



Phelan Piñon Hills Community Services District

Annual Financial Report

For the Fiscal Year Ended June 30, 2011



PHELAN PIÑON HILLS COMMUNITY SERVICES DISTRICT

List of Elected and Appointed Officials

June 30, 2011

Elected Officials

BOARD OF DIRECTORS

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

Appointed Official

General Manager Don Bartz

**Phelan Piñon Hills Community Services District
4176 Warbler Road
Phelan, California 92371
(760) 868-1212 www.pphcsd.org**



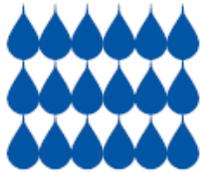
Phelan Piñon Hills Community Services District
Annual Financial Report
For the Fiscal Year Ended June 30, 2011

**Phelan Piñon Hills Community Services District
Annual Financial Report
For the Fiscal Year Ended June 30, 2011**

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Financial Section



Charles Z. Fedak, CPA, MBA
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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 Pinon Hills Community Services District (District) as of and for the year ended June 30, 2011, 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 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; and the State Controller's Minimum Audit Requirements for California Special Districts. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the Phelan Pinon Hills Community Services District as of June 30, 2011, 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.

As described in Note 1.B to the basic financial statements, the District adopted the provisions of Governmental Accounting Standards Board Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, for the year ended June 30, 2011.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 24, 2011, 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. That report can be found on page 31.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context.

Independent Auditor's Report, continued

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 inquires of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquires, the basic financial statements, and other knowledge we obtained during our audit of the basic 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.



Charles Z. Fedak: Company CPAs - An Accountancy Corporation

Charles Z. Fedak and Company, CPA's - An Accountancy Corporation
Cypress, California
October 24, 2011

**Phelan Piñon Hills Community Services District
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2011**

The following Management's Discussion and Analysis (MD&A) of activities and financial performance of the Phelan Piñon Hills Community Services District (District) provides an introduction to the financial statements of the District for the fiscal year ended June 30, 2011. We encourage readers to consider the information presented here in conjunction with the basic financial statements and related notes, which follow this section.

Financial Highlights

- Net assets increased 2.28% or \$773,044 to \$34,693,544 as a result of this year's operations.
- Total revenues decreased 7.22% or \$452,598 in 2011 due primarily to a \$212,339 decrease in other non-operating revenue in the water fund as a result of a prior year gain on sale of disposed assets and a \$183,538 decrease in other income in the government funds from fiscal year 2010.
- Total expenses increased by 3.73% or \$181,355 in 2011 due primarily to a increase in the water fund expenses of \$127,534 from fiscal year 2010.

Using This Financial Report

This annual report consists of a series of financial statements. The Statement of Net Assets and the Statement of Activities provides information about the activities and performance of the District using accounting methods similar to those used by private sector companies. The Statement of Net Assets includes all of the District's investments in resources (assets) and the obligations to creditors (liabilities). It also provides the basis for computing a rate of return, evaluating the capital structure of the District and assessing the liquidity and financial flexibility of the District. All of the current year's revenue and expenses are accounted for in the Statement of Activities. This statement measures the success of the District's operations over the past year and can be used to determine the District's profitability and credit worthiness.

Government-wide Financial Statements

Statement of Net Assets and Statement of Activities

One of the most important questions asked about the District's finances is, "Is the District better off or worse off as a result of this year's activities?" The Statement of Net Assets and the Statement of Activities report information about the District in a way that helps answer this question. These statements include all assets and liabilities using the *accrual basis of accounting*, which is similar to the accounting used by most private sector companies. All of the current year's revenues and expenses are taken into account regardless of when the cash is received or paid.

These two statements report the District's *net assets* and changes in them. Think of the District's net assets – the difference between assets and liabilities – as one way to measure the District's financial health, or *financial position*. Over time, *increases or decreases* in the District's net assets are one indicator of whether its *financial health* is improving or deteriorating. You will need to consider other non-financial factors; however, such as changes in the District's property tax base and the types of grants the District applies for to assess the *overall financial health* of the District.

**Phelan Piñon Hills Community Services District
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2011**

Fund Financial Statements

Balance Sheet and Statement of Revenues, Expenditures and Changes in Fund Balance

Governmental funds are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating a government's near term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures and changes in fund balance provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

Notes to the Basic Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the basic financial statements can be found on pages 16 through 30.

Government-wide Financial Analysis

Statement of Net Assets

The following table is a summary of the statement of net assets at June 30, 2011.

	Condensed Statement of Net Assets					
	Governmental Activities		Business-type Activities		Total District	
	2011	2010	2011	2010	2011	2010
Assets:						
Current and other assets	\$ 3,072,421	1,882,460	10,360,518	11,792,531	13,432,939	13,674,991
Non-current assets	129,876	126,400	-	-	129,876	126,400
Capital assets, net	2,062,298	2,104,045	22,572,994	21,885,230	24,635,292	23,989,275
Total assets	<u>5,264,595</u>	<u>4,112,905</u>	<u>32,933,512</u>	<u>33,677,761</u>	<u>38,198,107</u>	<u>37,790,666</u>
Liabilities:						
Current liabilities	13,324	116,006	727,077	908,120	740,401	1,024,126
Non-current liabilities	5,126	2,105	2,759,036	2,833,935	2,764,162	2,836,040
Total liabilities	<u>18,450</u>	<u>118,111</u>	<u>3,486,113</u>	<u>3,742,055</u>	<u>3,504,563</u>	<u>3,860,166</u>
Net assets:						
Investment in capital assets, net of related debt	2,062,298	2,104,045	19,762,550	18,971,254	21,824,848	21,075,299
Unrestricted	3,183,847	1,890,749	9,684,849	10,954,452	12,868,696	12,845,201
Total net assets	<u>\$ 5,246,145</u>	<u>3,994,794</u>	<u>29,447,399</u>	<u>29,925,706</u>	<u>34,693,544</u>	<u>33,920,500</u>

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the District, assets of the District exceeded liabilities by \$34,693,544 as of June 30, 2011. Compared to prior year, net assets of the District increased 2.28% or \$773,044. The District's net assets are made-up of two components: (1) net investment in capital assets and (2) unrestricted net assets.

**Phelan Piñon Hills Community Services District
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2011**

Statement of Activities

The following table is a summary of the statement of activities for the year ended June 30, 2011.

	<u>Governmental Activities</u>		<u>Business-type Activities</u>		<u>Total District</u>	
	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>
Revenues:						
Program revenues:						
Charges for services	\$ 20,622	142,601	3,932,214	3,860,371	3,952,836	4,002,972
Capital grants and contributions	600,000	300,000	151,582	176,546	751,582	476,546
General revenues:						
Property taxes	907,485	1,108,201	-	14,631	907,485	1,122,832
Interest earnings	10,967	11,191	81,866	147,916	92,833	159,107
Other	-	183,538	113,131	325,470	113,131	509,008
Total revenues	<u>1,539,074</u>	<u>1,745,531</u>	<u>4,278,793</u>	<u>4,524,934</u>	<u>5,817,867</u>	<u>6,270,465</u>
Expenses:						
Parks and recreation	274,856	229,139	-	-	274,856	229,139
Street lighting	12,867	13,963	-	-	12,867	13,963
Water	-	-	4,757,100	4,620,366	4,757,100	4,620,366
Total expenses	<u>287,723</u>	<u>243,102</u>	<u>4,757,100</u>	<u>4,620,366</u>	<u>5,044,823</u>	<u>4,863,468</u>
Change in net assets	1,251,351	1,502,429	(478,307)	(95,432)	773,044	1,406,997
Net assets, beginning of year	<u>3,994,794</u>	<u>2,492,365</u>	<u>29,925,706</u>	<u>30,021,138</u>	<u>33,920,500</u>	<u>32,513,503</u>
Net assets, end of year	<u>\$ 5,246,145</u>	<u>3,994,794</u>	<u>29,447,399</u>	<u>29,925,706</u>	<u>34,693,544</u>	<u>33,920,500</u>

Net assets increased by 2.28% or \$773,044 due in part to an increase in capital contributions of \$275,036 from the prior year and the result of operations.

Total revenues decreased 7.22% or \$452,598 in 2011 due primarily to a \$212,339 decrease in other non-operating revenue in the water fund as a result of a prior year gain on sale of disposed assets and a \$183,538 decrease in other income in the park fund from fiscal year 2010.

The District's total expenses increased by 3.73% or \$181,355 in 2011 due primarily to an increase in the water fund expenses of \$127,534 from fiscal year 2010.

Capital Asset Administration

	Capital Assets					
	<u>Governmental Activities</u>		<u>Business-type Activities</u>		<u>Total District</u>	
	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>
Capital assets:						
Non-depreciable assets	\$ 1,246,197	1,233,329	2,972,869	1,625,829	4,219,066	2,859,158
Depreciable assets	<u>1,069,849</u>	<u>1,069,849</u>	<u>34,751,392</u>	<u>34,164,754</u>	<u>35,821,241</u>	<u>35,234,603</u>
Total capital assets	2,316,046	2,303,178	37,724,261	35,790,583	40,040,307	38,093,761
Accumulated depreciation	<u>(253,748)</u>	<u>(199,133)</u>	<u>(15,151,267)</u>	<u>(13,905,353)</u>	<u>(15,405,015)</u>	<u>(14,104,486)</u>
Total capital assets, net	<u>\$ 2,062,298</u>	<u>2,104,045</u>	<u>22,572,994</u>	<u>21,885,230</u>	<u>24,635,292</u>	<u>23,989,275</u>

At the end of fiscal year 2011, the District's investment in capital assets amounted to \$24,635,292 (net of accumulated depreciation). This investment in capital assets includes land, buildings, building improvements, furnishings and equipment, collection and distribution systems, tanks, wells, water transmission and distribution systems and construction-in-process. The capital assets of the District are more fully analyzed in Note 4 to the basic financial statements.

**Phelan Piñon Hills Community Services District
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2011**

Long-Term Debt Administration

	<u>Long-term Debt</u>					
	<u>Governmental Activities</u>		<u>Business-Type Activities</u>		<u>Total</u>	
	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>
Long-term debt:						
Long-term debt	\$ -	-	2,810,444	2,913,976	2,810,444	2,913,976

Long-term debt decreased due to regular debt payments. The long-term debt position of the District is more fully analyzed in Note 6 to the basic financial statements.

Conditions Affecting Current Financial Position

Management is unaware of any conditions, which could have a significant impact on the District's current financial position, net assets or operating results in terms of past, present and future.

Requests for Information

This financial report is designed to provide the District's funding sources, customers, stakeholders and other interested parties with an overview of the District's financial operations and financial condition. Should the reader have questions regarding the information included in this report or wish to request additional financial information, please contact the District's Administrative Services Manager at 4176 Warbler Road, Phelan, California 92371 or (760) 868-1212.

Basic Financial Statements

Phelan Piñon Hills Community Services District
Statement of Net Assets
June 30, 2011

<i>Assets</i>	Governmental Activities	Business-type Activities	Total
Current assets:			
Cash and cash equivalents (note 2)	\$ 3,030,481	\$ 9,244,514	12,274,995
Accrued interest receivable	-	332	332
Accounts receivable – water sales and services	-	807,840	807,840
Accounts receivable – other	-	9,548	9,548
Property taxes and assessments receivable	41,940	60,042	101,982
Materials and supplies inventory	-	95,006	95,006
Prepaid expenses and other assets	-	143,236	143,236
Total current assets	<u>3,072,421</u>	<u>10,360,518</u>	<u>13,432,939</u>
Non-current assets:			
Note receivable - property tax from state (note 3)	129,876	-	129,876
Capital assets – not being depreciated (note 4)	1,246,197	2,972,869	4,219,066
Capital assets – being depreciated, net (note 4)	<u>816,101</u>	<u>19,600,125</u>	<u>20,416,226</u>
Total non-current assets	<u>2,192,174</u>	<u>22,572,994</u>	<u>24,765,168</u>
Total assets	<u>5,264,595</u>	<u>32,933,512</u>	<u>38,198,107</u>
<i>Liabilities and Net Assets</i>			
Current liabilities:			
Accounts payable and accrued expenses	4,513	267,887	272,400
Accrued salaries and related payables	3,685	195,815	199,500
Customer deposits and deferred revenue	-	53,169	53,169
Accrued interest on long-term debt	-	47,302	47,302
Long-term liabilities – due within one year:			
Compensated absences (note 5)	5,126	55,748	60,874
Long-term debt (note 6)	<u>-</u>	<u>107,156</u>	<u>107,156</u>
Total current liabilities	<u>13,324</u>	<u>727,077</u>	<u>740,401</u>
Non-current liabilities:			
Long-term liabilities – due in more than one year:			
Compensated absences (note 5)	5,126	55,748	60,874
Long-term debt (note 6)	<u>-</u>	<u>2,703,288</u>	<u>2,703,288</u>
Total non-current liabilities	<u>5,126</u>	<u>2,759,036</u>	<u>2,764,162</u>
Total liabilities	<u>18,450</u>	<u>3,486,113</u>	<u>3,504,563</u>
Net assets:			
Investment in capital assets, net of related debt (note 8)	2,062,298	19,762,550	21,824,848
Unrestricted (note 9)	<u>3,183,847</u>	<u>9,684,849</u>	<u>12,868,696</u>
Total net assets	<u>\$ 5,246,145</u>	<u>\$ 29,447,399</u>	<u>34,693,544</u>

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Statement of Activities
For the Fiscal Year Ended June 30, 2011

Functions/Programs	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Assets		
		Charges for Services	Capital Grants and Contributions	Governmental Activities	Business-type Activities	Total
Governmental activities:						
Parks and recreation	\$ 274,856	20,622	600,000	345,766	-	345,766
Street lighting	12,867	-	-	(12,867)	-	(12,867)
Total governmental	287,723	20,622	600,000	332,899	-	332,899
Business-type activities:						
Water	4,757,100	3,932,214	151,582	-	(673,304)	(673,304)
Total business-type	4,757,100	3,932,214	151,582	-	(673,304)	(673,304)
Total	\$ 5,044,823	3,952,836	751,582	332,899	(673,304)	(340,405)
		General revenues:				
		Property taxes		\$ 907,485	-	907,485
		Interest earnings		10,967	81,866	92,833
		Other		-	113,131	113,131
		Total general revenues		918,452	194,997	1,113,449
		Change in net assets		1,251,351	(478,307)	773,044
		Net assets, beginning of year		3,994,794	29,925,706	33,920,500
		Net assets, end of year		\$ 5,246,145	29,447,399	34,693,544

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Balance Sheets – Governmental Funds
June 30, 2011

	Parks and Recreation	Street Lighting	Total Governmental Activities
Assets:			
Cash and cash equivalents	\$ 3,030,481	-	3,030,481
Property taxes and assessments receivable	41,940	-	41,940
Total assets	3,072,421	-	3,072,421
Liabilities:			
Accounts payable and accrued expenses	4,513	-	4,513
Accrued wages and related payables	3,685	-	3,685
Total liabilities	8,198	-	8,198
Fund balance:			
Assigned	10,252	-	10,252
Unassigned	3,053,971	-	3,053,971
Total fund balance	3,064,223	-	3,064,223
Total liabilities and fund balance	\$ 3,072,421	-	3,072,421

Phelan Piñon Hills Community Services District
Reconciliation of the Balance Sheets of Governmental Funds to the Statement of Net Assets
June 30, 2011

Reconciliation:

Fund balance of governmental funds	\$	3,064,223
Amounts reported for governmental activities in the statement of net assets is different because:		
Non-current assets applicable to the District are not receivable in the current period and, therefore, are not reported as fund assets. All assets both current and non-current, are reported in the Statement of Net Assets as follows:		129,876
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.		2,062,298
Long-term liabilities applicable to the District are not due and payable in the current period and accordingly are not reported as fund liabilities. All liabilities both current and long-term, are reported in the Statement of Net Assets as follows:		<u>(10,252)</u>
Net assets of governmental activities	\$	<u><u>5,246,145</u></u>

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 Fiscal Year Ended June 30, 2011

	<u>Parks and Recreation</u>	<u>Street Lighting</u>	<u>Total Governmental Activities</u>
Revenues:			
Charges for services	\$ 20,622	-	20,622
Property taxes	904,009	-	904,009
Capital grants	600,000	-	600,000
Interest earnings	10,967	-	10,967
Total revenues	<u>1,535,598</u>	<u>-</u>	<u>1,535,598</u>
Expenditures:			
Parks and recreation	213,497	-	213,497
Street lighting	-	12,867	12,867
Capital outlay	12,868	-	12,868
Total expenditures	<u>226,365</u>	<u>12,867</u>	<u>239,232</u>
Net income(loss)	<u>1,309,233</u>	<u>(12,867)</u>	<u>1,296,366</u>
Other financing sources(uses):			
Transfers in(out)	<u>(12,867)</u>	<u>12,867</u>	<u>-</u>
Total other financing sources	<u>(12,867)</u>	<u>12,867</u>	<u>-</u>
Change in fund balance	<u>1,296,366</u>	<u>-</u>	<u>1,296,366</u>
Fund balance, beginning of year	<u>1,767,857</u>	<u>-</u>	<u>1,767,857</u>
Fund balance, end of year	<u>\$ 3,064,223</u>	<u>-</u>	<u>3,064,223</u>

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, 2011

Reconciliation:

Net changes in fund balance of total governmental funds	\$	1,296,366
Amounts reported for governmental activities in the statement of activities are different because:		
Some revenues reported in the Statement of Activities are not considered current financial resources and therefore are not reported as revenues in the government funds as follows:		
Accrued interest - property tax from State		3,476
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:		
Capital outlay		12,868
Depreciation expense		(54,615)
Some expenses reported in the Statement of Activities do not require the use of current financial resources and are therefore not reported as expenses in the governmental fund as follows:		
Net change in compensated absences		<u>(6,744)</u>
Change in net assets of governmental activities	\$	<u><u>1,251,351</u></u>

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Statement of Net Assets – Enterprise Fund
June 30, 2011

<i>Assets</i>	Water Enterprise
Current assets:	
Cash and cash equivalents	\$ 9,244,514
Accrued interest receivable	332
Accounts receivable – utilities, net	807,840
Accounts receivable – other	9,548
Property taxes and assessments receivable	60,042
Materials and supplies inventory	95,006
Prepaid expenses and other assets	143,236
Total current assets	10,360,518
Non-current assets:	
Capital assets – not being depreciated	2,972,869
Capital assets – being depreciated, net	19,600,125
Total non-current assets	22,572,994
Total assets	32,933,512
<i>Liabilities and Net Assets</i>	
Current liabilities:	
Accounts payable and accrued expenses	267,887
Accrued salaries and related payables	195,815
Customer deposits and deferred revenue	53,169
Accrued interest on long-term debt	47,302
Long-term liabilities – due within one year:	
Compensated absences	55,748
Long-term debt	107,156
Total current liabilities	727,077
Non-current liabilities:	
Long-term liabilities – due in more than one year:	
Compensated absences	55,748
Long-term debt	2,703,288
Total non-current liabilities	2,759,036
Total liabilities	3,486,113
Net assets:	
Net investment in capital assets	19,762,550
Unrestricted	9,684,849
Total net assets	\$ 29,447,399

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Statement of Revenues, Expenses and Changes in Fund Net Assets – Enterprise Fund
For the Year Ended June 30, 2011

	<u>Water Enterprise</u>
Operating revenues:	
Water consumption sales	\$ 2,124,831
Monthly meter service charge	1,411,724
Special assessment	324,650
Other charges and services	71,009
Total operating revenues	<u>3,932,214</u>
Operating expenses:	
Source of supply – water related purchases	147,596
Pumping – utilities	752,063
Transmission and distribution	408,278
General and administrative	2,087,333
Total operating expenses	<u>3,395,270</u>
Operating income before depreciation	536,944
Depreciation	<u>(1,245,913)</u>
Operating loss	<u>(708,969)</u>
Non-operating revenues(expenses):	
Interest earnings	81,866
Interest expense – long-term debt	(105,876)
Other non-operating revenues	113,131
Other non-operating expenses	<u>(10,041)</u>
Total non-operating revenues, net	<u>79,080</u>
Net loss before capital contributions	<u>(629,889)</u>
Capital contributions:	
Capital grants	<u>151,582</u>
Capital contributions	<u>151,582</u>
Change in net assets	(478,307)
Net assets, beginning of year	<u>29,925,706</u>
Net assets, end of year	<u>\$ 29,447,399</u>

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Statement of Cash Flows – Enterprise Fund
For the Year Ended June 30, 2011

	<u>Water Enterprise</u>
Cash flows from operating activities:	
Cash receipts from customers	\$ 3,849,078
Cash paid to vendors and suppliers	<u>(3,501,857)</u>
Net cash provided by operating activities	<u>347,221</u>
Cash flows from non-capital financing activities:	
Other non-operating revenues	113,131
Other non-operating expenses	<u>(10,041)</u>
Net cash provided by non-capital financing activities	<u>103,090</u>
Cash flows from capital and related financing activities:	
Acquisition and construction of capital assets	(1,934,599)
Proceeds from capital contributions	151,582
Principal payments on long-term debt	(103,532)
Interest payments on long-term debt	<u>(58,574)</u>
Net cash used in capital and financing activities	<u>(1,945,123)</u>
Cash flows from investing activities:	
Purchases and sales of investments, net	154,801
Interest earnings	<u>81,534</u>
Net cash provided by investing activities	<u>236,335</u>
Net decrease in cash	(1,361,567)
Cash and cash equivalents, beginning of year	<u>10,606,081</u>
Cash and cash equivalents, end of year	\$ <u><u>9,244,514</u></u>
Reconciliation of operating loss to net cash provided by operating activities:	
Operating loss	<u>(708,969)</u>
Adjustments to reconcile operating loss to net cash provided by operating activities:	
Depreciation expense	1,245,913
Changes in assets and liabilities:	
(Increase)decrease in assets:	
Accounts receivable – water sales and services	(179,462)
Accounts receivable – other	12,341
Property taxes and assessments receivable	83,985
Materials and supplies inventory	23,125
Prepaid expenses and other assets	21,426
Increase(decrease) in liabilities:	
Accounts payable and accrued expenses	(273,608)
Accrued salaries and related payables	4,341
Customer deposits and deferred revenue	45,785
Compensated absences	72,344
Total adjustments	<u>1,056,190</u>
Net cash provided by operating activities	\$ <u><u>347,221</u></u>

See accompanying notes to the basic financial statements

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements
June 30, 2011

(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
June 30, 2011

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

B. New Accounting Pronouncements

Government Accounting Standards Board Statement No. 54

For the fiscal year ended June 30, 2011, the District implemented Government Accounting Standards Board Statement No. 54 (GASB 54), *Fund Balance Reporting and Governmental Fund Type Definitions*. The requirements of this statement are effective for the financial statement periods beginning after June 15, 2010.

GASB 54 enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied, and it clarifies the existing governmental fund type definitions. It establishes balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in the governmental funds. These classifications are described in the Fund Equity section of Note 1.D.8.

GASB 54 also provides guidance for classifying stabilization amounts on the face of the balance sheet and requires disclosure of certain information about stabilization arrangements in the notes to the financial statements. The definitions of the general fund, special revenue fund type, capital projects fund type, debt service fund type, and permanent fund type are also clarified by the provisions in this statement.

C. 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.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements
June 30, 2011

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

C. Basis of Accounting and Measurement Focus, continued

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.

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.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

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

C. Basis of Accounting and Measurement Focus, continued

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.

D. 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.

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

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

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

D. Financial Statement Elements, continued

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

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 constraints placed on net assets use through external constraints imposed by creditors, grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.
- **Unrestricted Net Assets** – This component of net assets consists of net assets that do not meet the definition of *restricted* or *net investment in capital assets*.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

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

D. Financial Statement Elements, continued

8. Fund Equity

The financial statements, governmental funds report fund balance as nonspendable, restricted, committed, assigned or unassigned based primarily on the extent to which the District is bound to honor constraints on how specific amounts can be spent.

- **Nonspendable fund balance** – amounts that cannot be spent because they are either (a) not spendable in form or (b) legally or contractually required to be maintained intact.
- **Restricted fund balance** – amounts with constraints placed on their use that are either (a) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments; or (b) imposed by law through constitutional provisions enabling legislation.
- **Committed fund balance** – amounts that can only be used for specific purposes determined by formal action of the District’s highest level of decision-making authority (the Board of Directors) and that remain binding unless removed in the same manner. The underlying action that imposed the limitation needs to occur no later than the close of the reporting period.
- **Assigned fund balance** – amounts that are constrained by the District’s intent to be used for specific purposes. The intent can be established at either the highest level of decision-making, or by a body or an official designated for that purpose. This is also the classification for residual funds in the District’s special revenue funds.
- **Unassigned fund balance** – the residual classification for the District’s general fund that includes amounts not contained in the other classifications. In other funds, the unassigned classification is used only if expenditures incurred for specific purposes exceed the amounts restricted, committed, or assigned to those purposes.

The Board of Directors established, modifies or rescinds fund balance commitments and assignments by passage of an ordinance or resolution. This is done through adoption of the budget and subsequent budget amendments that occur throughout the year.

When both restricted and unrestricted resources are available for use, it is the District’s policy to use restricted resources first, followed by the unrestricted, committed, assigned and unassigned resources as they are needed.

Fund Balance Policy

The District believes that sound financial management principles require that sufficient funds be retained by the District to provide a stable financial base at all times. To retain this stable financial base, the District needs to maintain an unrestricted fund balance in its funds sufficient to fund cash flows of the District and to provide financial reserves for unanticipated expenditures and/or revenue shortfalls of an emergency nature. Committed, assigned and unassigned fund balances are considered unrestricted.

The purpose of the District’s fund balance policy is to maintain a prudent level of financial resources to protect against reducing service levels or raising taxes and fees because of temporary revenue shortfalls or unpredicted one-time expenditures.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

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

D. Financial Statement Elements, continued

9. 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.

10. 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.

11. 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.

(2) Cash and Investments

Cash and cash equivalents consist of the following:

	2011
Cash on hand	\$ 500
Deposits held with financial institutions	11,994,381
Deposits held with California Local Agency Investment Fund (LAIF)	280,114
Total	\$ 12,274,995

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

Deposits held with California Local Agency Investment Fund (LAIF)	237 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.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

(2) Cash and Investments, continued

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. Of the District's bank balances, up to \$250,000 is federally insured and the remaining balance is collateralized in accordance with the code.

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 contain 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.

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 2% of the District's total depository and investment portfolio as of June 30, 2011.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

(3) Note Receivable – Property Tax from State

Under the provisions of the State of California Proposition 1A and as part of the 2010 fiscal year State of California budget package passed by the California State Legislature on July 28, 2009, the State of California borrowed 8.0% of the amount of property tax revenue apportioned to cities, counties and special districts. The State of California is required to repay this borrowing plus interest by June 30, 2013. After repayment of this initial borrowing, the California State Legislature may consider only one additional borrowing within a ten-year period. The amount of the borrowing plus interest pertaining to the District was \$129,876. The borrowing by the State of California was recognized as a note receivable in the accompanying financial statements.

(4) Capital Assets

Governmental Activities:

Changes in capital assets for the year were as follows:

	<u>Balance 2010</u>	<u>Additions</u>	<u>Deletions/ Transfers</u>	<u>Balance 2011</u>
Non-depreciable assets:				
Land	\$ 1,180,743	-	-	1,180,743
Construction in progress	52,586	12,868	-	65,454
Total non-depreciable assets	<u>1,233,329</u>	<u>12,868</u>	<u>-</u>	<u>1,246,197</u>
Depreciable assets:				
Land improvements	1,057,004	-	-	1,057,004
Equipment	12,845	-	-	12,845
Total depreciable assets	<u>1,069,849</u>	<u>-</u>	<u>-</u>	<u>1,069,849</u>
Accumulated depreciation:				
Land improvements	(197,153)	(53,973)	-	(251,126)
Equipment	(1,980)	(642)	-	(2,622)
Total accumulated depreciation	<u>(199,133)</u>	<u>(54,615)</u>	<u>-</u>	<u>(253,748)</u>
Total depreciable assets, net	<u>870,716</u>	<u>(54,615)</u>	<u>-</u>	<u>816,101</u>
Total capital assets, net	<u>\$ 2,104,045</u>			<u>2,062,298</u>

Major governmental capital asset additions during fiscal year 2011 include additions to non-depreciable construction in progress.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

(4) Capital Assets, continued

Enterprise Funds:

Changes in capital assets for the year were as follows:

	<u>Balance 2010</u>	<u>Additions</u>	<u>Deletions/ Transfers</u>	<u>Balance 2011</u>
Non-depreciable assets:				
Land	\$ 780,835	-	(1,011)	779,824
Construction in progress	844,994	1,936,501	(588,450)	2,193,045
Total non-depreciable assets	<u>1,625,829</u>	<u>1,936,501</u>	<u>(589,461)</u>	<u>2,972,869</u>
Depreciable assets:				
Transmission and distribution mains	17,189,515	-	-	17,189,515
Reservoirs	4,187,496	-	-	4,187,496
Pumping Station	4,114,808	-	-	4,114,808
Wells	4,442,165	247,950	-	4,690,115
Tanks	1,463,404	-	-	1,463,404
Hydrants and telemetry control	191,669	-	-	191,669
Meters	1,921,146	-	-	1,921,146
Planning and development	-	319,427	-	319,427
Vehicles and equipment	654,551	19,261	-	673,812
Total depreciable assets	<u>34,164,754</u>	<u>586,638</u>	<u>-</u>	<u>34,751,392</u>
Accumulated depreciation:				
Transmission and distribution mains	(9,096,530)	(467,485)	-	(9,564,015)
Reservoirs	(1,517,428)	(159,247)	-	(1,676,675)
Pumping Station	(2,084,447)	(111,265)	-	(2,195,712)
Wells	(675,615)	(119,658)	-	(795,273)
Tanks	(160,588)	(38,611)	-	(199,199)
Hydrants and telemetry control	(121,028)	(38,334)	-	(159,362)
Meters	(48,029)	(192,115)	-	(240,144)
Planning and development	-	(1,331)	-	(1,331)
Vehicles and equipment	(201,688)	(117,868)	-	(319,556)
Total accumulated depreciation	<u>(13,905,353)</u>	<u>(1,245,914)</u>	<u>-</u>	<u>(15,151,267)</u>
Total depreciable assets, net	<u>20,259,401</u>	<u>(659,276)</u>	<u>-</u>	<u>19,600,125</u>
Total capital assets, net	<u>\$ 21,885,230</u>	<u>1,277,225</u>	<u>(589,461)</u>	<u>22,572,994</u>

Major enterprise capital asset additions during fiscal year 2011 include additions to non-depreciable construction in progress and depreciable wells, planning and development, and vehicles and equipment.

(5) Compensated Absences

Compensated absences comprise unpaid vacation leave that accrue when benefits are fully vested and are determined annually. Compensated absences turn-over each year, therefore, the compensated absence balance of the District is considered a current liability on the Statements of Net Assets.

The changes to compensated absences balances at June 30, were as follows:

	<u>Balance 2010</u>	<u>Earned</u>	<u>Taken</u>	<u>Balance 2011</u>	<u>Due Within One Year</u>	<u>Due in more than one year</u>
\$	42,660	216,728	(137,640)	121,748	60,874	60,874

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

(6) Long-term Debt

Changes in long-term debt were as follows:

	Balance 2010	Additions	Payments	Balance 2011
CA Infrastructure & Economic Dev. Bank	\$ 2,913,976	-	(103,532)	2,810,444
Total loan payable	2,913,976	-	(103,532)	2,810,444
Less: current portion	(100,040)			(107,156)
	\$ 2,813,936			2,703,288

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.

Fiscal Year	Principal	Interest	Total
2012	\$ 107,156	113,524	220,680
2013	110,906	109,774	220,680
2014	114,788	105,892	220,680
2015	118,805	101,875	220,680
2016	122,964	97,716	220,680
2017-2021	682,467	420,932	1,103,399
2022-2026	810,557	292,842	1,103,399
2027-2030	742,801	126,038	868,839
Totals	2,810,444	1,368,593	4,179,037
Less: current portion	(107,156)		
Total non-current	\$ 2,703,288		

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

(7) Defined Benefit Pension Plan

Plan Description

The District contributes to the California Public Employees Retirement System (CalPERS), a cost-sharing multi-employer defined benefit pension plan. CalPERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. CalPERS act as a common investment and administrative agent for participating public agencies within the State of California. Benefit provisions and all other requirements are established by state statute and the Agency. Copies of CalPERS annual financial report may be obtained form their executive Office: 400 P Street, Sacramento, CA, 95814.

Funding Policy

The contribution rate for plan members in the CalPERS 2.5% at 55 Risk Pool Retirement Plan is 8% of their annual covered salary. The Agency makes these contributions required of Agency employees on their behalf and for their account. Also, the Agency is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The required employer contribution rates are equal to the annual pension costs (APC) percentage of payroll for fiscal year 2011 as noted below. The contribution requirements of the plan members are established by State statute, and the employer contribution rate is established and may be amended by CalPERS. For fiscal year 2011, the Agencies annual contribution for CalPERS and were equal to the Agencies required and actual contribution for each fiscal year as follows:

Three Year Funding Information:

<u>Fiscal Year</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>	<u>APC Percentage of Payroll</u>
2009*	\$ -	100%	-	0.000%
2010	200,484	100%	-	10.309%
2011	170,288	100%	-	10.309%

The Districts defined benefit pension plan was implemented in fiscal year 2010.

(8) 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	\$ 1,246,197	2,972,869	4,219,066
Capital assets – being depreciated, net	816,101	19,600,125	20,416,226
Long-term debt – current portion	-	(107,156)	(107,156)
Long-term debt – long-term portion	-	(2,703,288)	(2,703,288)
Total	<u>\$ 2,062,298</u>	<u>19,762,550</u>	<u>21,824,848</u>

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

(9) Unrestricted Net Assets

Net assets are designated as follows:	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Total</u>
Parks and recreation	\$ 3,182,388	-	3,182,388
Street lighting	-	-	-
Materials and supplies inventory	-	95,006	95,006
Prepaid expenses and other assets	1,459	143,236	144,695
Water operations and capital replacement	-	9,446,607	9,446,607
Total	<u>\$ 3,183,847</u>	<u>9,684,849</u>	<u>12,868,696</u>

(10) Fund Balance

Fund balances are presented in the following categories: nonspendable, restricted, committed, assigned, and unassigned (See Note 1.D.8 for a description of these categories). A detailed schedule of fund balances and their funding composition at June 30, 2011 is as follows:

<u>Fund Balance Category</u>	
Assigned:	
Compensated absences	\$ 10,252
Unassigned fund balance:	<u>3,053,971</u>
Total fund balance	<u>\$ 3,064,223</u>

(11) 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, 2011, 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.

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 coverage's.
- 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 \$2,000 deductible per occurrence.
- Boiler and machinery coverage for the replacement cost up to \$100 million per occurrence, subject to a \$1,000 deductible per occurrence.
- Public officials personal liability up to \$500,000 each occurrence, with an annual aggregate of \$500,000 per each elected/appointed official to which this coverage applies, subject to the terms, with no deductible per claim.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

(11) Risk Management, continued

- Workers' compensation insurance with statutory limits 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 2011 and 2010. 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, 2011 and 2010.

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

The Governmental Accounting Standards Board (GASB) has issued several pronouncements prior to June 30, 2011, that has effective dates that may impact future financial presentations.

Governmental Accounting Standards Board Statement No. 60

In November 2010, the GASB issued Statement No.60, *Accounting and Financial Reporting for Service Concession Arrangements*. This standard address how to account for and report service concession arrangements (SCAs), a type of public-private or public-public partnership that state and local governments are increasingly entering into. This statement is effective for financial statements for periods beginning after December 15, 2011. The impact of the implementation of this Statement to the District's financial statements has not been assessed at this time.

Governmental Accounting Standards Board Statement No. 61

In November 2010, the GASB issued Statement No.61, *The Financial Reporting Entity, Omnibus*. This standard is designed to improve financial reporting for governmental entities by amending the requirements of GASB Statement No. 14, *The Financial Reporting Entity*, and GASB Statement No. 34, *Basic Financial Statement and Management's Discussion and Analysis for State and local Governments*. This statement is effective for financial statements for periods beginning after December 15, 2011. The impact of the implementation of this Statement to the District's financial statements has not been assessed at this time.

Governmental Accounting Standards Board Statement No. 63

In June 2011, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. This standard is designed to improve financial reporting by standardizing the presentation of deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets. This statement is effective for financial statements for periods beginning after December 15, 2011. The impact of the implementation of this Statement to the District's financial statements has not been assessed at this time.

Governmental Accounting Standards Board Statement No. 64

In June 2011, the GASB issued Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions – an amendment of GASB Statement No. 53*. This standard is designed to improve financial reporting by clarifying the circumstances in which hedge accounting should continue when a swap counterparty, or swap counterparty's credit support provider, is replaced. This statement is effective for financial statements for periods beginning after December 15, 2011. The impact of the implementation of this Statement to the District's financial statements has not been assessed at this time.

Phelan Piñon Hills Community Services District
Notes to the Basic Financial Statements, continued
June 30, 2011

(13) 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.

Grant Awards

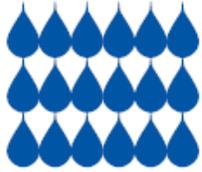
Grant funds received by the District are subject to audit by the grantor agencies. Such audit could lead to requests for reimbursements to the grantor agencies for expenditures disallowed under terms of the grant. Management of the District believes that such disallowances, if any, would not be significant.

(14) Subsequent Event

Events occurring after June 30, 2011 have been evaluated for possible adjustment to the financial statements or disclosure as of October 24, 2011, which is the date the financial statements were available to be issued.

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Report on Compliance and Internal Controls



Charles Z. Fedak, CPA, MBA
Paul J. Kaymark, CPA
Christopher J. Brown, CPA

Charles Z. Fedak & Company

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Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters 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, 2011, and have issued our report thereon dated October 24, 2011. 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 audits, 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 deficiency in internal control over financial reporting 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 and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, 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 grant agreements, 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 or other matters 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.

Charles Z. Fedak & Company CPAs - An Accountancy Corporation

Charles Z. Fedak and Company, CPA's – An Accountancy Corporation
Cypress, California
October 24, 2011