

KINNELOA IRRIGATION DISTRICT

FINANCIAL STATEMENTS

**FOR THE YEARS ENDED
DECEMBER 31, 2003 AND 2002**

AND INDEPENDENT AUDITORS' REPORT

KINNELOA IRRIGATION DISTRICT
INDEX TO FINANCIAL STATEMENTS
DECEMBER 31, 2003 AND 2002

	Page
Board of Directors and District Management Personnel	1
Management's Discussion and Analysis	2
Independent Auditors' Report	7
Balance Sheets	8
Statements of Revenues, Expenses and Changes in Net Assets, For the Years Ended December 31, 2003 and 2002	9
Statements of Cash Flows, For the Years Ended December 31, 2003 and 2002	10
Notes to Financial Statements	12
Supplementary Information	21

KINNELOA IRRIGATION DISTRICT
BOARD OF DIRECTORS AND DISTRICT MANAGEMENT PERSONNEL
DECEMBER 31, 2003 AND 2002

BOARD OF DIRECTORS

<u>NAME</u>	<u>OFFICE</u>	<u>TERM EXPIRES</u>
Melvin Matthews	Chairman	2005
Steven Sorell	Treasurer	2007
Jay Stock	Director	2005
Maurice Pickard	Secretary	2007
Robert Brain	Director	2007

MANAGEMENT PERSONNEL

William Redcay	General Manager
Shirley Burt	Administrative Assistant

**KINNELOA IRRIGATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2003 AND 2002**

Our discussion and analysis of the financial performance of KINNELOA IRRIGATION District (the "District") provides an overview of the District's financial activities for the fiscal year ended December 31, 2003. Please read it in conjunction with the District's financial statements, which begin on page 8.

FINANCIAL HIGHLIGHTS

- The District is required to apply the Governmental Accounting Standards Board ("GASB") Statement No. 34, "Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments" ("GASB 34") for periods beginning after June 15, 2002. This new standard has minor impacts upon the financial reporting and accounting performed by the District.
- The District's net assets decreased approximately \$38 thousand, or 1.3 percent, which compared to an increase of \$325 thousand, or nearly 12 percent for the prior fiscal year.
- During the year, the District had operating revenues that were \$16,000 less than last year and operating expenses that were \$140,879 more than last year.
- The District's non-operating revenues decreased by \$272,716, or 9.6 percent, primarily due to a combination of the decrease in other income due to a one-time settlement of an obligation.
- Water usage decreased 1.18% over 2002 due to construction and a rate increase. Water usage was over 721 acre-feet, or .234 billion gallons.

DESCRIPTION OF BASIC FINANCIAL STATEMENTS

The District operates as a utility enterprise and its annual report consists of a series of financial statements presented on the full accrual basis of accounting. The Balance Sheets and the Statements of Revenues, Expenses and Changes in Net Assets (on pages 8 and 9) provide information about the District as a whole and present a longer-term view of the District's finances.

**KINNELOA IRRIGATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2003 AND 2002**

CONDENSED FINANCIAL INFORMATION

The following condensed financial information provides an overview of the District's financial activities for the year ended December 31, 2003 and 2002.

NET ASSETS

	<u>2003</u>	<u>2002</u>
Capital assets, net	\$2,143,120	\$1,990,877
Other assets, net	802,163	1,040,773
Total assets	<u>2,945,283</u>	<u>3,031,650</u>
Long-term liabilities	-	42,243
Other liabilities	92,195	98,480
Total liabilities	<u>92,195</u>	<u>140,723</u>
Invested in capital assets, net of debt	2,143,120	1,990,877
Restricted for debt service	41,600	86,400
Unrestricted	<u>668,368</u>	<u>813,650</u>
Total net assets	<u><u>\$2,853,088</u></u>	<u><u>\$2,890,927</u></u>

Capital and other assets – The change in capital assets is net of an increase of \$280 thousand primarily capital improvement projects, and depreciation expense of \$113 thousand.

Long-term and other liabilities - Long-term liabilities decreased due to principal payments on the District's debt.

Net assets – Unrestricted net assets decreased from the prior year due to the loss from operations.. Unrestricted net assets consist of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt".

**KINNELOA IRRIGATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2003 AND 2002**

CHANGES IN NET ASSETS

	<u>2003</u>	<u>2002</u>
Total operating revenues	\$ 822,712	838,875
Total non-operating revenues	<u>18,351</u>	<u>296,018</u>
Total revenues	841,063	1,134,893
Total operating expenses	870,821	729,942
Total non-operating expenses	<u>8,081</u>	<u>13,032</u>
Total expenses	<u>878,902</u>	<u>742,974</u>
Change in net assets	(37,839)	391,919
Net assets, beginning of year	<u>2,890,927</u>	<u>2,499,008</u>
Net assets, end of year	\$ <u>2,853,088</u>	<u>2,890,927</u>

Revenues – The District's operating revenues consist primarily of water sales. Revenues from water sales decreased by approximately 1.9% as compared to 2002 due to cooler, wetter weather conditions and conservation which was partially offset by a rate increase. For 2003, the main source of the District's non-operating revenues is interest earned on its investments. In 2003 and 2002, the District earned \$13,848 and \$16,311 in interest, respectively. Interest earnings decreased due to lower interest rates earned on the District's investments and a decrease in invested funds.

Expenses – The District's operating expenses increased by \$140,879 due primarily the increased use of outside contractors for preventative maintenance projects and the increased cost of system maintenance supplies and engineering services.

BUDGET ANALYSIS AND VARIANCES

Revenues from water sales for 2003 were \$822,712 which was greater than the budgeted amount of \$786,240. This amount is lower than 2002 due to cooler, wetter weather conditions and conservation partially offset by a rate increase. Operating expenses for 2003 were \$870,921 which was higher than budget due primarily to the increased number of preventative maintenance projects and the related cost of system maintenance supplies and engineering services. However, overall operating surplus exceeded budget by \$30,610 for

**KINNELOA IRRIGATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2003 AND 2002**

BUDGET ANALYSIS AND VARIANCES (continued)

2003 which is a favorable result as compared to budget. Each year the District budgets amounts for capital projects and planned maintenance based on its expected operations and reserves. The aggregate amount of these budgeted expenditures was approximately \$150,000 in the years of 2003 and 2002. The majority of the budgeted improvement funds in 2003 were dedicated to long term planned maintenance expenditures such as the recoating of storage tanks to prevent corrosion and therefore extend the life of these existing assets. In 2002, the majority of the budgeted expenditures were used for capital projects which increased the assets on the District's balance sheet but had only a minimal effect on operating expenses.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets – At December 31, 2003 and 2002, the District had investments in land, buildings, wells and distribution systems, machinery and equipment, and construction in progress as follows).

	2003	2002
Land	\$ 96,700	96,700
Water rights	52,060	52,060
Buildings, wells and distribution system	2,779,012	2,677,971
Machinery and equipment	407,334	373,102
Construction in progress	<u>129,871</u>	<u>-</u>
Totals	<u>\$ 3,464,978</u>	<u>3,199,833</u>

The District's capital improvement for 2004 includes the engineering and construction of a transmission line from one of its wells. The cost of these improvements is budgeted at \$230,000.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

- Inflation as measured by the consumer price index for all urban consumers was 2.3% in 2003 (most recent available data).
- The population growth was zero in 2003 and forecasted to increase 4% in 2004.
- The District has approved 21 new homes to be built by a developer.

These factors are anticipated to have a positive effect on the District's operations. It is anticipated that there will be more construction in the area, which will increase the amount of water sold as well as bringing in additional capital improvement fees for new construction.

KINNELOA IRRIGATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2003 AND 2002

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our purveyors, 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 any questions about this report, or need additional financial information, contact the District's finance office at 1999 Kinclair Dr., Pasadena, CA 91107

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INDEPENDENT AUDITORS' REPORT

The Board of Directors
Kinneloa Irrigation District
Pasadena, California

We have audited the accompanying balance sheets of Kinneloa Irrigation District (the "District") as of December 31, 2003 and 2002, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. 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 audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Kinneloa Irrigation District as of December 31, 2003 and 2002 and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying supplementary information presented on page 21 for the years ended December 31, 2003 and 2002 is presented for purposes of additional analysis and is not required as part of the basic financial statements. Such supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



March 18, 2004

**KINNELOA IRRIGATION DISTRICT
BALANCE SHEETS
DECEMBER 31, 2003 AND 2002**

	<u>2003</u>	<u>2002</u>
ASSETS		
Current assets		
Cash	\$ 67,916	37,582
Temporary investments	611,068	882,748
Receivables		
Water sales, net of allowance for doubtful accounts	63,478	64,730
Other receivables	18,544	19,964
Prepaid expenses	21,157	15,749
Materials and supplies	<u>20,000</u>	<u>20,000</u>
Total current assets	802,163	1,040,773
Capital assets, net of accumulated depreciation	<u>2,143,120</u>	<u>1,990,877</u>
TOTAL ASSETS	<u>\$ 2,945,283</u>	<u>3,031,650</u>
LIABILITIES AND NET ASSETS		
Current liabilities		
Current portion of lease payable	\$ 1,778	5,090
Current portion of bonds payable	40,000	40,000
Accounts payable and accrued expenses	24,731	14,218
Accrued bond interest payable	6,400	6,400
Accrued payroll and payroll taxes	6,799	21,644
Customer deposits	<u>12,487</u>	<u>11,128</u>
Total current liabilities	92,195	98,480
Long-term liabilities		
Bonds payable less current portion	-	40,000
Obligation under capital lease	<u>-</u>	<u>2,243</u>
Total long-term liabilities	<u>-</u>	<u>42,243</u>
Total liabilities	<u>92,195</u>	<u>140,723</u>
Net assets		
Invested in capital assets, net of related debt	2,143,120	1,990,877
Restricted for debt service	41,600	86,400
Unrestricted	<u>668,368</u>	<u>813,650</u>
Total net assets	<u>2,853,088</u>	<u>2,890,927</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 2,945,283</u>	<u>3,031,650</u>

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

**KINNELOA IRRIGATION DISTRICT
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002**

	<u>2003</u>	<u>2002</u>
Operating revenues		
Water sales and service fees	\$ <u>822,712</u>	<u>838,875</u>
Operating expenses		
Operating and maintenance	515,707	394,545
Administration and general	242,214	237,645
Depreciation	<u>112,900</u>	<u>97,752</u>
Total operating expenses	<u>870,821</u>	<u>729,942</u>
Operating loss	<u>(48,109)</u>	<u>108,933</u>
Non-operating revenues (expenses)		
Interest	13,848	16,311
Bond assessments	4,503	29,707
Interest expense	(6,400)	(9,600)
Other income		250,000
Bond administration expenses	<u>(1,681)</u>	<u>(3,432)</u>
Total non-operating revenue	<u>10,270</u>	<u>282,986</u>
Change in net assets	(37,839)	391,919
Net assets, beginning of year	<u>2,890,927</u>	<u>2,499,008</u>
Net assets, end of year	<u>\$ 2,853,088</u>	<u>2,890,927</u>

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

**KINNELOA IRRIGATION DISTRICT
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002**

Cash flows from operating activities:	<u>2003</u>	<u>2002</u>
Cash received from customers	\$ 823,964	863,453
Cash payments to employees for services	(261,005)	(243,619)
Cash payments for services and goods	<u>(491,817)</u>	<u>(369,745)</u>
Net cash provided by operating activities	<u>71,142</u>	<u>250,089</u>
 Cash flows from capital and related financing		
Cash paid for construction and acquisition of capital	(279,981)	(117,421)
Principal paid on debt	(40,000)	(40,000)
Payments on capital lease obligation	(5,556)	(4,523)
Settlement of obligation		250,000
Customer deposits	1,359	(27,291)
Assessments received	4,398	38,308
Bond administrative expenses	(1,681)	(3,432)
Interest and redemption expenses paid	<u>(6,400)</u>	<u>(9,600)</u>
Cash used by capital and related financing activities	<u>(327,861)</u>	<u>86,041</u>
 Cash flows from investing activities:		
Interest received	<u>15,373</u>	<u>15,951</u>
Cash provided by investing activities	<u>15,373</u>	<u>15,951</u>
Net increase in cash and cash equivalents	(241,346)	352,081
Cash and tempory investments, beginning of the year	<u>920,330</u>	<u>568,249</u>
Cash and tempory investments, end of the year	<u>\$ 678,984</u>	<u>920,330</u>
 SUMMARY OF BALANCE SHEET CASH and CASH EQUIVALENTS		
Cash	\$ 67,916	37,582
Temporary investments	<u>611,068</u>	<u>882,748</u>
Total cash	<u>\$ 678,984</u>	<u>920,330</u>

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

**KINNELOA IRRIGATION DISTRICT
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002**

Reconciliation of operating income to net cash	<u>2003</u>	<u>2002</u>
operating activities:		
Operating (loss) income	\$ (48,109)	108,933
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	112,900	97,752
Decrease (increase) in receivables	2,672	35,135
(Increase) decrease in prepaid expenses	8,011	613
Decrease in accounts payable and accrued expenses	<u>(4,332)</u>	<u>7,656</u>
 Net cash provided by operating activities	 <u>\$ 71,142</u>	 <u>250,089</u>

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

KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003 AND 2002

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Kinneloa Irrigation District (the "District") is a special district organized in 1953 under the provisions of Division 11 of the Water Code of the State of California. The District delivers water to the residents in a specific area of Los Angeles County, northeast of the City of Pasadena. This District is not a subdivision of a larger governmental organization.

The District is governed by an elected Board of Directors. At December 31, 2003, The Board of Directors were as follows:

<u>Name</u>	<u>Title</u>
Mr. Melvin Matthews	Chairman
Mr. Steven Sorell	Treasurer
Mr. Maurice Pickard	Secretary
Mr. Robert Brain	Director
Mr. Jay Stock	Director

The Improvement District No. 1 was formed to service the bonded debt. Properties within the Improvement District are assessed \$.80 per \$100 of property value.

The accounting policies of the District conform to generally accepted accounting principles as applicable to governmental enterprise funds. The District applies Governmental Accounting Standards Board ("GASB") pronouncements and Financial Accounting Standards Board ("FASB") pronouncements issued on or before November 30, 1989, unless those pronouncements conflict or contradict GASB pronouncements. The more significant policies reflected in the financial statements are summarized as follows:

a. Fund Accounting

The District's accounts are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a set of self-balancing accounts that comprise its assets, liabilities, retained earnings, revenues and expenses. The District has one fund, which is presented in the accompanying financial statement as a Proprietary Fund category, Enterprise Fund type.

b. Basis of Accounting

The District uses the accrual method of accounting. Revenues are recorded when earned and expenses are recorded when the related liability is incurred. Unbilled receivables are not reflected in the accompanying financial statements because the amounts are not material.

The District is required to apply the Governmental Accounting Standards Board (GASB) Statement No. 34, "Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments" (GASB 34) for periods beginning after June 15, 2002. GASB 34 requires, among other things, that the difference between assets and liabilities be reported as net assets, not equity; that a Management's Discussion and Analysis (MD & A) section precede the

KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003 AND 2002

basic financial statements; that the statements of cash flows use the direct method, and that plant assets be capitalized and depreciated over their useful lives. As the District has historically capitalized its assets and recorded depreciation, the only significant changes made in order to comply with the new requirements were the MD & A section and the reporting of the details of net assets.

In conjunction with the adoption of GASB 34, the District has also adopted the provisions of GASB No 37, "Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments: Omnibus", and GASB No. 38, "Certain Financial Statement Note Disclosures."

c. Utility Plant

Utility plant is stated at cost. The District capitalizes applicable overhead costs in connection with self-constructed assets. Depreciation of all exhaustible utility plant is charged as an expense in the accompanying statements of income. Depreciation is provided over the estimated useful lives of the asset using the straight-line method. Estimated useful lives are as follows:

Water system	5 to 50 years
Autos and trucks	3 to 5 years
Office equipment	5 to 10 years
Office and production facilities	10 to 40 years

d. Restricted Assets and Liabilities

Tax assessments received by the District from customers located in Improvement District No. 1 are restricted assets for the purpose of repaying general obligation serial bonds.

e. Uncollectible Accounts

The District's management estimates that accounts receivable are collectible. However, an allowance for uncollectible accounts at December 31, 2003 and 2002 is \$988, respectively. Unpaid water accounts receivable become a lien on the property and must be paid upon the sale of the property.

f. Cash and Cash Equivalents

The District defines cash and cash equivalents as demand account balances and cash on hand.

The District invests cash in excess of its operating requirements primarily with the State Treasurer's Local Agency Investment Fund (LAIF).

KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003 AND 2002

g. Investments

All investments are stated at fair value as required by GASB Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools". Fair value is based on market price or contract amount.

h. Materials and Supplies

Materials and supplies are stated at cost and consist of expendable supplies held for consumption or future additions to Utility Plant.

i. Concentration of Credit Risk

The District's receivables are from consumers within a specific geographic area.

j. Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

k. Budgetary Process

Each year, the District adopts a budget which provides for its general operations. Budgets are prepared on the accrual basis of accounting. The District follows these procedures in establishing the budget for the fiscal year:

i. Formal budgetary integration is employed as a management control device during the year for the General Activity.

ii. The Board approves the total budget for the year for the General Activity. The Board is authorized to make any budget adjustments during the year.

iii. Unused appropriations lapse at the end of the year unless extended into the subsequent year by a vote of the Board of Directors.

l. Income Taxes

The District is exempt from income taxes under provisions of the Internal Revenue Code and related California statutes; accordingly, no provision for income taxes is required.

m. Compensated Absences

It is the District's policy to permit employees to accumulated paid time off for either vacation or illness in accordance with the terms expressed in its employee handbook. Upon termination, retirement or death of an employee, the District pays eligible accrued time in a lump-sum payment

KINNELOA IRRIGATION DISTRICT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2003 AND 2002

to the employee or beneficiary. Accumulated paid time off is recorded as an expense and a liability at the time the benefit is earned.

NOTE 2. Cash Deposits and investments

The District is permitted by State law and Board policy to invest in obligations deemed prudent. Such investments include interest bearing savings accounts, collateralized certificates of deposit, direct obligations of the United States Government and various federal agencies, approved money market funds and investment agreements, and various other approved investments. As mandated by state law, the District annually adopts its investment policy that defines allowable investments, restrictions on investment concentrations and maximum maturity periods, and other specific investment-related policies. The District has contracted with an investment advisor and given him authorization to make trades on the District's behalf, following the above guidelines. Currently, a majority of the District's cash deposits and investments are held at a single financial institution.

The District's cash deposits at December 31, 2003 were entirely covered by Federal depository insurance or by pledged collateral pools of either U.S. Government securities or mortgages. California Government Code requires California banks and savings and loan associations to secure a local agency's deposits by pledging 110% of government securities as collateral. California law also allows financial institutions to secure local agency deposits by pledging first trust deed mortgage notes having a value of 150% of a local agency's total deposits. Such collateral, however, is not held specifically in the name of the District.

Investments of governmental agencies, in accordance with GASB No. 3, are classified in three categories to give an indication of the level of custodial risk assumed by the entity. Category 1 consists of investments that are insured or collateralized with securities held by the District or its agent in the District's name. Category 2 includes investments collateralized with securities held by the pledging institution's trust department or by its agent in the District's name. Category 3 consists of investments collateralized with securities held by the pledging institution, or by its trust department or agent, but not in the District's name.

	2003			Total
	Category			
	1	2	3	
Pooled cash	\$ 611,068			611,068
Interest bearing				
Demand accounts	67,916	-		67,916
US Treasury securities				
Federal agency securities	-	-	-	-
	-	-	-	-
Total cash and investments	\$ 678,984	0	0	678,984

KINNELOA IRRIGATION DISTRICT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2003 AND 2002

NOTE 2. Cash Deposits and investments, continued

	2002			Total
	Category			
	1	2	3	
Pooled cash	\$ 882,747			882,747
Interest bearing Demand accounts	37,582	-		37,582
US Treasury securities Federal agency securities	-	-	-	-
Total cash and investments	\$ <u>920,329</u>	<u>0</u>	<u>0</u>	<u>920,329</u>

NOTE 3. Capital Assets

Capital asset activity for the years ended December 31, 2003 and 2002 was as follows:

	2003			Balance December 31
	Balance January 01	Additions	Transfers	
Land	\$ 96,700	-	-	96,700
Water rights	52,060	-	-	52,060
Buildings, wells and distribution system	2,677,971	101,041	-	2,779,012
Machinery and equipment	373,102	34,232	-	407,334
Construction in progress	-	129,871	-	129,871
	3,199,833	265,144	-	3,464,978
Less accumulated	(1,208,956)	112,902	-	(1,321,858)
Total capital assets	\$ <u>1,990,877</u>	<u>378,046</u>	<u>-</u>	<u>2,143,120</u>

KINNELOA IRRIGATION DISTRICT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2003 AND 2002

NOTE 3. Capital Assets, continued

2002				
	Balance January 01	Additions	Transfers	Balance December 31
Land	\$ 96,700	-	-	96,700
Water rights	52,060	-	-	52,060
Buildings, wells and distribution system	2,212,988	65,730	399,253	2,677,971
Machinery and equipment	321,412	51,690	-	373,102
Construction in progress	399,253		(399,253)	-
	3,082,413	117,420	-	3,199,833
Less accumulated	(1,111,205)	97,751	-	(1,208,956)
Total capital assets	\$ 1,971,208	19,669	-	1,990,877

Note 4 - Bonds Payable

The District issued \$600,000 of general obligation serial bonds in February 1975 to provide funds for the purchase and upgrade of Improvement District Number 1. The bonds bear interest at 8% per annum, payable semi-annually on January 1 and July 1. The bonds mature serially until July 1, 2004, in annual amounts.

Debt service at December 31, 2003 is as follows:

Year Ending December 31,	Bond Principal Due July 1	Bond Interest Due	Total Debt Service
2004	\$40,000	\$1,600	\$41,600

The bonds are repaid through tax assessments made on the land included in the Improvement District No. 1 in sufficient amounts, annually, to pay the interest and bond principal maturities during the year including a cash reserve.

KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003 AND 2002

Note 5 - Obligation Under Capital Lease

On June 1, 1999, the District entered into a capital lease for a 1999 Ford truck. Payments of \$506.39 are due monthly. The lease provides for a purchase option at termination. Payments on the obligation are \$1,778 during the year December 31, 2004.

Note 6 - Pension Plan

Plan Description

The District contributes to the State of California Public Employees Retirement System ("PERS"), an agent multi-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 statute and city ordinance. Copies of PERS' annual financial report may be obtained from their offices located at 400 P Street, Sacramento, CA 95814.

All full time employees are eligible to participate as members of PERS. Benefits vest after five years of service. District employees are eligible to retire upon attaining age 50. Annual retirement benefits are determined based upon the age at retirement, the length of membership service and the amount of earnings based upon the highest twelve consecutive months average.

Funding Policy

For the years ended December 31, 2002 and 2001, participants were required to contribute 7 % of their annual covered salary. For an exempt employee, the District contributed the amount as an employee benefit. The District is required to contribute at an actuarially determined rate; the rate was zero at December 31, 2002 and 2001. The contribution requirements of plan members and the District are established and may be amended by PERS.

Annual Pension Cost

Annual pension cost was zero for the years ended December 31, 2002 and 2001. The District made no employer contributions during the years ended December 31, 2002 and 2001. The District does not have a Net Pension Obligation.

Actuarial Assumptions and Methods

The actuarial valuation is computed using the entry age normal actuarial cost method. The actuarial assumptions include: (a) an investment rate of return of 8.25% compounded annually (b) projected annual salary increases that vary by duration of service, and (c) payroll cost-of-living adjustments of 3.75%. The rates used in (a) and (b) are compounded annually at 3.5%. The actuarial value of PERS assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a three-year period. Initial unfunded liabilities

**KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003 AND 2002**

are amortized over a specific period that depends upon the plan's date of entry into PERS. Subsequent plan amendments are amortized as a level percentage of projected payroll over a closed 20-year period. The District does not have an unfunded liability.

The following presents a short history of the funded status of the plan, covered payroll and related actuarial information:

Actuarial Valuation Date	(A) Entry Age Normal Accrued Liability	(B) Actuarial Value of Assets	(A) - (B) Unfunded Liability or (Excess Assets)	(B)/(A) Funded Status	(C) Annual Covered Payroll	[(A) - (B)]/(C) Unfunded Actuarial Liability as a % of Covered Payroll
6/30/98	\$281,636	\$405,691	\$(124,055)	144.0%	\$125,190	(99.093)%
6/30/99	330,276	450,047	(119,771)	136.3%	129,759	(92.303)%
6/30/00	355,223	493,286	(138,063)	138.9%	135,623	(101.799)%
06/30/01	369,707	504,368	(134,661)	136.4%	144,579	(93.140)%

NOTE 7. Insurance Pools

The District is a member of the Joint Powers Insurance Authority ("JPIA"), which pools together members of the Association of California Water Agencies for the purpose of paying group property, general liability and dam insurance claims. Premiums are remitted directly to the JPIA by its members. The property portion is entirely self-funded, and the general liability self-funded portion is capped at \$500,000. Excess liability insurance in the amount of \$29,500,000 has been purchased by the Authority, bringing the total liability coverage to \$30,000,000.

To date, the District and its counsel are not aware of any material claims incurred through the period ended December 31, 2003 regarding these insurance plans.

Note 8 - Agreement for Construction of Water System Improvement

In connection with an agreement to construct and maintain a portion of the water system, a developer paid \$250,000 as security for the maintenance of the water quality at the District's Eucalyptus Tunnel. During the year ended December 31, 2002, the developer was released from the obligation to maintain the water quality in exchange for the amount deposited. The District recognized this amount as other income in the accompanying statement of income.

KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2003 AND 2002

NOTE 9. Net Assets

GASB 34 requires that the difference between assets and liabilities be reported as net assets, not equity. Net assets are classified as either restricted, unrestricted or invested in capital assets, net of debt.

Net assets that are invested in capital assets, net of debt consist of capital assets, net of accumulated depreciation and amortization, and reduced by the outstanding balances of any bonds, notes or other borrowings attributable to the acquisition or construction of those assets.

Restricted net assets are those net assets that have external constraints placed on them by creditors, grantors, contributors, or laws or regulations of other governments, or imposed by law through constitutional provisions of enabling legislation.

Unrestricted net assets consist of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of debt." Unlike the restricted net assets, the Board has discretion in determining the use and establishing minimum/maximum balance requirements for the unrestricted cash and investment portion of net assets. The Board may at any time change or eliminate amounts established for these purposes.

NOTE 10 - Contingencies

The District is the subject of certain claims and assessment arising in the normal course of its operations. These include a proposed assessment by the California Regional Water Quality Control Board relating to certain environmental matters which the District vigorously opposes. Management of the District does not believe that the resolution of these matters will have a material adverse affect on the District's financial condition.

SUPPLEMENTARY INFORMATION

KINNELOA IRRIGATION DISTRICT
 SCHEDULE OF OPERATING EXPENSES
 FOR THE YEARS ENDED DECEMBER 31, 2003 AND 2002

	<u>2003</u>	<u>2002</u>
Operating & Maintenance		
Power	\$ 100,410	111,062
Emergency water	552	4,054
Labor	112,683	129,587
Engineering	32,868	7,506
Maintenance supplies	50,217	23,120
Signal service	3,069	4,618
Water analysis	17,356	14,389
Outside contractors	131,797	30,679
Truck maintenance	13,301	11,690
Equipment rental	1,697	1,606
Insurance	46,521	46,311
Safety equipment	-	5,540
Other	5,236	4,383
	<u>515,707</u>	<u>394,545</u>
	\$	

Administrative and General		
Administrative salaries	\$ 72,778	79,249
Office labor	38,330	35,543
Payroll taxes	20,203	19,260
CalPERS retirement	4,956	4,686
Outside services	18,828	24,366
Legal fees	24,187	8,689
Professional dues	3,746	3,972
Board meetings	2,621	685
Office expense	30,309	38,265
Telephone	11,906	11,677
Accounting fees	4,900	5,800
Permits and operational fees	0	4,465
Information systems	9,450	
Uncollectible accounts	-	988
	<u>242,214</u>	<u>237,645</u>
	\$	