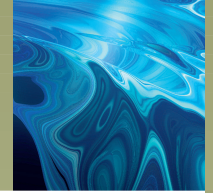


Independent Auditors' Report

**Mayer Hoffman McCann P.C.**

An Independent CPA Firm

Conrad Government Services Division

2301 Dupont Drive, Suite 200

Irvine, California 92612

949-474-2020 ph

949-263-5520 fx

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To the Honorable City Council and Board of Public Utilities
City of Riverside
Riverside, California

INDEPENDENT AUDITORS' REPORT

We have audited the accompanying financial statements of the City of Riverside, California, Water Utility, an enterprise fund of the City, as of and for the year ended June 30, 2007 as listed in the table of contents. These financial statements are the responsibility of the City of Riverside Water Utility's management. Our responsibility is to express an opinion on these financial statements based on our audits. The prior year partial comparative information has been derived from the financial statements of the Water Utility for the year ended June 30, 2006 and, in our report dated September 30, 2006, we expressed an unqualified opinion on those financial statements.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and 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.

As discussed in Note 1 to the financial statements, the financial statements of the City of Riverside, California, Water Utility are intended to present the financial position and the changes in financial position and cash flows for the City of Riverside, California, Water Utility, a fund of the City, and do not purport to, and do not, present fairly the financial position of the City of Riverside, California, and the changes in its financial position and its cash flows, where applicable, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Riverside, California, Water Utility, as of June 30, 2007 and the changes in its financial position and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

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To the Honorable City Council and Board of Public Utilities
City of Riverside

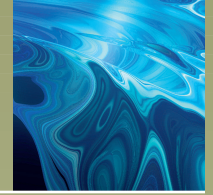
Our audits were conducted for the purpose of forming an opinion on the financial statements that comprise the City of Riverside, California, Water Utility's basic financial statements. The supplementary information entitled Water Key Historical Data, as listed in the table of contents, is presented for the purpose of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audits of the basic financial statements and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 12, 2007 on our consideration of the City of Riverside'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 considered in assessing the results of our audit.

Irvine, California

October 19, 2007

Management's Discussion and Analysis



As management of Riverside Public Utilities (a department of the City of Riverside), we offer the readers of Riverside's Water Utility financial statements, an enterprise fund of the City, this narrative overview and analysis of the financial activities of the Water Utility (Utility) for the fiscal years ended June 30, 2007 and 2006. We encourage readers to consider the information presented here in conjunction with additional information furnished in our financial statements, which begin on page 51 of this report. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

FINANCIAL HIGHLIGHTS

Fiscal years 2007 and 2006 reflected strong operating results for the Water Utility, with retail sales exceeding the previous year's results, primarily from an expanded customer base, increased consumption due to a prolonged summer heat wave, and the effects of rate increases.

- Retail sales, net of reserve/recovery were \$43,403 and \$34,301 for the years ended June 30, 2007 and 2006, respectively. The increase in sales was primarily due to recent rate increases to support the Water Utility's Water Master, Water Supply and Asset Management Plans.
- The assets of the Water Utility exceeded its liabilities (equity) at the close of fiscal years 2007 and 2006 by \$253,917 and \$228,880, respectively. Of this amount, \$39,707 and \$35,344, respectively, may be used to meet the Utility's ongoing obligations to creditors and customers.
- The Utility's total equity as of June 30, 2007 and 2006 increased by \$25,037 and \$29,397 from fiscal years ended June 30, 2007 and 2006, respectively.
- As of June 30, 2007 and 2006, unrestricted equity represented over 106% and 103% of annual operating expenses, respectively.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City of Riverside Water Utility financial statements. The Water Utility is a department of the City of Riverside, and its activities are recorded in a separate enterprise fund. These financial statements include only the activities for the City of Riverside Water Utility and provide comparative information for the last two fiscal years. Information on city-wide financial results is available in the City of Riverside's "Comprehensive Annual Financial Report."

The City of Riverside Water Utility's financial statements comprise two components: 1) financial statements, and 2) notes to the financial statements. In addition, this report also contains other supplementary information to provide the reader additional information about the Water Utility, including key historical operating and other relevant data.

Included as part of the financial statements are three separate statements, which collectively provide an indication of the Water Utility's financial health.

The **Balance Sheets** present information on assets and liabilities, with the difference between the two reported as equity. Over time, increases or decreases in equity may serve as a useful indicator of whether the financial condition of the Utility is improving or deteriorating.

The **Statements of Revenues, Expenses and Changes in Equity** present information showing how the Utility's equity changed during the most recent two fiscal years. Results of operations are reported as underlying events occur, regardless of the timing of cash flows. Thus, revenues and expenses are reported in these statements for some items that will result in cash flows in future fiscal periods, e.g., accounts payable and accounts receivable. This is called the accrual basis of accounting and is more fully described in the accompanying Notes to the Financial Statements.

The **Statements of Cash Flows** present the cash flow changes occurring during the last two fiscal years in highly liquid cash and cash equivalents, including certain restricted assets.

Management's Discussion and Analysis



The **Notes to the Financial Statements** provide additional information that is essential to a full understanding of the data provided in the Water Utility's financial statements. The notes to the financial statements can be found on pages 55 to 64 of this report.

UTILITY FINANCIAL ANALYSIS

As noted earlier, equity (also called net assets) may serve over time as a useful indicator of the fund's financial position. In the case of Riverside's Water Utility, assets exceeded liabilities by \$253,917 and \$228,880 at the close of the fiscal years 2007 and 2006, respectively.

The following table summarizes the Water Utility's financial condition as of June 30, 2007, 2006 and 2005:

CONDENSED STATEMENTS OF EQUITY (NET ASSETS)

	2007	2006	2005
Current and other assets	\$ 77,827	\$ 86,812	\$ 37,197
Capital assets	286,396	254,425	241,699
Total assets	364,223	341,237	278,896
Long-term debt outstanding	91,568	94,961	63,180
Other liabilities	18,738	17,396	16,233
Total liabilities	110,306	112,357	79,413
Invested in capital assets, net of related debt	200,832	180,708	175,041
Restricted	13,378	12,828	8,572
Unrestricted	39,707	35,344	15,870
Total equity (net assets)	\$ 253,917	\$ 228,880	\$ 199,483

Assets

Fiscal Year 2007 Total assets of \$364,223 reflect an increase of \$22,986 (6.7%), mainly due to the following:

- The increase in net capital assets (Utility plant) of \$31,971 is a result of significant expenses in the pipeline replacement program, system expansion and improvements, and the contribution of treatment facilities as discussed in the "Capital Assets and Debt Administration" section on page 48 to 49 of this report.
- Current and other assets reflect a net decrease of \$8,985 due to positive operating results and the use of bond proceeds and operating cash for construction projects and equipment. Restricted assets decreased by \$14,124 primarily due to a \$15,121 decrease in bond proceeds used for capital projects, offset by a \$516 increase in the Utility's Conservation and Reclamation Program assets. Unrestricted assets increased by \$5,139 largely from a \$6,362 increase in cash and cash equivalents from positive operating results, offset by a \$819 decrease in accounts receivable.

Fiscal Year 2006 Total assets of \$341,237 increased \$62,341 (22.4%), due to a \$12,726 increase in net capital assets (Utility plant), primarily relating to improvements to the Water Utility's distribution system and treatment facilities, and a \$49,615 increase in current and other assets. The \$49,615 is comprised of \$28,900 in restricted cash and investments (predominantly from \$34,400 in new bond proceeds offset by use of bond proceeds for construction projects), \$2,094 in accounts receivable, and \$17,854 in cash from operations, primarily relating to sales of excess water property.

Management's Discussion and Analysis



Liabilities

Fiscal Year 2007 The Utility's total liabilities were \$110,306, a decrease of \$2,051 (1.8%), due to the following:

- Long-term debt outstanding decreased by \$3,393 largely due to \$4,300 in principal repayments, offset by the amortization of deferred bond refunding costs, capital appreciation, and bond discounts.
- Other liabilities increased by \$1,342, primarily from a \$1,188 increase in accounts payable.

Fiscal Year 2006 The Water Utility's liabilities increased by \$32,944 (41.5%) to a total of \$112,357. Long-term obligations increased by \$31,781 principally due to \$61,125 Water Refunding/Revenue bond issue, offset by a \$26,598 deposit into a refunding escrow account and \$3,912 of principal payments.

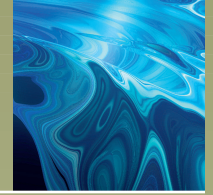
Equity (Net Assets)

Fiscal Year 2007 The Water Utility's equity, which represents the difference between the Utility's resources and its obligations, totaled \$253,917, an increase of \$25,037 (10.9%), comprised of the following:

- The largest portion of the Utility's equity is \$200,832 (79.1%), and reflects its investment in capital assets, such as treatment, pumping, source of supply, transmission and distribution facilities, less any related outstanding debt used to acquire those assets. This portion increased by \$20,124 (11.1%) over prior fiscal year due to the amount of capital assets constructed or purchased that are not bond financed. The Water Utility uses these capital assets to provide services to customers; consequently, these assets are not available for future spending. Resources needed to repay the outstanding debt shown on the Balance Sheets must come from other sources such as operations, since the capital assets themselves cannot be used to liquidate these long-term obligations. Additional capital asset information can be found in the "Capital Assets and Debt Administration" section.
- The restricted portion totaled \$13,378 (5.3% of total equity), and represents resources that are subject to internal and external restrictions on how they may be used. These are reserved for items such as debt repayment and funds collected for the Water Conservation and Reclamation programs. This portion increased by \$550 from prior fiscal year primarily due to Water Conservation and Reclamation program assets.
- The unrestricted portion totaled \$39,707 (15.6% of total equity), an increase of \$4,363, primarily attributable to positive operating results. This portion may be used to meet the Utility's ongoing obligations to creditors and customers.

Fiscal Year 2006 Total Water fund equity increased \$29,397 (14.7%) to a total of \$228,880. The portion of equity invested in capital assets, net of related debt, increased by \$5,667. The restricted portion increased by \$4,256, due to an increase in the required debt service reserve as a result of the \$61,125 bond issue. The unrestricted portion increased by \$19,474 primarily from positive operating results.

Management's Discussion and Analysis



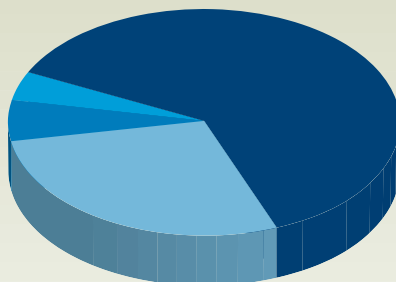
The Water Utility's overall increase in equity of \$25,037 and \$29,397 during fiscal years 2007 and 2006, respectively, due to positive operating results can be further explained in the following Condensed Statements of Changes in Equity:

CONDENSED STATEMENTS OF CHANGES IN EQUITY (NET ASSETS)

	2007	2006	2005
Revenues:			
Retail sales, net	\$ 43,403	\$ 34,301	\$ 30,754
Other revenues	4,491	19,708	5,066
Investment income	2,931	1,773	582
Capital contributions	20,074	16,511	11,826
Total revenues	70,899	72,293	48,228
Expenses:			
Operations and maintenance	23,449	21,514	20,129
Purchased energy and water	6,233	5,742	6,331
Depreciation	7,783	7,142	6,314
Interest expense and fiscal charges	4,469	4,959	3,812
Total expenses	41,934	39,357	36,586
Transfers to the City's general fund	(3,928)	(3,539)	(3,487)
Special item	-	-	(3,014)
Changes in equity	25,037	29,397	5,141
Equity, July 1	228,880	199,483	194,342
Equity, June 30	\$ 253,917	\$ 228,880	\$ 199,483

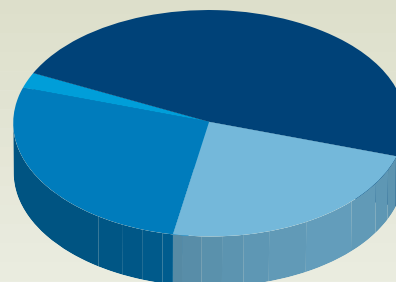
REVENUES BY SOURCES

June 30, 2007



- Retail Sales (62%)
- Capital Contributions (28%)
- Other (6%)
- Investment Income (4%)

June 30, 2006



- Retail Sales (48%)
- Capital Contributions (23%)
- Other (27%)
- Investment Income (2%)

Management's Discussion and Analysis



Fiscal Year 2007 Total revenues of \$70,899, decreased by \$1,394 (1.9%), due to the following major changes:

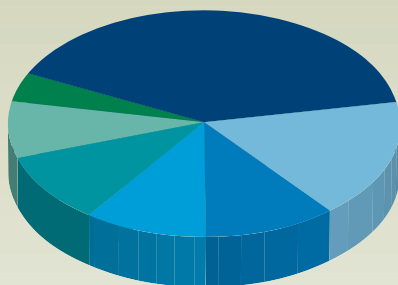
- Retail sales (residential, commercial, industrial, and other sales), net of reserve/recovery of \$43,403 was an increase of \$9,102 (26.5%) over the prior fiscal year. Retail sales continue to be the primary revenue source for the Water Utility, making up 61.2% of total revenues. The increase in retail sales is primarily due to an 8.5% rate increase that became effective June 1, 2006, a 12% increase that became effective November 1, 2006 as part of the SAFE W.A.T.E.R. Plan, and an 11.3% increase in retail consumption.
- Other revenues of \$4,491 decreased by \$15,217 (77.2%) predominantly due to \$15,384 received from the sale of surplus property in the previous fiscal year.
- Capital contributions were \$20,074 and reflect an increase of \$3,563 (21.6%), primarily due to a non-cash contribution of \$7,243 for treatment facilities from settlement agreements with parties responsible for contaminating the Water Utility's ground water resources, offset by a decrease of \$5,598 in construction projects funded by developers.
- Investment income of \$2,931 reflects an increase of \$1,158 (65.3%), due to an increase in operating cash resulting in increased interest earnings of \$726, and an overall net increase in the fair market value of investments of \$432.

Fiscal Year 2006 Total revenues of \$72,293, reflect an increase of \$24,065 (49.9%), with significant changes due to:

- Net retail sales were \$34,301, making up 47.4% of total revenues. Net retail sales increased \$3,547 (11.5%) due to an 8.5% rate increase that became effective June 1, 2005 and a 3.6% increase in consumption over prior year.
- Other revenues of \$19,708 increased by \$14,642 (289.0%) due to \$15,384 received from sales of surplus property.
- Capital contributions were \$16,511, an increase of \$4,685 (39.6%), reflecting a higher level of construction projects funded by developers.

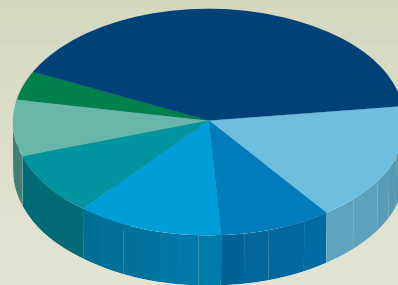
EXPENSES BY SOURCES

June 30, 2007



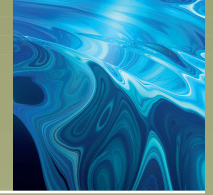
- Operations (40%)
- Depreciation (17%)
- Maintenance (11%)
- Interest Expense (10%)
- Purchased Energy (10%)
- Contributions to the City's General Fund (8%)
- Purchased Water (4%)

June 30, 2006



- Operations (41%)
- Depreciation (17%)
- Maintenance (9%)
- Interest Expense (12%)
- Purchased Energy (9%)
- Contributions to the City's General Fund (8%)
- Purchased Water (4%)

Management's Discussion and Analysis



Fiscal Year 2007 Total expenses were \$41,934, an increase of \$2,577 (6.5%), due to the items discussed below:

- Purchased energy and water costs of \$6,233 increased by \$491 (8.6%) due to a \$624 increase in the cost of electricity and gas necessary for operations, offset by a \$133 reduction in purchased water costs.
- Operations and maintenance costs were \$23,449, and reflected an increase of \$1,935 (9.0%), largely due to an increase in labor costs, professional service costs and maintenance expenses.

Fiscal Year 2006 Total expenses were \$39,357, reflecting a \$2,771 (7.6%) increase, due to higher interest expense as a result of a new revenue bond issue, increased costs for labor, taxes and assessments, offset by lower purchased water costs and charges for professional services.

Transfers

Transfers to the City's general fund are limited to a maximum of 11.5% of the prior year gross operating revenues by Section 1204(f) of the City Charter. The City uses these funds to help provide needed public services to the residents of the City, including police, fire, parks, libraries and other benefits.

Fiscal Year 2007 The Water Utility transferred the maximum allowable by the City Charter, or \$3,928, an increase of \$389, as a result of an increase in retail sales of \$3,547 for fiscal year 2006.

Fiscal Year 2006 Transfers to the City's general fund of \$3,539, increased by \$52, primarily the result of a \$391 increase in retail sales for fiscal year 2005.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Water Utility's investment in Capital Assets includes investments in source of supply, pumping, treatment, transmission and distribution facilities, and construction in progress, as well as general items such as office equipment, furniture, etc.

The following table summarizes the Utility's capital assets, net of depreciation as of June 30:

	2007	2006	2005
Source of supply	\$ 22,266	\$ 22,727	\$ 21,935
Pumping	7,641	7,918	4,714
Treatment	20,293	13,483	12,758
Transmission and distribution	195,557	190,708	173,732
General	3,680	3,066	3,352
Land	3,923	3,891	6,283
Intangible	5,969	5,969	6,269
Construction in progress	27,067	6,663	12,656
Total	\$ 286,396	\$ 254,425	\$ 241,699

Management's Discussion and Analysis



Fiscal Year 2007 The Water Utility's investment in capital assets, net of accumulated depreciation, was \$286,396, an increase of \$31,971 (12.6%). The increase resulted primarily from the following significant capital projects:

- \$11,279 for continued pipeline replacement programs.
- \$10,045 for system expansion and improvements including pump station replacements and facilities rehabilitation.
- \$7,243 from non-cash contributions for treatment facilities from settlement agreements with parties responsible for contaminating the Water Utility's ground water resources.

Fiscal Year 2006 Capital assets, net of depreciation, for the Water Utility increased \$12,726 (5.3%), for a total of \$254,425. Major capital projects included the following:

- \$10,700 related to the ongoing pipeline replacement program.
- \$5,300 related to system expansion and improvements to water facilities.

Additional information regarding capital assets can be found in Note 3 on Page 60 of this report.

Debt Administration

The following table summarizes outstanding long-term debt (revenue bonds) as of June 30:

	2007	2006	2005
Revenue bonds	\$ 99,515	\$ 103,815	\$ 71,015
Contracts payable	974	979	1,015
Less:			
Current portion	(4,505)	(4,450)	(4,225)
Unamortized deferred bond refunding costs	(2,510)	(2,587)	(504)
Unamortized capital appreciation	(1,629)	(2,487)	(3,499)
Unamortized bond discounts	(277)	(309)	(622)
Total	<u>\$ 91,568</u>	<u>\$ 94,961</u>	<u>\$ 63,180</u>

The Water Utility's bond indentures require the Utility to maintain a minimum debt service coverage ratio, as defined by the bond covenants, of 1.25. The Water Utility's debt service coverage ratio was 3.38, 5.11, and 2.85 at June 30, 2007, 2006 and 2005, respectively. The revenue bond debt is backed by the revenues of the Utility.

Fiscal Year 2007 Total long-term debt decreased by \$3,393 (3.6%) to a total of \$91,568, due to repayment of principal on outstanding revenue bonds and the amortization of deferred bond refunding costs, capital appreciation and bond discounts.

Fiscal Year 2006 Long-term debt of \$94,961 increased by \$31,781 (50.3%), due to the issuance of a \$61,125 variable rate Water Refunding/Revenue bond issue offset by the repayment of principal on the Water Utility's outstanding revenue bonds.

Additional information on the Water Utility's long-term debt can be found in Note 4 on pages 60 to 63 of this report.

Credit Ratings

The Water Utility maintains an "AA" credit rating from Standard & Poor's and Fitch, Inc. for its revenue bonds.



ECONOMIC FACTORS AND RATES

Although inflationary trends in the Riverside region continue to compare favorably to the national indices, the Water Utility's escalation in costs are not strictly attributable to inflation. One of the primary drivers of the increase in costs relates to the Water Utility's aging infrastructure.

To address this concern, in March 2006, the Board of Public Utilities, after the requisite public hearing, adopted and the City Council unanimously approved, the SAFE W.A.T.E.R. (Water Available to Everyone in Riverside) Plan. This plan implements system improvements contained in the Water Master, Water Supply and Asset Management Plans. The SAFE W.A.T.E.R. Plan is initially funded by a fifty-two percent, five-year water rate increase, consisting of a twelve percent and four-ten percent increases effective November 1, 2006, 2007, 2008, 2009, and 2010, respectively.

In addition to inflation, management continually plans for and identifies issues or potential contingencies that could impact future rates such as reclaimed water, infrastructure needs, system growth, source of supply, ground water contamination, stricter contaminant guidelines, legislative mandates, and others. In an effort to control costs to its customers, the Utility is aggressive in pursuing outside parties, and holding them responsible for any negative effects they may cause to Riverside's water quality.

Requests for Information

This financial report is designed to provide a general overview of the City of Riverside Water Utility's finances. Questions concerning any information provided in this report or requests for additional financial information should be addressed to the Assistant General Manager Finance/Customer Relations or the Utilities Assistant Chief Financial Officer, Riverside Public Utilities, 3901 Orange Street, Riverside, CA 92501. Additional financial information can also be obtained by visiting www.riversidepublicutilities.com.

Balance Sheets



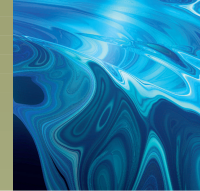
ASSETS	June 30, 2007	June 30, 2006
	(in thousands)	
UTILITY PLANT:		
Source of supply	\$ 32,822	\$ 32,684
Pumping	14,053	13,986
Treatment	22,697	15,449
Transmission and distribution	284,010	273,785
General	10,045	8,969
	<u>363,627</u>	<u>344,873</u>
Less accumulated depreciation	(114,190)	(106,971)
	<u>249,437</u>	<u>237,902</u>
Land	3,923	3,891
Intangible	5,969	5,969
Construction in progress	27,067	6,663
	<u>286,396</u>	<u>254,425</u>
RESTRICTED ASSETS:		
Cash and cash equivalents (Note 2)	4,475	4,424
Cash and investments at fiscal agent (Note 2)	17,982	32,673
	<u>22,457</u>	<u>37,097</u>
OTHER NON-CURRENT ASSETS:		
Deferred pension costs	5,838	5,876
Deferred bond issuance costs	1,003	1,067
Advances to the City's general fund	20	28
	<u>6,861</u>	<u>6,971</u>
Total non-current assets	<u>315,714</u>	<u>298,493</u>
CURRENT ASSETS:		
<i>Unrestricted:</i>		
Cash and cash equivalents (Note 2)	40,127	33,765
Accounts receivable, less allowance for doubtful accounts 2007 \$58; 2006 \$36	5,290	4,283
Accounts receivable, other utilities and governments, less allowance for doubtful accounts 2007 \$155; 2006 \$215	1,838	3,664
Accrued interest receivable	399	327
Prepaid expenses	2	368
	<u>47,656</u>	<u>42,407</u>
<i>Restricted assets:</i>		
Cash and cash equivalents (Note 2)	741	276
Conservation and Reclamation Programs Receivable	112	61
	<u>853</u>	<u>337</u>
Total current assets	<u>48,509</u>	<u>42,744</u>
Total assets	<u>\$ 364,223</u>	<u>\$ 341,237</u>

Balance Sheets



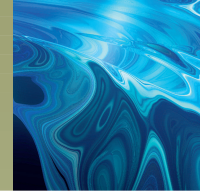
EQUITY AND LIABILITIES	June 30, 2007	June 30, 2006
	(in thousands)	
EQUITY:		
Invested in capital assets, net of related debt	\$ 200,832	\$ 180,708
Restricted for:		
Debt service (Note 5)	12,525	12,491
Conservation & Reclamation Programs	853	337
Unrestricted	39,707	35,344
Total equity	253,917	228,880
LONG-TERM OBLIGATIONS, LESS CURRENT PORTION (NOTE 4)	91,568	94,961
OTHER NON-CURRENT LIABILITIES:		
Pension obligation (Note 4)	5,761	5,823
Arbitrage liability	416	-
Total other non-current liabilities	6,177	5,823
CURRENT LIABILITIES PAYABLE FROM RESTRICTED ASSETS:		
Accrued interest payable	318	325
Current portion of long-term debt (Note 4)	4,355	4,300
Total current liabilities payable from restricted assets	4,673	4,625
CURRENT LIABILITIES:		
Accounts payable	4,436	3,248
Accrued liabilities	1,959	2,150
Current portion of long-term debt (Note 4)	150	150
Customer deposits	1,343	1,400
Total current liabilities	7,888	6,948
Total liabilities	110,306	112,357
COMMITMENTS AND CONTINGENCIES (NOTES 6 AND 7)	-	-
Total equity and liabilities	\$ 364,223	\$ 341,237

Statements of Revenues, Expenses and Changes in Equity



	For the Fiscal Years Ended June 30,	
	2007	2006
	(in thousands)	
OPERATING REVENUES:		
Residential sales	\$ 28,396	\$ 22,336
Commercial sales	13,255	10,470
Other sales	1,916	1,617
Wholesale sales	164	151
Conservation & Reclamation	737	434
Other operating revenue	2,602	2,598
	<hr/>	<hr/>
Total operating revenues before (reserve)/recovery	47,070	37,606
Reserve for uncollectible, net of bad debt recovery	(164)	(122)
	<hr/>	<hr/>
Total operating revenues, net of (reserve)/recovery	46,906	37,484
OPERATING EXPENSES:		
Operations	18,382	17,593
Maintenance	4,846	3,693
Purchased energy	4,534	3,910
Purchased water	1,699	1,832
Conservation & Reclamation Programs	221	228
Depreciation	7,783	7,142
	<hr/>	<hr/>
Total operating expenses	37,465	34,398
	<hr/>	<hr/>
Operating income	9,441	3,086
NON-OPERATING REVENUES (EXPENSES):		
Investment income	2,931	1,773
Interest expense and fiscal charges	(4,469)	(4,959)
Gain (loss) on sale of capital assets	(144)	12
Gain on sale of land	70	15,384
Other	1,062	1,129
	<hr/>	<hr/>
Total non-operating revenues (expenses)	(550)	13,339
	<hr/>	<hr/>
Income before contributions and transfers	8,891	16,425
	<hr/>	<hr/>
Capital contributions	20,074	16,511
Transfers out - contributions to the City's general fund	(3,928)	(3,539)
	<hr/>	<hr/>
Total capital contributions and transfers out	16,146	12,972
	<hr/>	<hr/>
Increase in equity	25,037	29,397
	<hr/>	<hr/>
EQUITY, BEGINNING OF YEAR	228,880	199,483
	<hr/>	<hr/>
EQUITY, END OF YEAR	\$ 253,917	\$ 228,880

Statements of Cash Flows



	For the Fiscal Years Ended June 30,	
	2007	2006
	(in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from customers and users	\$ 47,781	\$ 35,497
Cash paid to suppliers and employees	(28,445)	(26,476)
Other receipts	1,062	1,129
Net cash provided by operating activities	20,398	10,150
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES:		
Transfers out - contributions to the City's general fund	(3,928)	(3,539)
Principal paid on pension obligation bonds	(62)	(67)
Net cash used by non-capital financing activities	(3,990)	(3,606)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Purchase of utility plant	(25,469)	(17,167)
Proceeds from the sale of utility plant	103	18,327
Principal paid on long-term obligations	(4,305)	(3,912)
Interest paid on long-term obligations	(3,445)	(4,086)
Proceeds from the sale of revenue bonds, net of bond premium	-	61,824
Deposit to escrow account for advance bond refunding	-	(24,450)
Bond issuance cost	-	(2,940)
Capital contributions	5,611	10,878
Net cash provided (used) by capital and related financing activities	(27,505)	38,474
CASH FLOWS FROM INVESTING ACTIVITIES:		
Reduction in advances to the City's general fund	8	20
Purchases of investment securities	(430)	(3,589)
Income from investments	3,276	1,663
Net cash provided (used) by investing activities	2,854	(1,906)
Net increase (decrease) in cash and cash equivalents	(8,243)	43,112
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR (including \$29,327 and \$4,069 at June 30, 2006 and June 30, 2005, respectively, reported in restricted accounts)	63,092	19,980
CASH AND CASH EQUIVALENTS, END OF YEAR (including \$14,722 and \$29,327 at June 30, 2007 and June 30, 2006, respectively, reported in restricted accounts)	\$ 54,849	\$ 63,092
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	\$ 9,441	\$ 3,086
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	7,783	7,142
Amortization of deferred charges-pension costs	38	14
Increase (decrease) in allowance for uncollectible accounts	(38)	28
Decrease (increase) in accounts receivable	806	(2,172)
Decrease (increase) in prepaid expenses	366	(368)
Increase in accounts payable	1,188	1,133
Increase (decrease) in accrued liabilities	(191)	123
Increase (decrease) in customer deposits	(57)	35
Other receipts	1,062	1,129
Net cash provided by operating activities	\$ 20,398	\$ 10,150
SCHEDULE OF NON-CASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:		
Capital contributions - capital assets	14,463	5,633
Increase in fair value of investments	23	6

Notes to the Financial Statements



NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Water Utility exists under, and by virtue of, the City Charter enacted in 1883. The Water Utility is responsible for the production, transmission and distribution of water for sale in the City, except for certain areas served by another water utility.

BASIS OF ACCOUNTING

The Water Utility uses the accrual basis of accounting as required for enterprise funds with accounting principles generally accepted in the United States of America as applicable to governments. The accounting records of the Water Utility are also in conformity with the Uniform System of Accounts prescribed by the California Public Utilities Commission. The Water Utility is not subject to the regulations of the California Public Utilities Commission. The Water Utility is not required to and does not elect to implement the pronouncements of the Financial Accounting Standards Board issued after November 1989.

USE OF ESTIMATES

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

REVENUE RECOGNITION

Water Utility customers are billed monthly. Unbilled water service charges are recorded at year-end and are included in accounts receivable. Unbilled accounts receivable totaled \$2,732 at June 30, 2007, and \$2,553 at June 30, 2006.

An allowance for doubtful accounts is maintained for utility and miscellaneous accounts receivable. The balance in this account is adjusted at fiscal year-end to approximate the amount anticipated to be uncollectible.

UTILITY PLANT AND DEPRECIATION

Utility plant assets are valued at historical costs or estimated historical cost, if actual historical cost is not available. Costs include labor; materials; interest during construction; allocated indirect charges such as engineering, supervision, construction and transportation equipment, retirement plan contributions and other fringe benefits. Contributed plant assets are valued at estimated fair value on the date contributed. The cost of relatively minor replacements is included in maintenance expense.

Depreciation is recorded over the estimated useful lives of the related assets using the straight-line method. The estimated useful lives are as follows:

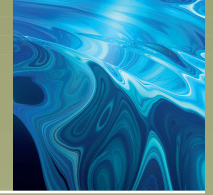
Supply, pumping and treatment plant.....	15-60 years
Transmission and distribution plant.....	25-50 years
General plant and equipment.....	3-50 years

RESTRICTED ASSETS

Proceeds of revenue bonds yet to be used for capital projects, as well as certain resources set aside for debt service, are classified as restricted assets on the Balance Sheets because their use is limited by applicable bond covenants.

In June 2004, the City began collecting a surcharge for water conservation and reclamation programs. This surcharge was approved by the City Council and was phased in over a three-year period with a 0.5%, 1.0% and 1.5% surcharge effective June 1, 2004, 2005 and 2006, respectively. The programs and services offered include conservation, education, and water use efficiency programs; programs to encourage the use of reclaimed water; research, development and demonstration programs to advance science and technology with respect to water conservation and reclamation; and water service provided to low-income customers. This surcharge is scheduled to be in effect for services rendered on or after June 1, 2004 through May 31, 2014. The activity associated with the surcharge for water conservation and reclamation programs is reflected in the accompanying financial statements on the Balance Sheets, Statements of Revenues, Expenses and Changes in Equity, and Statements of Cash Flows.

Notes to the Financial Statements



NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

CASH AND INVESTMENTS

In accordance with Water Utility policy, the Water Utility's cash and investments, except for cash and investments with fiscal agents, are invested in a pool managed by the Treasurer of the City. The Water Utility does not own specific, identifiable investments of the pool. The pooled interest earned is allocated monthly based on the month end cash balances.

The City values its cash and investments in accordance with provisions of Governmental Accounting Standards Board (GASB) Statement No. 31, "Accounting and Financial Reporting for Certain Investments and External Investment Pools (GASB 31)," which requires governmental entities, including governmental external investment pools, to report certain investments, at fair value in the Statements of Net Assets/Balance Sheets and recognize the corresponding change in the fair value of investments in the year in which the change occurred. Fair value is determined using published market prices.

Cash accounts of all funds are pooled for investment purposes to enhance safety and liquidity while maximizing interest earnings. Investments are stated at fair value.

City-wide information concerning cash and investments for the year ended June 30, 2007, including authorized investments, custodial credit risk, credit and interest rate risk for debt securities and concentration of investments, carrying amount and market value of deposits and investments may be found in the notes to the City's "Comprehensive Annual Financial Report."

CASH AND INVESTMENTS AT FISCAL AGENTS

Cash and investments maintained by fiscal agents are considered restricted by the Utility and are pledged as collateral for payment of principal and interest on outstanding bonds, or for use on construction of capital assets.

BOND DISCOUNTS, CAPITAL APPRECIATION, ISSUANCE COSTS, GAINS AND LOSSES ON REFUNDING

Bond discounts, capital appreciation, issuance costs and gains and losses on refunding are deferred and amortized over the term of the bonds using the effective interest method. Bond discounts, capital appreciation, and gains and losses on refunding are presented as a reduction of the face amount of bonds payable, whereas issuance costs are recorded as other assets. Capital appreciation is the annual increase in the value of bonds originally issued at a discounted amount. These bonds do not pay annual interest and mature at a pre-determined par value.

CUSTOMER DEPOSITS

The City holds customer deposits as security for the payment of utility bills. The Water Utility's portion of these deposits as of June 30, 2007 and 2006, respectively, was \$1,343 and \$1,400 (including \$969 and \$1,032, respectively, held on behalf of La Sierra Water Company pending dissolution and distribution of the remaining cash asset to shareholders, of which the City is the largest owner).

COMPENSATED ABSENCES

The accompanying financial statements include accruals for salaries, fringe benefits and compensated absences due employees at June 30, 2007 and 2006. The Water Utility treats compensated absences due employees as an expense and a current liability. The amount accrued for compensated absences was \$1,899 at June 30, 2007, and \$2,114 at June 30, 2006, and is included in accrued liabilities in the accompanying Balance Sheets.

Employees receive 10 to 25 vacation days per year based upon length of service. A maximum of two years vacation accrual may be accumulated and unused vacation is paid in cash upon separation.

Employees primarily receive one day of sick leave for each month of employment with unlimited accumulation. Upon retirement or death, certain employees or their estates receive a percentage of unused sick leave paid in a lump sum based on longevity.

Notes to the Financial Statements



NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

INSURANCE PROGRAMS

The Water Utility participates in a self-insurance program for worker's compensation and general liability coverage that is administered by the City. The Water Utility pays an amount to the City based on actuarial estimates of the amounts needed to fund prior and current year claims and incidents that have been incurred but not reported. The City maintains property insurance on most City property holdings, including Utility plant with a limit of \$100,000.

City-wide information concerning risks, insurance policy limits and deductibles and designation of general fund balance for risks for the year ended June 30, 2007, may be found in the notes to the City's "Comprehensive Annual Financial Report."

Although the ultimate amount of losses incurred through June 30, 2007, is dependent upon future developments, management believes that amounts paid to the City are sufficient to cover such losses. Premiums paid to the City by the Water Utility were \$219 and \$376 for the years ended June 30, 2007 and 2006, respectively. Any losses above the City's reserves would be covered through increased rates charged to the Water Utility in future years.

EMPLOYEE RETIREMENT PLAN

The City contributes to the California Public Employees Retirement System (PERS), an agent multiple-employer public employee retirement system that acts as a common investment and administrative agency for participating public entities within the State of California.

All permanent full-time and selected part-time employees are eligible for participation in PERS. Benefits vest after five years of service and are determined by a formula that considers the employee's age, years of service and salary. Employees may retire at age 55 and receive 2.7 percent of their highest annual salary for each year of service completed. PERS also provides death and disability benefits. These benefit provisions and all other requirements are established by state statute and City ordinance.

Employee contributions are 8.0 percent of their annual covered salary. The Water Utility is required to contribute the remaining amounts necessary to fund the benefits for its employees using the actuarial basis recommended by the PERS actuaries and actuarial consultants and adopted by the PERS Board of Administration. The employer portion of PERS funding as of June, 30 2007 and 2006, was 13.18 percent and 19.74 percent, respectively, of annual covered payroll. The Water Utility pays both the employee and employer contributions. The total Water Utility's contribution to PERS as of June 30, 2007 and 2006, was \$1,579 and \$1,539, respectively.

City-wide information concerning elements of the unfunded actuarial accrued liabilities, contributions to PERS for the fiscal year ended June 30, 2007, and recent trend information may be found in the notes to the City's "Comprehensive Annual Financial Report" for the fiscal year ended June 30, 2007.

PENSION OBLIGATION BONDS

In 2005, the City issued Pension Obligation Bonds in the amount of \$60,000, of which the Water Utility's share is \$5,890 as reflected in the accompanying Balance Sheet as deferred pension costs and a corresponding long-term obligation. The deferred charge relating to the net pension asset will be amortized over 19 years in accordance with the method used by CalPERS for calculating actuarial gains and losses. The Bonds will be used to fund the unfunded actuarial accrued liability for non-safety employees and the proceeds were deposited with CalPERS. The balance in deferred pension costs as of June 30, 2007 and 2006 was \$5,838 and \$5,876, respectively. For more discussion relating to the City's issue, see the notes to the City's "Comprehensive Annual Financial Report" for the fiscal year ended June 30, 2007.

ARBITRAGE LIABILITY

The Tax Reform Act of 1986 (the Act) requires the Water Utility to calculate and remit rebatable arbitrage earnings to the Internal Revenue Service. Certain debt and interest earnings on the proceeds of the Water Utility are subject to the requirements of the Act which contain yield restrictions on investment of proceeds from tax-exempt financing in higher yielding taxable securities. The balance in arbitrage liability as of June 30, 2007 was \$416.

Notes to the Financial Statements



NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

EQUITY

The Water Utility's equity consists of its net assets (assets less liabilities) which are classified into the following three components:

Invested in capital assets, net of related debt – this component consists of capital assets (net of accumulated depreciation) and unamortized debt expenses reduced by the outstanding balance of any bonds or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

Restricted – this component consists of net assets on which constraints are placed as to their use. Constraints include those imposed by creditors (such as through debt covenants), contributors, or laws or regulation of other governments or constraints imposed by law through constitutional provisions or through enabling legislation.

Unrestricted net assets – this component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

CONTRIBUTIONS TO THE CITY'S GENERAL FUND

Pursuant to the City Charter, the Water Utility may transfer up to 11.5 percent of its prior year's gross operating revenues to the City's general fund. In fiscal years 2006-07 and 2005-06, the Water Utility transferred 11.5 percent of gross operating revenues, or \$3,928 and \$3,539, respectively.

CASH AND CASH EQUIVALENTS

For the Statements of Cash Flows, cash and cash equivalents include all unrestricted and restricted highly liquid investments with original purchase maturities of three months or less, and all bond construction proceeds available for capital projects. Pooled cash and investments in the City's Treasury represent monies in a cash management pool. Such accounts are similar in nature to demand deposits, and are classified as cash equivalents for the purpose of presentation in the Statements of Cash Flows.

BUDGETS AND BUDGETARY ACCOUNTING

The Water Utility presents, and the City Council adopts, an annual budget. The proposed budget includes estimated expenses and forecasted revenues. The City Council adopts the Water Utility's budget in June each year via resolution.

RECLASSIFICATIONS

Certain reclassifications have been made to prior year's financial statements to conform with the current year's presentation.

PRIOR YEAR DATA

Selected information regarding the prior year has been included in the accompanying financial statements. This information has been included for comparison purposes only and does not represent a complete presentation in accordance with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the government's prior year financial statements, from which this selected financial data was derived.

Notes to the Financial Statements



NOTE 2. CASH AND INVESTMENTS

Cash and investments at June 30, 2007 and 2006, consist of the following (in thousands):

	June 30, 2007	June 30, 2006
	(Fair Value)	
Equity interest in City Treasurer's investment pool	\$ 45,343	\$ 38,465
Investments at fiscal agent	17,982	32,673
Total cash and investments	\$ 63,325	\$ 71,138
The amounts above are reflected in the accompanying financial statements as:		
	June 30, 2007	June 30, 2006
Unrestricted cash and cash equivalents	\$ 40,127	\$ 33,765
Restricted cash and cash equivalents	5,216	4,700
Restricted cash and investments at fiscal agent	17,982	32,673
Total cash and investments	\$ 63,325	\$ 71,138

Cash and investments distribution by maturities as of year end are as follows:

Investment Type	Total	Remaining Maturity (in Months)			
		12 Months or less	13 to 24 Months	25 to 60 Months	More than 60 Months
Held by fiscal agent					
Money market funds	\$ 107	\$ 107	\$ -	\$ -	\$ -
Federal agency securities	415	415	-	-	-
Investment contracts ¹	15,029	-	9,506	-	5,523
Commercial paper	2,431	-	-	2,431	-
City Treasurer's investment pool ²					
Money market funds	3,609	3,609	-	-	-
Federal agency securities	27,808	5,736	3,980	18,092	-
Corp medium term notes	2,270	-	2,270	-	-
State investment pool	11,656	11,656	-	-	-
Total	\$ 63,325	\$ 21,523	\$ 15,756	\$ 20,523	\$ 5,523

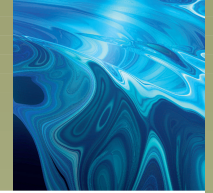
Presented below is the actual rating as of year end for each investment type:

Investment Type	Total	Rating as of Year End			
		AAA	Aa	A-1	Unrated
Held by fiscal agent					
Money market funds	\$ 107	\$ 107	\$ -	\$ -	\$ -
Federal agency securities	415	415	-	-	-
Investment contracts	15,029	15,029	-	-	-
Commercial paper	2,431	-	-	2,431	-
City Treasurer's investment pool ²					
Money market funds	3,609	-	-	-	3,609
Federal agency securities	27,808	27,808	-	-	-
Corp medium term notes	2,270	-	2,270	-	-
State investment pool	11,656	-	-	-	11,656
Total	\$ 63,325	\$ 43,359	\$ 2,270	\$ 2,431	\$ 15,265

¹ Amounts related to bond construction proceeds are invested in specific maturities but are available for construction of capital assets as funding is needed.

² Additional information on investment types and credit risk may be found in the City's "Comprehensive Annual Financial Report."

Notes to the Financial Statements



NOTE 3. UTILITY PLANT

The following is a summary of changes in utility plant during the fiscal years ended June 30, 2007 and 2006 (in thousands):

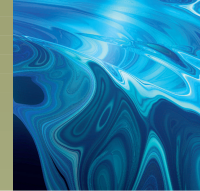
	Balance, As of 6/30/05	Additions	Retirements/ Transfers	Balance, As of 6/30/06	Additions	Retirements/ Transfers	Balance, As of 6/30/07
Source of supply	\$ 31,315	\$ 1,377	\$ (8)	\$ 32,684	\$ 138	\$ -	\$ 32,822
Pumping	10,515	3,471	-	13,986	67	-	14,053
Treatment	14,313	1,136	-	15,449	7,248	-	22,697
Transmission and distribution	251,583	22,374	(172)	273,785	10,873	(648)	284,010
General	8,977	234	(242)	8,969	1,210	(134)	10,045
Depreciable utility plant	316,703	28,592	(422)	344,873	19,536	(782)	363,627
Less accumulated depreciation:							
Source of supply	(9,380)	(587)	10	(9,957)	(595)	(4)	(10,556)
Pumping	(5,801)	(267)	-	(6,068)	(344)	-	(6,412)
Treatment	(1,555)	(411)	-	(1,966)	(438)	-	(2,404)
Transmission and distribution	(77,851)	(5,359)	133	(83,077)	(5,819)	443	(88,453)
General	(5,625)	(518)	240	(5,903)	(586)	124	(6,365)
Accumulated depreciation	(100,212)	(7,142)	383	(106,971)	(7,782)	563	(114,190)
Net depreciable utility plant	216,491	21,450	(39)	237,902	11,754	(219)	249,437
Land	6,283	221	(2,613)	3,891	35	(3)	3,923
Intangible	6,269	-	(300)	5,969	-	-	5,969
Construction in progress	12,656	22,831	(28,824)	6,663	24,294	(3,890)	27,067
Nondepreciable utility plant	25,208	23,052	(31,737)	16,523	24,329	(3,893)	36,959
Total utility plant	\$ 241,699	\$ 44,502	\$ (31,776)	\$ 254,425	\$ 36,083	\$ (4,112)	\$ 286,396

NOTE 4. LONG-TERM OBLIGATIONS

The following is a summary of changes in long-term obligations during the fiscal years ended June 30, 2007 and 2006 (in thousands):

	Balance, As of 6/30/05	Additions	Reductions	Balance, As of 6/30/06	Additions	Reductions	Balance, As of 6/30/07	Due Within One Year
Revenue bonds	\$ 66,390	\$ 58,854	\$ (26,812)	\$ 98,432	\$ -	\$ (3,333)	\$ 95,099	\$ 4,355
Pension obligation	5,890	-	(67)	5,823	-	(62)	5,761	79
Water stock acquisition rights	1,015	-	(36)	979	-	(5)	974	150
Arbitrage liability	-	-	-	-	416	-	416	-
Total long-term obligations	\$ 73,295	\$ 58,854	\$ (26,915)	\$ 105,234	\$ 416	\$ (3,400)	\$ 102,250	\$ 4,584

Notes to the Financial Statements



NOTE 4. LONG-TERM OBLIGATIONS (continued)

Long-term debt consists of the following (in thousands):

	June 30, 2007	June 30, 2006
Contracts Payable		
Water Stock Acquisitions: Payable on demand to various water companies	\$ 974	\$ 979
Total contracts payable	974	979
Revenue Bonds Payable		
\$69,840 1991 Water Revenue Bonds: \$25,900 serial capital appreciation bonds due in annual installments from \$3,235 to \$3,240 from October 1, 2007 through October 1, 2010, interest from 6.9 percent to 7.0 percent; (partially advance refunded in 1998)	12,950	16,185
\$30,965 1998 Water Refunding/Revenue Bonds: \$15,055 serial bonds due in annual installments from \$285 to \$3,690 through October 1, 2013, interest from 4.5 percent to 5.38 percent; \$10,155 term bonds due October 1, 2018, interest at 5.0 percent; \$5,755 term bonds due October 1, 2027; a portion of the serial and term bonds were advance refunded on September 20, 2005 with the 2005 Water Refunding/Revenue bonds	20,990	21,265
\$20,000 2001 Water Revenue Bonds: \$10,070 serial bonds due in annual installments from \$405 to \$585 through October 1, 2016, interest from 3.40 percent to 4.75 percent; \$4,345 term bonds due October 1, 2026, and \$5,585 term bonds due October 1, 2031 were advance refunded on September 20, 2005 with the 2005 Water Refunding/Revenue bonds	4,850	5,240
\$61,125 2005 Water Refunding/Revenue Bonds: \$61,125 Auction Rate Securities due in annual installments from \$425 to \$3,950 through October 1, 2035. Interest is variable and rate is subject to weekly repricing (rate at June 26, 2007 was 3.60 percent).	60,725	61,125
Total water revenue bonds payable	99,515	103,815
Total water revenue bonds and contracts payable	100,489	104,794
Unamortized deferred bond refunding costs	(2,510)	(2,587)
Unamortized capital appreciation	(1,629)	(2,487)
Unamortized bond discount	(277)	(309)
Total water revenue bonds and contracts payable, net of deferred bond refunding costs, capital appreciation and bond discount	96,073	99,411
Less current portion	(4,505)	(4,450)
Total long-term water revenue bonds and contracts payable	\$ 91,568	\$ 94,961

Notes to the Financial Statements



NOTE 4. LONG-TERM OBLIGATIONS (continued)

Annual debt service requirements to maturity, as of June 30, 2007, are as follows (in thousands):

	2008	2009	2010	2011	2012	2013-2017	2018-2022	2023-2027	2028-2032	2033-2036	Total
Principal	\$ 4,505	\$ 4,525	\$ 4,565	\$ 4,615	\$ 4,740	\$ 22,534	\$ 11,430	\$ 14,025	\$ 15,700	\$ 13,850	\$ 100,489
Interest	3,194	3,153	3,109	3,063	3,110	11,338	7,889	5,807	3,448	890	45,001
Total	\$ 7,699	\$ 7,678	\$ 7,674	\$ 7,678	\$ 7,850	\$ 33,872	\$ 19,319	\$ 19,832	\$ 19,148	\$ 14,740	\$ 145,490

ADVANCE REFUNDING

In prior years the Water Utility defeased certain Revenue Bonds by placing the proceeds of the new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Water Utility's financials statements. At fiscal year ended June 30, 2007, \$22,560 of bonds outstanding are considered defeased.

2005 WATER REFUNDING/REVENUE BONDS

On September 20, 2005, the Water Utility issued \$61,125 of Water Refunding/Revenue Bonds, in the form of Auction Rate Securities, to finance capital improvement programs and refund certain existing Water revenue bonds. \$30,000 of Water revenue bonds will be used to finance the costs of certain improvements to the City's Water System as part of the Capital Improvement Program. The remaining portion was used to refund all the outstanding 1994 FARECal bonds (\$3,425), \$7,705 of the outstanding 1998, and \$13,320 of the outstanding 2001 Water revenue bond issues. The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$2,271. This difference is being charged to operations using a proportional method. The City completed the current refunding to reduce net aggregate debt service payments over the next 26 years by \$3,663 and to obtain an economic gain (difference between present value of the old and new debt service payments) of \$2,303. Annual principal payments ranging from \$425 to \$3,950 are due from October 1, 2007 through October 1, 2035. Assuming a variable rate of 3.2%, the all-in true interest cost for this issue is 3.54%.

INTEREST RATE SWAPS ON REVENUE BONDS

Objective: As a means to lower borrowing costs, when compared against fixed-rate bonds at the time of issuance in September 2005, the City entered into interest rate swap agreements in connection with its \$61,125 2005 Water Refunding/Revenue Bonds. The intention of the swap was to effectively change the City's variable interest rate on the bonds to a synthetic fixed rate of 3.20% for the respective Water Refunding/Revenue Bonds.

Terms: Under the swaps, the City pays the counterparty a fixed payment as noted above and receives a variable payment computed as 62.68% of the London Interbank Offering Rate ("LIBOR") one month index plus 12 basis points. The swaps have notional amounts equal to the principal amounts stated above. Starting in fiscal year 2007, the notional value of the swaps and the principal amounts of the associated debt decline by \$400 to \$3,950 until the debt is completely retired in fiscal year 2036. The bonds' variable rate coupons are established on a weekly basis through the results of an auction process administered through an auction agent, termed Auction Rate Securities ("ARS").

Notes to the Financial Statements



NOTE 4. LONG-TERM OBLIGATIONS (continued)

The bonds and the related swap agreements for the 2005 Water Refunding/Revenue Bonds mature on October 1, 2035. As of June 30, 2007, rates were as follows:

Interest Rate Swap:	Terms	Rates
Fixed payment to counterparty	Fixed	3.20000%
Variable payment from counterparty	62.68 LIBOR + 12bps	(3.26362%)
Net interest rate swap payments		(0.06362%)
Variable-rate bond coupon payments	ARS	3.12994%
Synthetic interest on bonds		3.06632%

Fair value: As of June 30, 2007, in connection with all swap agreements, the transactions had a total positive fair value of \$3,371. Because the coupons on the City's variable-rate bonds adjust to changing interest rates, the bonds do not have a corresponding fair value decrease. The fair value was developed by a pricing service using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement of the swap.

Credit risk: As of June 30, 2007, the City was exposed to credit risk in the amount of \$3,371 because the swap had a positive value. The swap counterparty, Bear Stearns, was rated A+ by Standard & Poor's. To mitigate the potential for credit risk, if the counterparty's credit quality falls below A-, the fair value of the swap will be collateralized by the counterparty with U.S. Government securities. Collateral would be posted with a third-party custodian.

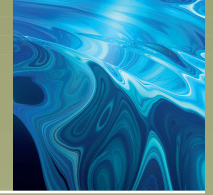
Basis risk: As noted above, the swaps expose the City to basis risk should the relationship between LIBOR and the auction-rate converge, changing the synthetic rate on the bonds. If a change occurs that results in the rates moving to convergence, the expected cost savings may not be realized.

Termination risk: The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. The Schedule to the Master Agreement includes an "additional termination event." That is, a swap may be terminated by the City if the counterparty's credit quality falls below "BBB-" as issued by Standard & Poor's. The City or the counterparty may terminate a swap if the other party fails to perform under the terms of the contract. If a swap is terminated, the variable-rate bond would no longer carry a synthetic interest rate. Also, if at the time of termination a swap has a negative fair value, the City would be liable to the counterparty for a payment equal to the swap's fair value.

Swap payments and associated debt: As of June 30, 2007, the debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same for their term, are summarized as follows. As rates vary, variable-rate bond interest payments and net swap payments will vary.

Fiscal Year Ending June 30,	Variable-Rate Bonds			
	Principal	Interest	Interest Rate Swaps, Net	Total
2008	\$ 425	\$ 1,887	\$ 38	\$ 2,350
2009	425	1,874	38	2,337
2010	425	1,861	37	2,323
2011	450	1,847	37	2,334
2012	800	1,821	37	2,658
2013-2017	4,075	8,714	176	12,965
2018-2022	10,550	7,563	153	18,266
2023-2027	14,025	5,533	112	19,670
2028-2032	15,700	3,208	65	18,973
2033-2036	13,850	726	15	14,591
Total	\$ 60,725	\$ 35,034	\$ 708	\$ 96,467

Notes to the Financial Statements



NOTE 5. RESTRICTED EQUITY

Pursuant to applicable bond indentures, a reserve for debt service has been established by restricting assets and reserving a portion of equity. Bond indentures for Riverside's water revenue bonds require reserves that equate to the maximum annual debt service required in future years plus three months interest and nine months principal due in the next fiscal year. The 2005 Refunding/Revenue bonds require 110% of the monthly accrued interest be included in the reserve. Additional reserves for the 1998 revenue bonds are not required due to the purchase of surety bonds to cover the reserve requirements.

NOTE 6. LITIGATION

The Water Utility is a defendant in various lawsuits arising in the normal course of business. Present lawsuits and other claims against the water utility are incidental to the ordinary course of operations of the Water Utility and are largely covered by the City's self-insurance program. In the opinion of management and the city attorney, such claims and litigation will not have a materially adverse effect upon the financial position or results of operation of the Water Utility.

The Water Utility is also a plaintiff in a lawsuit against the manufacturers and distributors of methyl tertiary-butyl ether (MTBE) and its by-products, and of fuel containing these chemicals, arising out of the threat to the Water Utility wells of contamination with those chemicals from leaking underground storage tanks.

The defendants removed this lawsuit to federal court and then transferred the case to the Judicial Panel on Multidistrict Litigation, New York, where it was consolidated with all other pending MTBE water contamination litigation cases in the country. The consolidated cases are in the discovery phase, with no trial date set.

The City also detected perchlorate in a number of its drinking water wells. While Lockheed Martin has not admitted liability for the presence of perchlorate in the City's wells, Lockheed Martin has agreed to pay for the design, construction, installation, rental and permitting, and to reimburse the City for its operational and maintenance costs associated with perchlorate treatment facilities on certain of the City's drinking water wells, under an agreement between the City and Lockheed Martin dated October 29, 2002 (the "Interim Perchlorate Agreement"). The Interim Perchlorate Agreement has been thrice amended, on November 25, 2003, on February 22, 2005, and on May 31, 2007, with each amendment increasing the number of wells from an original four wells to fourteen wells being treated for perchlorate at Lockheed Martin's expense.

NOTE 7. CONSTRUCTION COMMITMENTS

As of June 30, 2007, the Water Utility had major commitments of approximately \$19,276 with respect to unfinished capital projects, of which \$10,106 is expected to be funded by bonds, \$8,099 funded by other sources and \$1,071 funded by rates.

Key Historical Operating Data



WATER SUPPLY (ACRE FEET)	2006/2007	2005/2006	2004/2005	2003/2004	2002/2003
Pumping	85,299	76,605	73,732	81,797	70,977
Purchases	2,092	2,670	4,137	1,693	695
Total:	87,391	79,275	77,869	83,490	71,672
Percentage pumped	97.6%	96.6%	94.7%	98.0%	99.0%
System peak day (gallons)	109,200,000	118,782,000	112,094,000	105,029,000	101,484,000

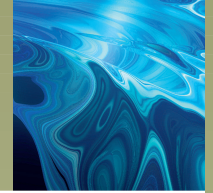
WATER USE	2006/2007	2005/2006	2004/2005	2003/2004	2002/2003
Number of meters as of year end					
Residential	57,666	57,308	56,916	56,254	55,376
Commercial/Industrial	5,279	5,204	5,114	4,932	4,782
Other	486	473	462	482	467
Total:	63,431	62,985	62,492	61,668	60,625
*CCF sales					
Residential	19,848,653	17,702,717	17,245,315	19,056,556	17,824,440
Commercial/Industrial	10,817,783	9,822,196	9,252,639	9,988,578	9,411,391
Other	1,243,927	1,157,130	1,199,448	1,361,809	995,815
Wholesale	199,845	182,987	177,851	189,377	1,052,205
Total:	32,110,208	28,865,030	27,875,253	30,596,320	29,283,851

*(CCF equals 100 cubic feet)

WATER FACTS	2006/2007	2005/2006	2004/2005	2003/2004	2002/2003
Average annual CCF per residential customer	345	312	308	342	324
Average price (\$/CCF) per residential customer	\$1.43	\$1.26	\$1.16	\$1.05	\$1.01
Debt service coverage ratio	3.38	5.11	2.85	3.52	2.60
Employees ¹	165	137	130	130	125

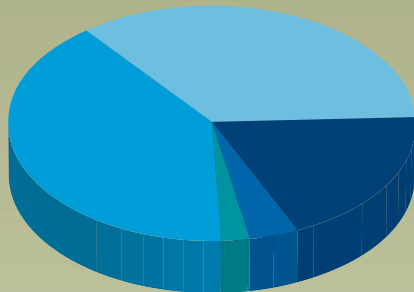
¹Approved positions

Key Historical Operating Data



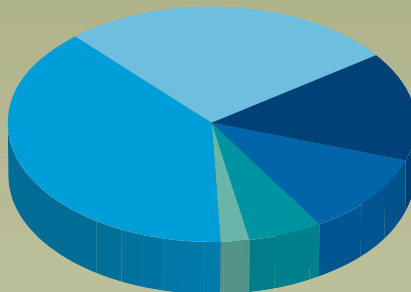
2006/2007 WATER REVENUE AND RESOURCES

Source of Revenue



- Residential Sales (40%)
- Other Revenues (35%)
- Commercial Sales (19%)
- Investment Income (4%)
- Other Sales (2%)

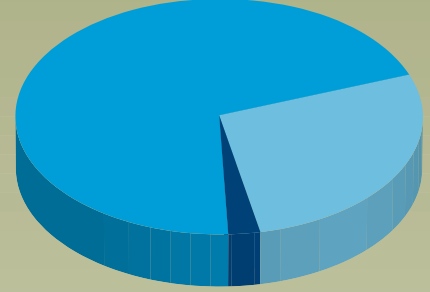
Distribution of Revenue



- Operations & Maintenance (39%)
- Additional Reserves (27%)
- Additions & Replacements to the System (15%)
- Debt Services (11%)
- Transfers to the City's general fund* (6%)
- Water Supply (2%)

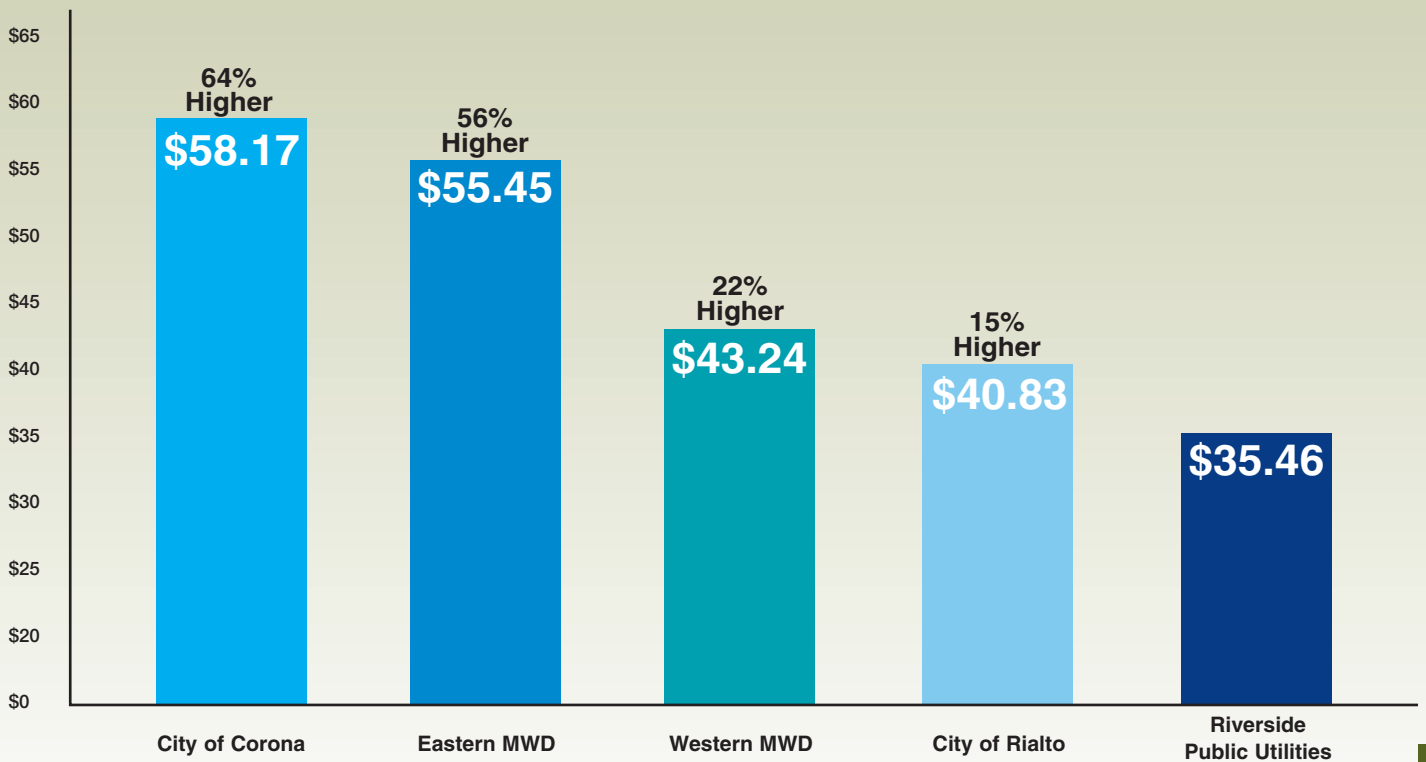
*Based on transfer of 11.5% of fiscal year 2005/2006 revenues

Water Resources



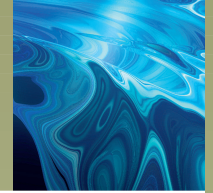
- San Bernardino Basin Wells (70.1%)
- Riverside Basin Wells (27.5%)
- Purchased Water (2.4%)

RESIDENTIAL WATER RATE COMPARISON - 27 CCF PER MONTH (AS OF JULY 1, 2007)



Water

Key Historical Operating Data



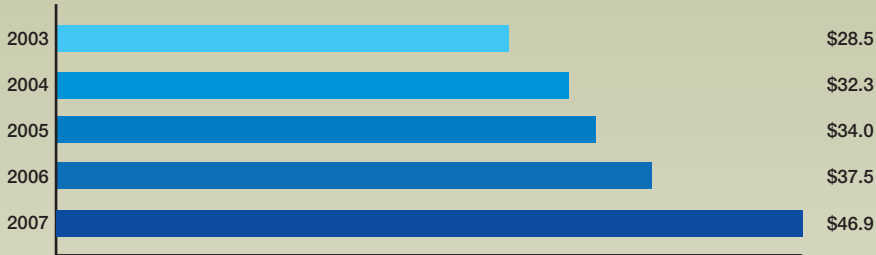
General Fund Transfer (in millions)



Number of Meters at Year End



Total Operating Revenue (in millions)



Production (in acre feet)



Peak Day Demand (in million gallons)



WATER FACTS AND SYSTEM DATA

Established	1913
Service Area Population	291,398
Service Area Size (square miles)	74.05
System Data:	
Smallest pipeline	2.0"
Largest pipeline	72.0"
Miles of pipeline	973
Number of domestic wells	49
Number of active reservoirs	16
Total reservoir capacity (gallons)	100,400,000
Number of treatment plants	10
Number of treatment vessels	98
Miles of canal	14
Number of fire hydrants	7,187
Daily average production (gallons)	75,927,063
2006-07 Peak day (gallons):	109,200,000
7/17/06 & 7/24/06	113 degrees
Historical peak (gallons):	118,782,000
8/9/05	99 degrees

BOND RATINGS

FITCH RATINGS	AA
STANDARD & POOR'S	AA