



Phelan Piñon Hills Community Services District
Annual Financial Report
For the Year Ended June 30, 2009



PHELAN PIÑON HILLS COMMUNITY SERVICES DISTRICT

List of Elected and Appointed Officials

June 30, 2009

Elected Officials

BOARD OF DIRECTORS

<u>Title</u>	<u>Director</u>	<u>Term Expires</u>
President	Al Morrisette	December 2013
Vice-President	Ken Anderson	December 2011
Director	Joe Fahlender	December 2011
Director	Charlie Johnson	December 2013
Director	Mark Roberts	December 2013

Appointed Official

General Manager Don Bartz

**Phelan Piñon Hills Community Services District
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Phelan, California 92371
(760) 868-1212 www.pphcsd.org**



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For the Year Ended June 30, 2009

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Financial Section



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Independent Auditor's Report

Board of Directors
Phelan Piñon Hills Community Services District
Phelan, California

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the Phelan Piñon Hills Community Services District (District) as of and for the year ended June 30, 2009, which collectively comprise the District's basic financial statements as listed in the table of contents. These basic financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these basic 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 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 respective financial position of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the Phelan Piñon Hills Community Services District as of June 30, 2009, and the respective changes in net assets and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 20, 2009 on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, 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 read in conjunction with this report in considering the results of our audit.

The District has not presented the *Management's Discussion and Analysis* that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be a part of, the basic financial statements because this is the District's first fiscal year in operation. See Note 1 - Organization and Operations of the Reporting Entity for further information.

October 20, 2009
Cypress, California

Charles Z. Fedak, CPA
An Accountancy Corporation

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Basic Financial Statements

Phelan Piñon Hills Community Services District
Statement of Net Assets
June 30, 2009

<i>Assets</i>	Governmental Activities	Business-type Activities	Total
Current assets:			
Cash and cash equivalents (note 2)	\$ 1,420,954	13,938,962	15,359,916
Accrued interest receivable	7,192	40,757	47,949
Accounts receivable – water sales and services	-	729,913	729,913
Accounts receivable – other	-	2,800	2,800
Property taxes and assessments receivable	160,190	-	160,190
Materials and supplies inventory	-	72,432	72,432
Prepaid expenses and other assets	-	27,348	27,348
Total current assets	<u>1,588,336</u>	<u>14,812,212</u>	<u>16,400,548</u>
Non-current assets:			
Capital assets – not being depreciated (note 3)	54,453	869,252	923,705
Capital assets – being depreciated, net (note 3)	897,060	18,339,586	19,236,646
Total non-current assets	<u>951,513</u>	<u>19,208,838</u>	<u>20,160,351</u>
Total assets	<u>2,539,849</u>	<u>34,021,050</u>	<u>36,560,899</u>
<i>Liabilities and Net Assets</i>			
Current liabilities:			
Accounts payable and accrued expenses	47,484	644,747	692,231
Accrued salaries and related payables	-	171,507	171,507
Customer deposits and deferred revenue	-	72,382	72,382
Accrued interest on long-term debt	-	52,023	52,023
Long-term liabilities – due within one year:			
Compensated absences	-	11,309	11,309
Long-term debt (note 4)	-	100,040	100,040
Total current liabilities	<u>47,484</u>	<u>1,052,008</u>	<u>1,099,492</u>
Non-current liabilities:			
Long-term liabilities – due in more than one year:			
Compensated absences	-	33,928	33,928
Long-term debt (note 4)	-	2,913,976	2,913,976
Total non-current liabilities	<u>-</u>	<u>2,947,904</u>	<u>2,947,904</u>
Total liabilities	<u>47,484</u>	<u>3,999,912</u>	<u>4,047,396</u>
Net assets:			
Net investment in capital assets (note 5)	951,513	16,194,822	17,146,335
Unrestricted (note 6)	1,540,852	13,826,316	15,367,168
Total net assets	<u>\$ 2,492,365</u>	<u>30,021,138</u>	<u>32,513,503</u>

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Statement of Activities
For the Year Ended June 30, 2009

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenues</u>		<u>Net (Expense) Revenue and Changes in Net Assets</u>		
		<u>Charges for Services</u>	<u>Capital Grants and Contributions</u>	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Total</u>
Governmental activities:						
Parks and recreation	\$ 191,489	19,109	-	(172,380)	-	(172,380)
Street lighting	16,753	-	-	(16,753)	-	(16,753)
Total governmental	<u>208,242</u>	<u>19,109</u>	<u>-</u>	<u>(189,133)</u>	<u>-</u>	<u>(189,133)</u>
Business-type activities:						
Water	<u>5,864,190</u>	<u>4,732,889</u>	<u>80,698</u>	<u>-</u>	<u>(1,050,603)</u>	<u>(1,050,603)</u>
Total business-type	<u>5,864,190</u>	<u>4,732,889</u>	<u>80,698</u>	<u>-</u>	<u>(1,050,603)</u>	<u>(1,050,603)</u>
Total	<u>\$ 6,072,432</u>	<u>4,751,998</u>	<u>80,698</u>	<u>(189,133)</u>	<u>(1,050,603)</u>	<u>(1,239,736)</u>
		General revenues:				
		Property taxes		\$ 1,373,294	-	1,373,294
		Interest earnings		9,390	455,757	465,147
		Other		85,300	390,367	475,667
		Transfers		-	-	-
		Total general revenues		<u>1,467,984</u>	<u>846,124</u>	<u>2,314,108</u>
		Change in net assets		<u>1,278,851</u>	<u>(204,479)</u>	<u>1,074,372</u>
		Net assets, beginning of year		<u>1,213,514</u>	<u>30,225,617</u>	<u>31,439,131</u>
		Net assets, end of year		<u>\$ 2,492,365</u>	<u>30,021,138</u>	<u>32,513,503</u>

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Balance Sheets – Governmental Funds
June 30, 2009

	Parks and Recreation	Street Lighting	Total Governmental Activities
Assets:			
Cash and cash equivalents	\$ 1,420,954	-	1,420,954
Accrued interest receivable	7,192	-	7,192
Property taxes and assessments receivable	160,190	-	160,190
Total assets	1,588,336	-	1,588,336
Liabilities:			
Accounts payable and accrued expenses	47,484	-	47,484
Total liabilities	47,484	-	47,484
Fund balance:			
Reserved for parks and recreation	1,540,852	-	1,540,852
Reserved for street lighting	-	-	-
Total fund balance	1,540,852	-	1,540,852
Total liabilities and fund balance	\$ 1,588,336	-	1,588,336

Phelan Piñon Hills Community Services District
Reconciliation of the Balance Sheets of Governmental Funds to the Statement of Net Assets
June 30, 2009

Reconciliation:

Fund balance of governmental funds	\$ 1,540,852
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Amounts reported for governmental activities in the statement of net assets is different because:

Capital assets used in governmental activities are not current financial resources and, therefore, are not reported in the governmental funds balance sheet. However, the statement of net assets includes those capital assets among the assets of the District as a whole.

951,513

Net assets of governmental activities	\$ <u><u>2,492,365</u></u>
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See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Statements of Revenues, Expenditures and Changes in Fund Balances– Governmental Funds
For the Year Ended June 30, 2009

	Parks and Recreation	Street Lighting	Total Governmental Activities
Revenues:			
Property taxes	\$ 1,373,294	-	1,373,294
Charges for services	19,109	-	19,109
Interest earnings	9,390	-	9,390
Other	85,300	-	85,300
Total revenues	1,487,093	-	1,487,093
Expenditures:			
Parks and recreation	138,427	-	138,427
Street lighting	-	16,753	16,753
Capital outlay	18,083	-	18,083
Total expenditures	156,510	16,753	173,263
Net income(loss)	1,330,583	(16,753)	1,313,830
Other financing sources(uses):			
Transfers in(out)	(16,753)	16,753	-
Total other financing sources	(16,753)	16,753	-
Change in fund balance	1,313,830	-	1,313,830
Fund balance, beginning of year	227,022	-	227,022
Fund balance, end of year	\$ 1,540,852	-	1,540,852

Phelan Piñon Hills Community Services District
Reconciliation of the Statements of Revenues, Expenditures and Changes in Fund Balance of
Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2009

Reconciliation:

Net changes in fund balance of total governmental funds	\$	1,313,830
<p style="margin-left: 20px;">Amounts reported for governmental activities in the statement of activities are different because:</p> <p style="margin-left: 40px;">Governmental funds report capital outlay as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense as follows:</p>		
Capital outlay		18,083
Depreciation expense		(53,062)
		18,083
		(53,062)
Change in net assets of governmental activities	\$	1,278,851

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Statements of Net Assets – Enterprise Funds
June 30, 2009

<i>Assets</i>	Water Enterprise
Current assets:	
Cash and cash equivalents	\$ 13,938,962
Accrued interest receivable	40,757
Accounts receivable – utilities, net	729,913
Accounts receivable – other	2,800
Materials and supplies inventory	72,432
Prepaid expenses and other assets	27,348
Total current assets	14,812,212
Non-current assets:	
Capital assets – not being depreciated	869,252
Capital assets – being depreciated, net	18,339,586
Total non-current assets	19,208,838
Total assets	34,021,050
<i>Liabilities and Net Assets</i>	
Current liabilities:	
Accounts payable and accrued expenses	644,747
Accrued salaries and related payables	171,507
Customer deposits and deferred revenue	72,382
Accrued interest on long-term debt	52,023
Long-term liabilities – due within one year:	
Compensated absences	11,309
Long-term debt	100,040
Total current liabilities	1,052,008
Non-current liabilities:	
Long-term liabilities – due in more than one year:	
Compensated absences	33,928
Long-term debt	2,913,976
Total non-current liabilities	2,947,904
Total liabilities	3,999,912
Net assets:	
Net investment in capital assets	16,194,822
Unrestricted	13,826,316
Total net assets	\$ 30,021,138

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Statements of Revenues, Expenses and Changes in Fund Net Assets – Enterprise Funds
For the Year Ended June 30, 2009

	Water Enterprise
Operating revenues:	
Water consumption sales	\$ 2,816,459
Monthly meter service charge	1,532,468
Special assessment	283,142
Other charges and services	100,820
Total operating revenues	4,732,889
Operating expenses:	
Source of supply – water related purchases	312,250
Pumping – utilities	1,050,477
Transmission and distribution	2,441,278
General and administrative	1,032,711
Total operating expenses	4,836,716
Operating loss before depreciation	(103,827)
Depreciation	(886,786)
Operating loss	(990,613)
Non-operating revenues(expenses):	
Interest earnings	455,757
Interest expense – long-term debt	(130,057)
Other non-operating revenues	390,367
Other non-operating expenses	(10,631)
Total non-operating revenues, net	705,436
Net loss before capital contributions	(285,177)
Capital contributions:	
Connection fees	80,698
Capital contributions	80,698
Other financing sources:	
Transfers in(out):	-
Total other financing sources	-
Change in net assets	(204,479)
Net assets, beginning of year	30,225,617
Net assets, end of year	\$ 30,021,138

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Statements of Cash Flows – Enterprise Funds
For the Year Ended June 30, 2009

	<u>Water</u> <u>Enterprise</u>
Cash flows from operating activities:	
Cash receipts from customers	\$ 4,000,176
Cash paid to vendors and suppliers	<u>(4,002,623)</u>
Net cash used in operating activities	<u>(2,447)</u>
Cash flows from non-capital financing activities:	
Other non-operating revenues	390,367
Other non-operating expenses	<u>(10,631)</u>
Net cash provided by non-capital financing activities	<u>379,736</u>
Cash flows from capital and related financing activities:	
Acquisition and construction of capital assets	(2,919,523)
Proceeds from capital contributions	80,698
Principal payments on long-term debt	(96,648)
Interest payments on long-term debt	<u>(78,034)</u>
Net cash used in capital and financing activities	<u>(3,013,507)</u>
Cash flows from investing activities:	
Purchases and sales of investments, net	(1,152,000)
Interest earnings	<u>415,000</u>
Net cash used in investing activities	<u>(737,000)</u>
Net decrease in cash	(3,752,954)
Cash and cash equivalents, beginning of year	<u>17,691,916</u>
Cash and cash equivalents, end of year	\$ <u><u>13,938,962</u></u>
Reconciliation of operating loss to net cash used in operating activities:	
Operating loss	<u>(990,613)</u>
Adjustments to reconcile operating loss to net cash used in operating activities:	
Depreciation expense	886,786
Changes in assets and liabilities:	
(Increase)decrease in assets:	
Accounts receivable – water sales and services	(729,913)
Accounts receivable – other	(2,800)
Materials and supplies inventory	(72,432)
Prepaid expenses and other assets	(27,348)
Increase(decrease) in liabilities:	
Accounts payable and accrued expenses	644,747
Accrued salaries and related payables	171,507
Customer deposits and deferred revenue	72,382
Compensated absences	<u>45,237</u>
Total adjustments	<u>988,166</u>
Net used in operating activities	\$ <u><u>(2,447)</u></u>

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(1) Reporting Entity and Summary of Significant Accounting Policies

A. Organization and Operations of the Reporting Entity

The Phelan Piñon Hills Community Service District (District) was established through an election on February 5, 2008. With an 81% approval rating, the voters approved the formation of the District as a consolidation of three San Bernardino County Special District Service Areas of: Zone-L70 Water, CSA-9 Phelan Parks and Street Lighting and CSA56-F1 Piñon Hills Parks. The San Bernardino County Special District Service Areas named above transferred \$31,439,131 in net assets to form the District.

This consolidation enabled the communities of Phelan and Piñon Hills to establish a form of self-governance while maintaining their individual rural integrity. The 128 square mile District is the largest Community Service District in San Bernardino County.

The primary component of the District is water service to the approximately 6,700 customers. Parks and recreation are a vital component to any community. As part of the District there are two community centers. These centers are utilized for a wide range of activities and are available to the community for a nominal fee. Adjacent to the centers are two parks that have picnic tables and playgrounds. They are available from morning until dusk. The street lights serve primarily the business district of Phelan. The street lights are not owned by the District, but the District pays for the electricity use costs for the street lights.

The District normally conducts two monthly general meetings of the Board of Directors which are held on the first and third Wednesdays of the month in the Phelan Community Center.

The criteria used in determining the scope of the financial reporting entity is based on the provisions of Governmental Accounting Statements No. 14, *The Financial Reporting Entity*, and No. 39, *Determining Whether Certain Organizations Are Component Units* (an amendment of No. 14). The District is the primary governmental unit based on the foundation of a separately elected governing board that is elected by the citizens in a general election. Component units are legally separate organizations for which the elected officials of the primary government are financially accountable. The District is financially accountable if it appoints a voting majority of the organization's governing body and: 1) It is able to impose its will on that organization, or 2) There is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary government. The District has no blended or discretely-presented component units.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

B. Basis of Accounting and Measurement Focus

The *basic financial statements* of the District are composed of the following:

- Government-wide financial statements
- Fund financial statements
- Notes to the basic financial statements

Government-wide Financial Statements

These statements are presented on an *economic resources* measurement focus and the accrual basis of accounting for both governmental and business-like activities. Accordingly, all of the District's assets and liabilities, including capital assets, are included in the accompanying Statement of Net Assets. The Statement of Activities presents changes in net assets. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used, such as, unbilled but utilized utility services are recorded at year end. The Statement of Activities demonstrates the degree to which the operating expenses of a given function are offset by operating revenues. Operating expenses are those that are clearly identifiable with a specific function. The types of transactions reported as operating revenues for the District are charges for services directly related to the operations of the District. Charges for services include revenues from customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by the District. Taxes, operating grants and other items not properly included among operating revenues are reported instead as non-operating revenues. Contributed capital and capital grants are included as capital contributions.

Fund Financial Statements

These statements include a Balance Sheet and a Statement of Revenues, Expenditures and Changes in Fund Balances for all major governmental funds. Accompanying these statements is a schedule to reconcile and explain the differences in fund balances as presented in these statements to the net assets presented in the Government-wide Financial Statements.

Governmental funds are accounted for on a spending or *current financial resources* measurement focus and the modified accrual basis of accounting. Accordingly, only current assets and liabilities are included on the Balance Sheet. The Statement of Revenues, Expenditures and Changes in Fund Balances present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets. Under modified accrual basis of accounting, revenues are recognized in the accounting period in which they become measurable and available to finance expenditures of the current period. Accordingly, revenues are recorded when received in cash, except that revenues subject to accrual (generally 60-days after year-end) are recognized when due. The primary sources susceptible to accrual for the District are property tax, interest earnings, investment revenue and operating and capital grant revenues. Expenditures are generally recognized under the modified accrual basis of accounting when the related fund liability is incurred. However, exceptions to this rule include principal and interest on debt, which are recognized when due.

The accrual basis of accounting is followed by the proprietary enterprise funds. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used, such as, unbilled but utilized utility services are recorded at year end.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred, regardless of when the related cash flows take place. Operating revenues and expenses, such as water sales and purchases of water, result from exchange transactions associated with the principal activity of the District. Exchange transactions are those in which each party receives and gives up essentially equal values. Management, administration and depreciation expenses are also considered operating expenses. Other revenues and expenses not included in the above categories, such as interest income and interest expense, are reported as non-operating revenues and expenses.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(1) Reporting Entity and Summary of Significant Accounting Policies, continued

B. Basis of Accounting and Measurement Focus, continued

Private sector standards of accounting and financial reporting issued prior to December 1, 1989, are generally followed in both the government-wide and propriety 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.

The accounts of the District are organized on the basis of funds, each of which is considered a separate accounting entity with a self-balancing set of accounts established for the purpose of carrying out specific activities or attaining certain objectives in accordance with specific regulations, restrictions or limitations.

Funds are organized into two major categories: governmental and proprietary categories. An emphasis is placed on major funds within the governmental and proprietary categories. A fund is considered major if it is the primary operation fund of the District or meets the following criteria:

- a) Total assets, liabilities, revenues, or expenditures/expenses of that individual governmental or proprietary fund are at least 10 percent of the corresponding total for all funds of that category or type; and
- b) Total assets, liabilities, revenues, or expenditures/expenses of the individual governmental fund or proprietary fund are at least 5 percent of the corresponding total for all governmental and proprietary funds combined.
- c) The entity has determined that a fund is important to the financial statement user.

The funds of the financial reporting entity are described below:

Governmental Funds

Parks and Recreation – This fund is used to account for all parks and recreation activities within the District.

Street Lighting – This fund is used to account for all street lighting activities within the District.

Enterprise Funds

Water – This fund accounts for the water transmission and distribution operations of the District.

C. Financial Statement Elements

1. Cash and Cash Equivalents

Substantially all of the District's cash is invested in interest bearing accounts. The District considers all highly liquid investments with a maturity of three months or less to be cash equivalents.

2. Accounts Receivable – Water Sales and Services

The District extends credit to customers in the normal course of operations. Management reviews all accounts receivable as collectible.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(1) Reporting Entity and Summary of Significant Accounting Policies, continued

C. Financial Statement Elements, continued

3. Property Taxes and Assessments

The San Bernardino County Assessor's Office assesses all real and personal property within the County each year. The San Bernardino County Tax Collector's Office bills and collects the District's share of property taxes and/or tax assessments. The San Bernardino County Treasurer's Office remits current and delinquent property tax collections to the District throughout the year. Property tax in California is levied in accordance with Article 13A of the State Constitution at one percent (1%) of countywide assessed valuations.

Property taxes and assessments receivable at year-end are related to property taxes and special assessments collected by the San Bernardino County, which have not been credited to the District's cash balance as of June 30. The property tax calendar is as follows:

Lien date	March 1
Levy date	July 1
Due dates	November 1 and February 1
Collection dates	December 10 and April 10

4. Materials and Supplies Inventory

Materials and supplies inventory consists primarily of water meters, pipe and pipe fittings for construction and repair to the District's water transmission and distribution system. Inventory is valued at cost using a weighted average method. Inventory items are charged to expense at the time that individual items are withdrawn from inventory or consumed.

5. Prepaid Expenses

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

6. Capital Assets

Capital assets acquired and/or constructed are capitalized at historical cost. District policy has set the capitalization threshold for reporting capital assets at \$5,000. Donated assets are recorded at estimated fair market value at the date of donation and/or historical cost. Upon retirement or other disposition of capital assets, the cost and related accumulated depreciation are removed from the respective balances and any gains or losses are recognized. Depreciation is recorded on a straight-line basis over the estimated useful lives of the assets as follows:

Governmental Activities

- Infrastructure, street lighting – 30 to 40 years
- Vehicles and equipment – 5 to 10 years

Business-Type Activities

- Facility and systems – 10 to 40 years
- Vehicles and equipment – 5 to 10 years

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(1) Reporting Entity and Summary of Significant Accounting Policies, continued

C. Financial Statement Elements, continued

7. Net Assets/Fund Balances

The government-wide financial statements utilize a net assets presentation. Net assets categories are as follows:

- **Net Investment in Capital Assets** – This component of net assets consists of capital assets, net of accumulated depreciation and reduced by any outstanding debt against the acquisition, construction or improvement of those assets.
- **Restricted Net Assets** – This component of net assets consists of net assets that are restricted for a specific use and are not available for the general use of the District.
- **Unrestricted Net Assets** – This component of net assets consists of net assets that do not meet the definition of *restricted* or *net investment in capital assets*.

In the fund financial statements, reserves and designations segregate portions of fund balances that are either not available or have been earmarked for specific purposes. Reservations and designations of fund balance are described below:

- **Reserved** – Some of the assets reported in governmental funds are not available for spending in the subsequent year's budget. Fund balance also is reserved to indicate situations where a position of fund balance is not available for spending on any and all purposes of the fund.
- **Unreserved Designated** – Designations essentially reflect a government's self imposed limitations on the use of otherwise available current financial resources.

8. Water Sales and Services

Water sales are billed on a bi-monthly basis. Estimated unbilled water revenue through June 30 has been accrued at year-end for the enterprise funds.

9. Capital Contributions

Capital contributions represent cash and capital asset additions contributed to the District by property owners, granting agencies or real estate developers desiring services that require capital connection expenditures or capacity commitment.

10. Use of Estimates

The preparation of the basic 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 disclosures of contingent assets and liabilities at the date of the financial statements and the reported changes in net assets during the reporting period. Actual results could differ from those estimates.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(2) Cash and Cash Equivalents

Cash and cash equivalents consist of the following:

	2009
Cash on hand	\$ 1,300
Deposits held with financial institutions	548,802
Certificate-of-deposit due January 2010	1,152,060
Deposits held with California Local Agency Investment Fund (LAIF)	13,657,754
Total	\$ 15,359,916

As of June 30, the District's authorized deposits had the following maturities:

Deposits held with California Local Agency Investment Fund (LAIF)	235 days
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Authorized Deposits and Investments

The District's investment policy authorizes investments in Certificates-of-deposit and the California Local Agency Investment Fund (LAIF). The District's investment policy does contain specific provisions intended to limit its exposure to interest rate risk, credit risk, custodial risk, and concentration of credit risk.

Local Agency Investment Fund

The District is a voluntary participant in the California Local Agency Investment Fund (LAIF) that is regulated by California Code Section 16429 under oversight of the Treasurer of the State of California. Each agency in the fund may invest up to \$40 million and may invest without limitation in special bond proceeds accounts. Amounts held with LAIF are highly liquid, as deposits can be converted to cash within a twenty-four hour period without loss of accrued interest. Credit and market risk is unknown.

Custodial Credit Risk

Custodial credit risk for *deposits* is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The California Government Code and the District's investment policy does not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. The District had deposits with a bank balance of \$650,510 as of June 30, 2009 that are FDIC insured up to \$250,000. The bank balances of \$650,510 are also collateralized by the bank with pledged securities.

The custodial credit risk for *investments* is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The Code and the District's investment policy contains legal and policy requirements that would limit the exposure to custodial credit risk for investments. With respect to investments, custodial credit risk generally applies only to direct investments in marketable securities. Custodial credit risk does not apply to a local government's indirect investment in securities through the use of mutual funds or government investment pools.

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. The longer the maturity an investment has the greater its fair value has sensitivity to changes in market interest rates. The District's investment policy follows the Code as it relates to limits on investment maturities as a means of managing exposure to fair value losses arising from increasing interest rates.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(2) Cash and Cash Equivalents, continued

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization.

Concentration of Credit Risk

The District's investment policy does not contain various limitations on the amounts that can be invested in any one governmental agency or non-governmental issuer as stipulated by the California Government Code. The District's deposit portfolio with governmental agencies such as the Local Agency Investment Fund (LAIF) was 89% of the District's total depository and investment portfolio as of June 30, 2009.

(3) Capital Assets

Governmental Activities:

Changes in capital assets for the year were as follows:

	<u>Balance 2008</u>	<u>Additions</u>	<u>Deletions/ Transfers</u>	<u>Balance 2009</u>
Non-depreciable assets:				
Land	\$ 43,026	-	-	43,026
Construction in progress	<u>45,431</u>	<u>10,427</u>	<u>(44,431)</u>	<u>11,427</u>
Total non-depreciable assets	<u>88,457</u>	<u>10,427</u>	<u>(44,431)</u>	<u>54,453</u>
Depreciable assets:				
Land improvements	977,475	52,087	-	1,029,562
Equipment	<u>12,845</u>	<u>-</u>	<u>-</u>	<u>12,845</u>
Total depreciable assets	<u>990,320</u>	<u>52,087</u>	<u>-</u>	<u>1,042,407</u>
Accumulated depreciation:				
Land improvements	(91,589)	(52,420)	-	(144,009)
Equipment	<u>(696)</u>	<u>(642)</u>	<u>-</u>	<u>(1,338)</u>
Total accumulated depreciation	<u>(92,285)</u>	<u>(53,062)</u>	<u>-</u>	<u>(145,347)</u>
Total depreciable assets, net	<u>898,035</u>	<u>(975)</u>	<u>-</u>	<u>897,060</u>
Total capital assets, net	<u>\$ 986,492</u>			<u>951,513</u>

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(3) Capital Assets, continued

Enterprise Funds:

Changes in capital assets for the year were as follows:

	<u>Balance 2008</u>	<u>Additions</u>	<u>Deletions/ Transfers</u>	<u>Balance 2009</u>
Non-depreciable assets:				
Land	\$ 340,434	-	-	340,434
Construction in progress	2,636,052	424,338	(2,531,572)	528,818
Total non-depreciable assets	<u>2,976,486</u>	<u>424,338</u>	<u>(2,531,572)</u>	<u>869,252</u>
Depreciable assets:				
Transmission and distribution mains	15,321,698	1,626,121	-	16,947,819
Reservoirs	4,187,496	-	-	4,187,496
Pumping Station	3,927,984	7,097	-	3,935,081
Wells	2,161,928	1,749,867	-	3,911,795
Tanks	317,822	1,101,031	-	1,418,853
Hydrants and telemetry control	186,054	-	-	186,054
Vehicles and equipment	113,715	542,641	-	656,356
Total depreciable assets	<u>26,216,697</u>	<u>5,026,757</u>	<u>-</u>	<u>31,243,454</u>
Accumulated depreciation:				
Transmission and distribution mains	(8,196,553)	(439,053)	-	(8,635,606)
Reservoirs	(1,198,934)	(159,247)	-	(1,358,181)
Pumping Station	(1,885,099)	(99,066)	-	(1,984,165)
Wells	(492,182)	(80,037)	-	(572,219)
Tanks	(106,408)	(17,290)	-	(123,698)
Hydrants and telemetry control	(46,513)	(37,211)	-	(83,724)
Vehicles and equipment	(91,393)	(54,882)	-	(146,275)
Total accumulated depreciation	<u>(12,017,082)</u>	<u>(886,786)</u>	<u>-</u>	<u>(12,903,868)</u>
Total depreciable assets, net	<u>14,199,615</u>	<u>4,139,971</u>	<u>-</u>	<u>18,339,586</u>
Total capital assets, net	<u>\$ 17,176,101</u>	<u>4,564,309</u>	<u>(2,531,572)</u>	<u>19,208,838</u>

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(4) Long-term Debt

Changes in long-term debt were as follows:

	<u>Balance 2008</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance 2009</u>
Bonds payable:				
CA Infrastructure & Economic Dev. Bank	3,110,664	-	(96,648)	3,014,016
Total loan payable	\$ 3,110,664	-	(96,648)	3,014,016
Less: current portion	(96,648)			(100,040)
	<u>\$ 3,014,016</u>			<u>2,913,976</u>

California Infrastructure & Economic Development Bank – Revenue Bonds Payable

The San Bernardino County Special District County Service Area 70, Zone L, entered into an Installment Loan Agreement (Agreement) dated December 17, 2002 with the California Infrastructure and Economic Development Bank (CIEDB) to fund water system improvements in County Service Area 70, Zone L - Water Tank Project. According to the Agreement, the CIEDB is expected to issue a total amount of \$5,001,000 in Infrastructure State Revolving Fund Program Revenue Bonds (Bonds) to the San Bernardino County Special District County Service Area 70, Zone L, on a reimbursement basis. The San Bernardino County Special District County Service Area 70, Zone L, has agreed to make installment payments to the CIEDB on the Bonds, secured by a pledge of first lien on all the pledged net system revenue and all amounts in the San Bernardino County Special District County Service Area 70, Zone L.

Total amounts reimbursed by the CIEDB from inception to June 30, 2009 was \$3,537,908 and the principal amount paid by the San Bernardino County Special District County Service Area 70, Zone L on the Bond was \$457,244. The remainder of the loan payable balance was assumed by the Phelan-Piñon Hills Community Service District per LAFCO resolution No. 2989 as of March 18, 2008. The balance of the CIEDB loan assumed was \$3,110,664.

The term of the agreement is thirty years from December 17, 2002 at an interest rate of 3.50%. Principal and interest payments are due on the Bonds each February 1st.

As of June 30, 2009, the District has not requested any further reimbursements from the CIEDB and the District is currently working with CIEDB to close out the project and have the loan repayment schedule revised to reflect payment terms on the current remaining principal balance due. Therefore, as of the date of this report, a CIEDB loan repayment schedule has not been received and a loan repayment schedule has not been reflected in this report. Current loan principal and interest accrual amounts have been estimated and reflected in the statement of net assets for fiscal year 2010 CIEDB loan payments.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(5) Net Investment in Capital Assets

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Total</u>
The balance consists of the following:			
Capital assets – not being depreciated	\$ 54,453	869,252	923,705
Capital assets – being depreciated, net	897,060	18,339,586	19,236,646
Long-term debt – current portion	-	(100,040)	(100,040)
Long-term debt – long-term portion	-	(2,913,976)	(2,913,976)
Total	<u>\$ 951,513</u>	<u>16,194,822</u>	<u>17,146,335</u>

(6) Unrestricted Net Assets

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Total</u>
Net assets are designated as follows:			
Parks and recreation	\$ 1,540,852	-	1,540,852
Street lighting	-	-	-
Materials and supplies inventory	-	72,432	72,432
Prepaid expenses and other assets	-	27,348	27,348
Water operations and capital replacement	-	13,726,536	13,726,536
Total	<u>\$ 1,540,852</u>	<u>13,826,316</u>	<u>15,367,168</u>

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(7) 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 is a member of the Special District Risk Management Authority (SDRMA), an intergovernmental risk sharing joint powers authority created to provide self-insurance programs for California special districts. The purpose of the SDRMA is to arrange and administer programs of self-insured losses and to purchase excess insurance coverage. At June 30, 2009, the District participated in the liability and property programs of the SDRMA as follows:

- General and auto liability, public officials and employees' errors and omissions: Total risk financing self-insurance limits of \$2,500,000, combined single limit at \$2,500,000 per occurrence. The District purchased additional excess coverage layers: \$7,500,000 for general, auto and public officials liability, which increases the limits on the insurance coverage noted above.

In addition to the above, the District also has the following insurance coverage:

- Employee dishonesty coverage up to \$400,000 per loss includes public employee dishonesty, forgery or alteration and theft, disappearance and destruction coverages.
- Property loss is paid at the replacement cost for property on file, if replaced within two years after the loss, otherwise paid on an actual cash value basis, to a combined total of \$1.0 billion per occurrence, subject to a \$5,000 deductible per occurrence.
- Boiler and machinery coverage for the replacement cost up to \$100 million per occurrence, subject to a \$5,000 deductible per occurrence.
- Public officials personal liability up to \$500,000 each occurrence, with an annual aggregate of \$100,000 per each elected/appointed official to which this coverage applies, subject to the terms, with a deductible of \$500 per claim.
- Workers' compensation insurance up to \$200 million per occurrence and Employer's Liability Coverage up to \$5 million.

Settled claims have not exceeded any of the coverage amounts in the last fiscal years. There were no reductions in insurance coverage in fiscal year 2009. Liabilities are recorded when it is probable that a loss has been incurred and the amount of the loss can be reasonably estimated net of the respective insurance coverage. Liabilities include an amount for claims that have been incurred but not reported (IBNR). There were no material IBNR claims payable as of June 30, 2009.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
For the Year Ended June 30, 2009

(8) Governmental Accounting Standards Board Statements Issued, Not Yet Effective

The Governmental Accounting Standards Board (GASB) has issued several pronouncements prior to June 30, 2009, that have effective dates that may impact future financial presentations.

Governmental Accounting Standards Board Statement No. 51

In June 2007, the GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. This statement requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets. This statement is not effective for this District until the fiscal year ended June 30, 2010. This statement is not expected to have a significant impact on the presentation of the District's financial statements.

Governmental Accounting Standards Board Statement No. 53

In June 2008, the GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. This statement addresses the recognition, measurement, and disclosure of information regarding derivative instruments entered into by state and local governments. This statement is not effective for this District until the fiscal year ended June 30, 2010. This statement is not expected to have a significant impact on the presentation of the District's financial statements.

(9) Commitments and Contingencies

Litigation

In the ordinary course of operations, the District is subject to claims and litigation from outside parties. After consultation with legal counsel, the District believes the ultimate outcome of such matters, if any, will not materially affect its financial condition.

(10) Subsequent Event

CalPERS Defined Benefit Pension Plan

The District has elected to participate in the CalPERS Defined Benefit Pension Plan with a benefit of 2.5% at 55 years-of-age. The District will begin contributing to the CalPERS Defined Benefit Pension Plan in fiscal year 2010.

Report on Compliance and Internal Controls



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Independent Auditor's Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Board of Directors
Phelan Piñon Hills Community Services District
Phelan, California

We have audited the basic financial statements of the Phelan Piñon Hills Community Services District (District) as of and for the year ended June 30, 2009, and have issued our report thereon dated October 20, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the District's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the District's financial statements that is more than inconsequential will not be prevented or detected by the District's internal control. A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the District's internal control. Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

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

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

October 20, 2009
Cypress, California

Charles Z. Fedak, CPA
An Accountancy Corporation