)
Increase in accounts payable	34,540
Increase in deposits held for others	<u>82,156</u>

Net cash provided by operating activities: \$ 157,322

PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Pine-Strawberry Water District (District) have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to government units. The operations of the District are presented in the accompanying financial statements as a single proprietary fund. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The more significant of the District's accounting policies are described below.

A. Reporting Entity

Management of the District is independent of other state or local governments. The County Treasurer collects taxes for the District, but exercises no control over its expenditures/expenses.

The Board of Directors consists of five members elected by the public. Under existing statutes, the Board of Directors' duties and powers include, but are not limited to, the acquisition, maintenance and disposition of District property, charges for water and related services.

The Board also has broad financial responsibilities, including the approval of the annual budget, and the establishment of a system of accounting and budgetary controls.

The financial reporting entity consists of a primary government. A component unit is a legally separate entity that must be included in the reporting entity in conformity with generally accepted accounting principles. The District is a primary government because it is a special-purpose government that has a separately elected governing body, is legally separate, and is fiscally independent of other state or local governments. Furthermore, there are no component units combined with the District for financial statement presentation purposes, and the District is not included in any other governmental reporting entity. Consequently, the District's financial statements include only the funds of those organizational entities for which its elected Board of Directors is financially accountable. The District's major operations include education, construction and maintenance of District facilities, and charges for water and related services.

PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

B. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The District's 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 when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied.

Operating revenues and expenses are distinguished from *nonoperating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the District are water fees and property taxes. Operating expenses include the cost of goods and services and administrative expenses. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The District has elected not to follow subsequent private-sector guidance.

C. Cash and Investments

For purposes of the Statement of Cash Flows, the District considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. Cash and cash equivalents at year end were cash in bank, and cash and investments held by the County Treasurer.

D. Investment Income

Investment income is composed of interest, dividends, and net changes in the fair value of applicable investments. Investment income is included in nonoperating revenues in the enterprise financial statements.

E. Receivables and Payables

All receivables, including property taxes receivable, are shown net of an allowance for uncollectibles.

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Property tax levies are obtained by applying tax rates against either the primary assessed valuation or the secondary assessed valuation. Primary and secondary valuation categories are composed of the exact same properties. However, the primary category limits the increase in property values to 10% from the previous year, while there is no limit to the increase in property values for secondary valuation. Override and debt service tax rates are applied to the secondary assessed valuation and all other tax rates are applied to the primary assessed valuation.

The County levies real property taxes on or before the third Monday in August, which become due and payable in two equal installments. The first installment is due on the first day of October and becomes delinquent after the first business day of November. The second installment is due on the first day of March of the next year and becomes delinquent after the first business day of May. The billings are considered past due after these dates, at which time the applicable property is subject to penalties and interest.

The County also levies various personal property taxes during the year, which are due the second Monday of the month following receipt of the tax notice, and become delinquent 30 days thereafter.

Pursuant to A.R.S., a lien against assessed real and personal property attaches on the first day of January preceding assessment and levy; however according to case law, an enforceable legal claim to the asset does not arise.

F. Inventory

All inventories are valued at cost using the first-in/first-out (FIFO) method. Inventories consist of expendable supplies held for consumption. Inventories are recorded as expenses when consumed.

G. Prepaid Items

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in the enterprise financial statements.

H. Capital Assets

Capital assets, which include land and improvements, buildings and improvements, vehicles, furniture, and equipment, and construction in progress.

On September 30, 2009 the District acquired a water utility company. The District valued the assets using the Reconstructed Cost New Less Depreciation (RCNLD) method.

PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Capital assets are defined by the District as assets with an initial, individual cost in excess of \$1,000 and an estimated useful life of more than one year. Such assets are recorded at historical cost, or estimated historical cost if actual historical cost is not available. Donated capital assets are recorded at the estimated fair market value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend the life of the asset are not capitalized.

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

Infrastructure	5 – 50 years
Leasehold improvements	3 years
Buildings and improvements	10 years
Vehicles, furniture and equipment	5 – 10 years

I. Long-term Obligations

In the proprietary financial statements, long-term debt and other long-term obligations are reported as liabilities on the statement of net assets. Note premiums and discounts, as well as issuance costs and the difference between the reacquisition price and the net carrying amount of the old debt, are deferred and amortized over the life of the notes using the straight-line method over the term of the related debt.

J. Net Assets

Net assets comprise the various net earnings from operating income, nonoperating revenues and expenses, and capital contributions. Net assets are classified in the following three components.

Invested in capital assets, net of related debt: This component of the net assets consists of capital assets, net of accumulated depreciation and 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 is not included in the calculation of invested net assets, net of related debt. Rather, that portion of the debt is included in the same net asset component of the unspent proceeds.

Restricted: This component of net assets consists of constraints imposed by creditors (such as through debt covenants), grantors, contributors, 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.”

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Concl'd)

K. Estimates

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

NOTE 2 – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Net Assets – At year end, the District reported a deficit in net assets.

<u>Deficit</u>
\$ 310,283

The deficit arose because of operations during the year. Additional revenues received in future fiscal years are expected to eliminate the deficit.

NOTE 3 – CASH AND INVESTMENTS

Custodial Credit Risk – Deposits. Custodial credit risk is the risk that in the event of bank failure the District’s deposits may not be returned to the District. The District does not have a deposit policy for custodial credit risk. At year end, the carrying amount of the District’s deposits was \$521,729 and the bank balance was \$573,706. At year end, \$250,000 of the District’s deposits were covered by Federal depository insurance, \$323,706 were guaranteed under the transaction account guarantee component of the Temporary Liquidity Guarantee Program.

At year end, the District’s investments consisted of the following.

	<u>Average Maturities</u>	<u>Fair Value</u>
County Treasurer’s investment pool	1.66 years	\$ 19,020
Total		<u>\$ 19,020</u>

PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

NOTE 3 – CASH AND INVESTMENTS (Concl'd)

Interest Rate Risk. The District does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk. The District has no investment policy that would further limit its investment choices. As of year end, the District's investment in the County Treasurer's investment pool did not receive a credit quality rating from a national rating agency.

Custodial Credit Risk - Investments. The District's investment in the County Treasurer's investment pool represents a proportionate interest in the pool's portfolio; however, the District's portion is not identified with specific investments and is not subject to custodial credit risk.

NOTE 4 – RECEIVABLES

Accounts receivables are net of an allowance for doubtful accounts of \$12,255 leaving a net accounts receivable balance of \$41,186 at June 30, 2010. The District's receivables primarily consist of amounts due from individuals and businesses in the Town of Pine, Arizona and the Town of Strawberry, Arizona areas and are not subject to liens unless accounts are delinquent.

NOTE 5 – GOODWILL

Goodwill arose during the year as a result of the acquisition of a water utility company on September 30, 2009. The District has elected to amortize the goodwill over a 40 year period.

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010**

NOTE 6 – CAPITAL ASSETS

A summary of capital asset activity for the current fiscal year follows.

<u>Governmental Activities</u>	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$	\$ 91,239	\$	\$ 91,239
Construction in progress		202,061		202,061
Total capital assets, not being depreciated		<u>293,300</u>		<u>293,300</u>
Capital assets, being depreciated:				
Infrastructure		2,183,737		2,183,737
Buildings and improvements		83,705		83,705
Leasehold improvements		5,665		5,665
Vehicles, furniture and equipment		85,247		85,247
Total capital assets being depreciated		<u>2,358,354</u>		<u>2,358,354</u>
Less accumulated depreciation for:				
Infrastructure		(331,486)		(331,486)
Buildings		(10,693)		(10,693)
Leasehold improvements		(1,246)		(1,246)
Vehicles, furniture and equipment		(5,719)		(5,719)
Total accumulated depreciation		<u>(349,144)</u>		<u>(349,144)</u>
Total capital assets, being depreciated, net		<u>2,009,210</u>		<u>2,009,210</u>
Governmental activities capital assets, net	<u>\$</u>	<u>\$ 2,302,510</u>	<u>\$</u>	<u>\$ 2,302,510</u>

Depreciation expense was charged to expense functions as follows.

Administration	\$ 4,963
Operations	344,181
Total depreciation expense	<u>\$ 349,144</u>

Construction Commitments – At year end, the District had contractual commitments related to various capital projects for the construction of Milk Ranch Well. At year end, the District had spent \$202,061 on the projects and had estimated remaining contractual commitments of \$685,000. These projects are being funded with water fees.

NOTE 7 – OPERATING LEASES

The District leases a copier under the provisions of long-term lease agreements classified as operating leases for accounting purposes. Rental expenses under the terms of the operating lease totaled \$7,696 for the year ended June 30, 2010.

**PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010**

NOTE 7 – OPERATING LEASES (Concl'd)

The District has a noncancelable operating lease for the use of office facilities. The lease generally contains a renewal option and requires the District to pay certain executory costs such as taxes, maintenance, and insurance. Rental expense for the lease consisted of \$248 for the year ended June 30, 2010.

NOTE 8 – LINE OF CREDIT

The District has a \$2,250,000 revolving line of credit to provide cash flow during the year to mitigate the impact of timing differences of expenditures and the receipt of water fees and property tax revenues. Water fees and property tax revenues will be used to repay the line of credit. At June 30, 2010, the outstanding balance was \$599,899. The principal for the drawdowns will be repaid on September 30, 2012.

NOTE 9 – NOTES PAYABLE

The District entered into a secured loan agreement in the aggregate sum of \$4,164,000. Interest commenced accruing on November 1, 2009 and is payable on the first of each month until October 1, 2011. On October 1, 2011, monthly payments of the principal balance, together with unpaid interest which has accrued on the outstanding principal balance during the preceding interest period is payable on the first of each month. The fixed interest rate established for the note is 7.80%. The maturity date of the note is September 30, 2012.

Current cash flows are not adequate to cover the balloon payment on September 30, 2012. The District is currently in negotiations with the lending institution to restructure the debt. Additionally, management has changed their fee schedule to pay future debt obligations.

Annual debt service requirements to maturity on notes payable at year end are summarized as follows.

Year Ending June 30:	<u>Principal</u>	<u>Interest</u>
2011	\$	\$ 176,304
2012	86,482	191,461
2013	<u>4,077,518</u>	<u>62,107</u>
Total	<u>\$ 4,164,000</u>	<u>\$ 429,872</u>

PINE-STRAWBERRY WATER IMPROVEMENT DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010

NOTE 10 – CHANGES IN LONG-TERM LIABILITIES

Long-term liability activity for the current fiscal year was as follows.

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental activities:					
Notes payable	\$	\$ 4,164,000	\$	\$ 4,164,000	\$
Line of Credit		599,899		599,899	
Governmental activity long-term liabilities	\$	\$ 4,763,899	\$	\$ 4,763,899	\$

NOTE 11 – DEFERRED CHARGES

The deferred charges relate to the financing charges and other costs for the note payable utilized by the District to acquire the water utility company. The charges are being amortized over the life of the associated debt, which is currently structured as 3 year term. As discussed in further detail in Note 9 the District is in negotiations with their lending institution to renegotiate the terms of their debt arrangement and lengthen the terms to a time frame that is more in line with industry standards. The amortization period for the deferred charges would be revised accordingly should such refinancing occur.

NOTE 12 – RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District carries commercial insurance for all risks of loss, including property and liability, workers' compensation and employee health and accident insurance. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.