

FINANCIAL STATEMENTS
AND INDEPENDENT AUDITORS' REPORT



For the Years Ended December 31, 2012 and 2011

EGAN & EGAN
Certified Public Accountants

**KINNELOA IRRIGATION DISTRICT
FINANCIAL STATEMENTS
FOR THE YEARS ENDED
DECEMBER 31, 2012 AND 2011**

AND INDEPENDENT AUDITORS' REPORT

KINNELOA IRRIGATION DISTRICT
INDEX TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

	Page
Board of Directors and District Personnel	1
Management's Discussion and Analysis	2
Independent Auditors' Report	7
Balance Sheets	8
Statements of Revenues, Expenses and Changes in Net Assets, For the Years Ended December 31, 2012 and 2011	9
Statements of Cash Flows, For the Years Ended December 31, 2012 and 2011	10
Notes to Financial Statements	12
Supplementary Information	20

KINNELOA IRRIGATION DISTRICT
BOARD OF DIRECTORS AND DISTRICT PERSONNEL
DECEMBER 31, 2012 AND 2011

BOARD OF DIRECTORS

<u>NAME</u>	<u>OFFICE</u>	<u>TERM EXPIRES</u>
Gerrie G. Kilburn	Chair	2015
Richard L. Barkhurst	Treasurer	2013
Timothy Eldridge	Secretary	2015
Frank J. Griffith	Director	2013
Steven G. Sorell	Director	2015

MANAGEMENT PERSONNEL

Melvin Mathews	General Manager
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OFFICE PERSONNEL

Shirley Burt	Administrative Assistant
Bernadette Allen	Accounting Assistant

FIELD PERSONNEL

Chris Burt	Facilities Supervisor
Brian Fry	Facilities Operator
Chris Mellinger	Facilities Operator
Felix Galindo	Groundskeeper

KINNELOA IRRIGATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2012 AND 2011

Management's discussion and analysis of the financial performance of Kinneloa Irrigation District (the "District") provides an overview of the District's financial activities for the fiscal year ended December 31, 2012. Please read it in conjunction with the District's financial statements, which begin on page 8.

FINANCIAL HIGHLIGHTS

- The District's operating revenues, consisting primarily of water sales, increased by 7.6% to \$1,391,759 as compared to 2011 operating revenues of \$1,294,047. The increase is primarily due to additional wholesale water sales to the City of Pasadena in 2012.
- Total operating, maintenance, administrative and general expenses including depreciation increased by 4.9% to \$1,198,426 as compared to 2011 operating expenses of \$1,142,414. The increase is primarily due to higher expenses for maintenance and repairs, power, and the contractors who do leak repair and other projects for the District.

DESCRIPTION OF BASIC FINANCIAL STATEMENTS

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

DESCRIPTION OF OPERATIONS

The District provides water to 580 retail customers in a service area that includes a portion of the unincorporated Los Angeles County that is east of Altadena and an adjacent portion of the City of Pasadena. The District also sells excess groundwater when available to the City of Pasadena on a wholesale basis.

The District obtains its water from two vertical wells and five horizontal wells. These sources are sufficient to meet customer demand except in periods of extreme drought or other emergency. The District has five interconnections with the City of Pasadena municipal water system which allow either agency to supply water to the other agency under emergency conditions. Additionally, The District is a member of the Foothill Municipal Water District which supplies imported water from the Metropolitan Water District of Southern California to its member agencies.

More information about the Kinneloa Irrigation District can be found on the Internet at <http://www.kinneloairrigationdistrict.info>.

KINNELOA IRRIGATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2012 AND 2011

CONDENSED FINANCIAL INFORMATION

The following condensed financial information provides an overview of the District's financial activities for the year ended December 31, 2012 and 2011.

NET ASSETS

	<u>2012</u>	<u>2011</u>
Capital assets, net	\$4,221,215	\$4,434,303
Other assets, net	978,369	567,695
Total assets	<u>5,199,584</u>	<u>5,001,998</u>
Other liabilities	71,484	71,157
Total liabilities	<u>71,484</u>	<u>71,157</u>
Invested in capital assets, net of debt	4,221,215	4,434,303
Unrestricted	<u>906,885</u>	<u>496,538</u>
Total net assets	<u><u>\$5,128,100</u></u>	<u><u>\$4,930,841</u></u>

Capital and other assets – The change in capital and other assets is net of an increase in capital assets primarily due to completed projects.

Net assets – Unrestricted net assets increased primarily due to the net operating surplus for 2012. Unrestricted net assets consist of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt”.

KINNELOA IRRIGATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2012 AND 2011

CHANGES IN NET ASSETS

	<u>2012</u>	<u>2011</u>
Total operating revenues	\$ 1,391,759	1,294,047
Total non-operating revenues	<u>5,688</u>	<u>4,141</u>
Total revenues	1,397,447	1,298,188
Total operating expenses	<u>1,198,426</u>	<u>1,142,414</u>
Total non-operating expenses	<u>1,762</u>	<u>2,584</u>
Total expenses	<u>1,200,188</u>	<u>1,144,998</u>
Change in net assets	197,259	153,190
Net assets, beginning of year	<u>4,930,841</u>	<u>4,777,651</u>
Net assets, end of year	<u>\$ 5,128,100</u>	<u>4,930,841</u>

Revenues – Retail water sales by volume increased 11% to 685 acre-feet as compared to 615 acre-feet in 2011 and total operating revenue including the revenue from wholesale water sales increased by 7.6%.

The District also received \$3,671 in non-operating revenue from interest on its investments and \$2,017 in federal disaster assistance. The District's temporary investments at year end were \$838,987 and \$393,292 in 2012 and 2011, respectively. The increase is attributed to minimal expenditures for capital improvement projects in 2012 as compared to major capital improvement projects in 2011. The temporary investments provide an operating reserve and funds for planned future major capital improvement projects.

Expenses – The District's operating and maintenance expenses increased by \$44,854 in 2012 as compared to 2011. The increase is due primarily to greater expenditures for power, maintenance and repairs, and the contractors who do leak repair and other projects for the District. The District's administrative and general expenses increased by \$18,113 in 2012 as compared to 2011. Although many expenses decreased, the net increase is primarily due to the addition of one person to the administrative staff and an unexpected increase in permits and other fees.

KINNELOA IRRIGATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2012 AND 2011

BUDGET ANALYSIS AND VARIANCES

Revenue from retail and wholesale water sales for 2012 was \$1,391,759 as compared to the budgeted amount of \$1,121,000. The budgeted revenue was based on the actual amount from the previous year, adjusted for rate changes and/or expected new service connections for the year. Revenue from wholesale water sales was not budgeted for 2012. Since this source of revenue is considered discretionary and not predictable, the actual revenue allowed the District to exceed its overall revenue goal for 2012.

Overall, for 2012, the net revenue surplus before depreciation was \$452,412, as compared to the budgeted amount of \$134,091. Capital and planned maintenance projects in the amount of \$50,675 were completed as compared to the budgeted amount of \$117,181. A portion of the budgeted amount not spent in 2012 was carried over to future projects. The cash reserve at year end was \$838,987 as compared with the minimum target level of \$550,000 established by the Board. Each year the District budgets amounts for capital projects and planned maintenance projects based on its expected operations and available reserves. In 2012, the District completed several routine maintenance projects including purchase of replacement water meters; rebuilding of a booster pump; facility maintenance; electrical upgrades at several facilities; and improvements to the data acquisition and control system. The Board only approved routine maintenance projects such as these in order to build up the capital project reserve in anticipation of major pipeline and booster pump projects scheduled for 2013 and beyond.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets – At December 31, 2012 and 2011, the District had investments in land, buildings, wells and distribution systems, machinery and equipment, and construction in progress as follows:

	<u>2012</u>	<u>2011</u>
Land	\$ 96,700	96,700
Water rights	52,060	52,060
Buildings, wells and distribution system	6,529,271	6,525,057
Machinery and equipment	<u>738,705</u>	<u>716,128</u>
Totals	<u>\$ 7,416,736</u>	<u>7,389,945</u>

KINNELOA IRRIGATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2012 AND 2011

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

- Inflation as measured by the consumer price index for all urban consumers in the Los Angeles area was 2.0% for the 12 months ended December 2012.
- The general economic picture in 2013 is expected to reflect a continued slow recovery from the recent recession and there might be a continued loss of jobs and possible foreclosures in the service area. However, because water service is a basic necessity, these conditions would only lead to increased emphasis on conservation. This is consistent with the consumer message as the District strives to meet an expected 30% reduction in the ground water supply by July 2014 and achieve the "20% by 2020" water-use reduction mandate by the State of California.
- In order to build reserves to complete future high-priority capital and planned maintenance projects, the Board of Directors approved a budget for 2013 that maintains the net operating surplus at approximately the same level as 2012; reduces expenditures for current capital improvement and maintenance projects; and increases rates by an average of 10% in 2013. Additionally, wholesale water sales have been budgeted for 2013 to provide additional funds for future capital improvement projects. Although this revenue is not guaranteed, the District is confident from experience in prior years that its customer, the City of Pasadena, will purchase the water if the District does not need it for its own customers.
- Weather will continue to play a significant role in determining retail water sales for 2013. Fortunately, the District will likely have the option of selling surplus water to the City of Pasadena to offset any decline in retail sales due to higher than normal rainfall or greater conservation efforts. These factors when combined are anticipated to have a neutral effect on the District's operations in 2013. The District also has the flexibility to adjust expenditures for capital improvements and planned maintenance if necessary to meet the overall budget objectives for 2013.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our purveyors, customers, and creditors with a general overview of the District's finances and to show the District's accountability for the money it receives. If you have any questions about this report, or need additional financial information, contact the District's finance office at 1999 Kinclair Drive, Pasadena, CA 91107.

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INDEPENDENT AUDITORS' REPORT

The Board of Directors
Kinneloa Irrigation District
Pasadena, California

We have audited the accompanying balance sheets of Kinneloa Irrigation District (the "District") as of December 31, 2012 and 2011, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Kinneloa Irrigation District as of December 31, 2012 and 2011 and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying supplementary information presented on page 20 for the years ended December 31, 2012 and 2011 is presented for purposes of additional analysis and is not required as part of the basic financial statements. Such supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Egan & Egan

April 16, 2013

MEMBER OF THE AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

**KINNELOA IRRIGATION DISTRICT
BALANCE SHEETS
DECEMBER 31, 2012 AND 2011**

	<u>2012</u>	<u>2011</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 588,987	143,292
Cash, restricted as to use	250,000	250,000
Receivables		
Water sales, net of allowance for doubtful accounts	97,778	118,887
Other receivables	-	13,084
Prepaid expenses	21,604	22,432
Materials and supplies	<u>20,000</u>	<u>20,000</u>
Total current assets	978,369	567,695
Capital assets, net of accumulated depreciation	<u>4,221,215</u>	<u>4,434,303</u>
TOTAL ASSETS	<u>\$ 5,199,584</u>	<u>5,001,998</u>
LIABILITIES AND NET ASSETS		
Current liabilities		
Current portion of lease payable	\$ 18,979	18,118
Accounts payable and accrued expenses	36,227	17,664
Accrued payroll and payroll taxes	15,932	13,895
Customer deposits	<u>346</u>	<u>2,500</u>
Total current liabilities	71,484	52,177
Lease obligation, net of current portion	<u>-</u>	<u>18,980</u>
Total liabilities	71,484	71,157
Net assets		
Invested in capital assets, net of related debt	4,221,215	4,434,303
Unrestricted	<u>906,885</u>	<u>496,538</u>
Total net assets	<u>5,128,100</u>	<u>4,930,841</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 5,199,584</u>	<u>5,001,998</u>

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

**KINNELOA IRRIGATION DISTRICT
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011**

	<u>2012</u>	<u>2011</u>
Operating revenues		
Water sales and service fees	\$ <u>1,391,759</u>	<u>1,294,047</u>
Operating expenses		
Operating and maintenance	636,921	592,067
Administration and general	306,352	288,239
Depreciation	<u>255,153</u>	<u>262,108</u>
Total operating expenses	<u>1,198,426</u>	<u>1,142,414</u>
Operating income	<u>193,333</u>	<u>151,633</u>
Non-operating revenues (expenses)		
Interest	3,671	4,141
Interest expense	(1,762)	(2,584)
Federal disaster assistance	<u>2,017</u>	<u>-</u>
Total non-operating revenue	<u>3,926</u>	<u>1,557</u>
Change in net assets	197,259	153,190
Net assets, beginning of year	<u>4,930,841</u>	<u>4,777,651</u>
Net assets, end of year	<u>\$ <u>5,128,100</u></u>	<u><u>4,930,841</u></u>

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

**KINNELOA IRRIGATION DISTRICT
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011**

Cash flows from operating activities:	<u>2012</u>	<u>2011</u>
Cash received from customers	\$ 1,425,952	1,288,852
Cash payments to employees for services	(330,935)	(329,895)
Cash payments for services and goods	<u>(590,910)</u>	<u>(546,265)</u>
Net cash provided by operating activities	<u>504,107</u>	<u>412,692</u>
Cash flows from capital and related financing		
Cash paid for construction and acquisition of capital	(42,065)	(841,091)
Principal paid on lease obligation	(18,119)	(17,297)
Customer deposits	(2,154)	(20,850)
Federal disaster assistance	<u>2,017</u>	<u> </u>
Cash used by capital and related financing activities	<u>(60,321)</u>	<u>(879,238)</u>
Cash flows from investing activities:		
Interest received	3,671	4,141
Interest paid	<u>(1,762)</u>	<u>(2,584)</u>
Cash provided by investing activities	<u>1,909</u>	<u>1,557</u>
Net increase in cash and cash equivalents	445,695	(464,989)
Cash and temporary investments, beginning of the year	<u>393,292</u>	<u>858,281</u>
Cash and temporary investments, end of the year	<u>\$ 838,987</u>	<u>393,292</u>
SUMMARY OF BALANCE SHEET CASH and CASH EQUIVALENTS		
Cash	\$ 588,987	143,292
Temporary investments, restricted as to use	<u>250,000</u>	<u>250,000</u>
Total cash	<u>\$ 838,987</u>	<u>393,292</u>

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

**KINNELOA IRRIGATION DISTRICT
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011**

Reconciliation of operating income to net cash operating activities:	<u>2012</u>	<u>2011</u>
Operating income	\$ 193,333	151,633
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	255,153	262,108
Decrease (increase) in receivables	34,193	(5,195)
Decrease (increase) in prepaid expenses	828	6,299
(Decrease) increase in accounts payable and accrued expenses	<u>20,600</u>	<u>(2,153)</u>
Net cash provided by operating activities	<u>\$ 504,107</u>	<u>412,692</u>

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

KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

The District is governed by an elected Board of Directors. At December 31, 2012, the Board of Directors were as follows:

<u>Name</u>	<u>Title</u>
Gerrie G. Kilburn	Chair
Richard Barkhurst	Treasurer
Timothy Eldridge	Secretary
Frank J. Griffith	Director
Steven G. Sorell	Director

The accounting policies of the District conform to generally accepted accounting principles as applicable to governmental enterprise funds. The more significant policies reflected in the financial statements are summarized as follows:

a. Fund Accounting

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

b. Basis of Accounting

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

The District maintains its financial statements using accounting principles for Enterprise Funds.

KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

c. Utility Plant

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

	<u>Number of Years</u>
Water system	5 to 50
Autos and trucks	3 to 5
Office equipment	5 to 10
Office and production facilities	10 to 40

d. Restricted Assets

The Board of Directors has designated a portion of the District's cash and cash equivalents to be maintained for future capital improvements.

e. Uncollectible Accounts

The District's management estimates that accounts receivable are collectible. Unpaid water accounts receivable become a lien on the property and must be paid upon the sale of the property.

f. Cash and Cash Equivalents

The District defines cash and cash equivalents as demand account balances, cash on hand and money market accounts.

The District invests cash in excess of its operating requirements primarily with the State Treasurer's Local Agency Investment Fund (LAIF) and CalTrust, a money market account.

g. Materials and Supplies

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

h. Concentration of Credit Risk

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

i. Estimates

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

KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

j. Budgetary Process

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

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

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

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

k. Income Taxes

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

l. Compensated Absences

It is the District's policy to permit employees to accumulated paid time off for either vacation or illness in accordance with the limits expressed in its employee handbook. Upon termination, retirement or death of an employee, the District pays eligible accrued time in a lump-sum payment to the employee or beneficiary. Accumulated paid time off is recorded as an expense and a liability at the time the benefit is earned.

m. Operating Revenues and Expenses

Operating revenues, principally water sales, are charges for services resulting from exchange transactions associated with the principal activity of the District and billed monthly. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues result from nonexchange transactions or ancillary activities in which the District gives or receives value without directly receiving or giving equal value in exchange.

n. Property taxes

The Constitution of the State of California, Article 13A, limits the District's ability to levy taxes on property within the District. Taxes may be imposed upon the vote of a two-thirds vote of the qualified electors of the District. Such taxes would be limited for a specific purpose such as bond indebtedness or improvements to the water system.

o. Subsequent Events

The District has evaluated subsequent events through the date at which the financial statements were available to be issued. No material subsequent events required disclosure.

KINNELOA IRRIGATION DISTRICT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011

NOTE 2. CASH AND CASH EQUIVALENTS

At December 31, 2012 and 2011 cash and cash equivalents consist of:

	<u>2012</u>	<u>2011</u>
Insured with financial institutions	\$ 259,683	17,659
Local Agency Investment Fund ("LAIF")	117,931	117,498
Uninsured and uncollateralized	<u>461,373</u>	<u>258,135</u>
	<u>\$ 838,987</u>	<u>393,292</u>

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 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. 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 (such as LAIF).

The California Government Code and the District's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments, 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. California law also allows financial institutions to secure District deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits. Of the bank balances, up to \$250,000 is federally insured and the remaining balance is collateralized in accordance with the Code; however, the collateralized securities are not held in the District's name.

The District is a voluntary participant in LAIF, which is regulated by California Government Code under the oversight of the Treasurer of the State of California. The fair value of the District's investment in this pool is reported in the accompanying financial statements at amounts based upon the District's prorata share of the fair value provided by LAIF for the entire LAIF portfolio. The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis.

The District invests in CalTrust, a Joint Powers Authority established by public agencies in California for the purpose of pooling and investing local agency funds. A Board of Trustees, comprised of experienced investment officers and policy-makers of the members, supervises and administers the investment program of the Trust. CalTrust invests in fixed income securities eligible for investment pursuant to California Government Code. Investment in CalTrust accounts are uninsured and uncollateralized.

KINNELOA IRRIGATION DISTRICT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011

NOTE 2. CASH AND CASH EQUIVALENTS, continued

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. The District manages its exposure to interest rate risk by participating in LAIF. 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. The District does not believe a credit risk exists from its deposits with LAIF.

NOTE 3. CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2012 and 2011 was as follows:

2012				
	Balance January 1	Additions	Transfers	Balance December 31
Land	\$ 96,700			96,700
Water rights	52,060			52,060
Buildings, wells and distribution system	6,525,057	4,214		6,529,271
Machinery and equipment	716,128	22,577		738,705
	7,389,945	26,791		7,416,736
Less accumulated	(2,955,642)	(239,879)		(3,195,521)
Total capital assets	\$ 4,434,303	(213,088)		4,221,215
2011				
	Balance January 1	Additions	Transfers	Balance December 31
Land	\$ 96,700			96,700
Water rights	52,060			52,060
Buildings, wells and distribution system	5,725,081	782,901	17,075	6,525,057
Machinery and equipment	657,939	58,189		716,128
Construction in progress	17,075		(17,075)	-
	6,548,855	841,090		7,389,945
Less accumulated	(2,444,905)	(510,737)		(2,955,642)
Total capital assets	\$ 4,103,950	330,353		4,434,303

KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

NOTE 4. PENSION PLAN

Plan Description

The District contributes to the State of California Public Employees Retirement System ("PERS"), an agent multi-employer public employee defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. PERS acts as a common investment and administrative agent for participating public entities within the State of California. Benefit provisions and all other requirements are established by statute and city ordinance. Copies of PERS' annual financial report may be obtained from their offices or through their web site.

All full time employees are eligible to participate as members of PERS. Benefits vest after five years of service. District employees are eligible to retire upon attaining age 60. Annual retirement benefits are determined based upon the age at retirement, the length of membership service and the amount of earnings based upon the highest twelve consecutive months average.

Funding Policy

For the years ended December 31, 2012 and 2011, participants were required to contribute 7 % of their annual covered salary. The District is required to contribute at an actuarially determined rate. The contribution requirements of plan members and the District are established and may be amended by PERS.

Annual Pension Cost

Annual pension cost was 5.813% and 5.903% for the periods January 1, 2012 through June 30, 2102 and the period July 1, 2012 through December 31, 2012, respectively. The District made contributions of \$14,341 and \$13,076 for the years ended December 31, 2012 and 2011, respectively. The District does not have a Net Pension Obligation under current generally accepted accounting principles.

Actuarial Assumptions and Methods

The actuarial valuation is computed using the entry age normal actuarial cost method. The actuarial assumptions include: (a) an investment rate of return of 7.75% compounded annually, after June 30, 2012, the rate was 7% (b) projected annual salary increases that vary by duration of service, and (c) payroll cost-of-living adjustments of 3.25%. The rates used in (a) and (b) are compounded annually at 3%. The actuarial value of PERS assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a three-year period. Initial unfunded liabilities are amortized over a specific period that depends upon the plan's date of entry into PERS. Subsequent plan amendments are amortized as a level percentage of projected payroll over a closed 20-year period. The District does not have an unfunded liability.

KINNELOA IRRIGATION DISTRICT
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2012 AND 2011

NOTE 4 - PENSION PLAN, continued

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

<u>Dollars in 1,000; Zeros Omitted</u>						
<u>Valuation Date</u>	<u>Accrued Liabilities</u>	<u>Actuarial Assets</u>	<u>PERS Unfunded Liabilities (UL)</u>	<u>Funded Ratio %</u>	<u>Annual Covered Payroll</u>	<u>UL as a % & of Payroll</u>
06/30/11	896,216	850,298	45,918	94.9	234,453	19.6
06/30/10	624,423	467,904	29,932	74.9	186,778	16.0
06/30/09	582,842	553,954	28,888	95.0	184,320	15.7

NOTE 5. INSURANCE POOLS

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

To date, the District and its counsel are not aware of any material claims incurred through the period ended December 31, 2012 regarding these insurance plans. The District does not anticipate the need for a reserve for IBNR.

NOTE 6. NET ASSETS

The District is required to present the difference between assets and liabilities as net assets, not equity. Net assets are classified as either restricted, unrestricted or invested in capital assets, net of debt.

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

KINNELOA IRRIGATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

NOTE 6. NET ASSETS, continued

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

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

NOTE 7 - CONTINGENCIES

The District is the subject of certain claims and assessment arising in the normal course of its operations. Management of the District does not believe that the resolution of these matters will have a material adverse effect on the District's financial condition.

SUPPLEMENTARY INFORMATION

KINNELOA IRRIGATION DISTRICT
SCHEDULE OF OPERATING EXPENSES
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011

	<u>2012</u>	<u>2011</u>
Operating & Maintenance		
Power	\$ 103,626	89,764
Leased water rights	37,200	27,900
Labor	160,019	183,140
Engineering	9,116	13,953
Maintenance and repairs	56,164	31,437
Water analysis	21,178	19,542
Outside contractors	122,387	113,500
Truck maintenance and fuel	15,722	22,771
Insurance	66,971	71,277
Safety equipment	99	493
Water master	11,360	10,567
Capital improvement fees	3,002	(565)
Other	30,077	8,288
	<u> </u>	<u> </u>
	\$ <u>636,921</u>	<u>592,067</u>

Administrative and General		
Administrative salaries	\$ 124,931	120,053
Office labor	63,922	45,053
Payroll taxes	26,018	25,994
CalPERS retirement	14,341	13,076
Outside services	9,299	13,583
Legal fees	3,645	3,093
Professional dues	7,872	7,064
Board meetings	5,200	4,800
Office expense	19,588	24,662
Telephone	8,237	9,465
Accounting fees	6,200	6,200
Permits and operational fees	14,272	6,230
Information systems	2,827	8,966
	<u> </u>	<u> </u>
	\$ <u>306,352</u>	<u>288,239</u>