Semitropic Water Storage District

Combined Financial Statements

December 31, 2010 and 2009

C O N T E N T S

BARBICH HOOPER KING
DILL HOFFMAN
ACCOUNTANCY CORPORATION

Independent Auditors' Report

Board of Directors
Semitropic Water Storage District
Wasco, California

We have audited the accompanying statements of net assets of the Semitropic Water Storage District (District) as of December 31, 2010 and 2009, and the related statements of revenue, 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 and the standards applicable to the 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 audit provides 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 District as of December 31, 2010 and 2009, and the respective changes in net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards,* we have also issued our report dated June 17, 2011, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and 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 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.

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Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 2 through 10 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's financial statements as a whole. The supplementary information is presented for purposes of additional analysis and is not a required part of the financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of State, Local Governments, and Non-Profit Organizations,* and is also not a required part of the financial statements. The schedule of expenditures of federal awards is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole. The supplementary information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurances on it.

BARBICH HOOPER KING
DILL HOFFMAN
Accountancy Corporation

Barbich Hooper King

Bakersfield, California
June 17, 2011

The following discussion and analyses of Semitropic Water Storage District financial performance provides an overview of the financial activities for the fiscal years ended December 31, 2010 and 2009. This information is presented in conjunction with the basic audited financial statements and accompanying notes, which follow this section.

Financial Highlights

The District's total net assets increased $9.6 million or 7% over the course of the year's operations.

The District's total revenues experienced a net increase of $0.5 million or 1% during the calendar year ended December 31, 2010. The primary reason for the increase was small increases in the operating revenue of $0.3 million, or 1%, and nonoperating revenues of $0.2 million, or 3%. Although revenue in total for 2010 and 2009 are similar in amount, 2010 represents a water delivery year and 2009 represents a water recovery year.

The District's total expenses decreased $8.8 million, or 21%. The primary reason for the decrease was due to a reduction of operating expenses in the amount of $10.5 million, or 28%, during the calendar year ended December 31, 2010. The decrease in operating expenses was in primarily due to a reduction in transmission and distribution of $8.8 million, or 50%.

The District's capital assets increased $5 million, or 2%, during the calendar year ended December 31, 2010 primarily due to the completion of several projects within the District.

Overview of the Financial Statements

This annual report includes this management's discussion and analysis report, the independent auditor's report, the basic financial statements of the District and selected additional information. The financial statements also include notes that explain in more detail some of the information in the financial statements.

Required Financial Statements

The financial statements of the District report information of the District using accounting methods similar to those used by private sector companies. The financial statements conform to accounting principles which are generally accepted in the United States of America and utilize the accrual basis of accounting.

The Statement of Net Assets includes all of the District's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to District creditors (liabilities), with the difference between the two reported as net assets. This statement will indicate which assets are restricted due to contractual, Board action, or other commitments. This statement also provides the basis for assessing the liquidity, capital structure and financial flexibility of the District.

Revenues and expenses for each of the last two fiscal years are accounted for in the Statement of Revenues and Expenses and Changes in Net Assets. These statements measure the success of the District's operations and can be used to determine profitability, credit worthiness and whether the District has successfully recovered all its costs through user fees and other charges.

The Statement of Cash Flows reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. From this statement, information related to sources and uses of cash, and the change in cash balances can be compared for each of the last two fiscal years.

Financial Analysis of the District

The required financial statements, discussed above, assist the reader in making an assessment of whether its financial health is improving or deteriorating. However, one will need to consider other non-financial factors such as changes in economic conditions, population growth, and new or changed government legislation.

To begin our analysis, a summary of the District's Statements of Net Assets is presented in Table A.

Table A-1
Condensed Statements of Net Assets
December 31, 2010 and 2009
(000's)

	2010	*2009*	*Dollar Change*	*Percentage Change*
Current assets	$ 16.6	$ 15.6	$ 1.0	6%
Noncurrent capital assets	235.4	236.5	(1.1)	0%
Noncurrent other assets	49.8	48.8	1.0	2%
Total assets	301.8	300.9	0.9	0%
Current liabilities	8.5	12.7	(4.2)	-33%
Long-term debt	142.7	146.7	(4.0)	-3%
Total liabilities	151.2	159.4	(8.2)	-5%
Invested in capital assets,				
Net of related debt	88.6	78.5	10.1	13%
Restricted	10.9	10.8	0.1	1%
Unrestricted	51.1	52.2	(1.1)	-2%
Total net assets	150.6	141.5	9.1	6%
Total liabilities and net assets	$ 301.8	$ 300.9	$ 0.9	0%

As the Net Asset table above indicates, total assets increased by $1.1 million to $302 million at December 31, 2010, up from $300.9 million at December 31, 2009. The increase in the total assets of the District was primarily due to a net increase in accounts receivables $1.0 million and an increase in investments of $1.2 million, with a net total decrease in capital assets of $1.1 million, or 1%.

Total liabilities decreased by $8.5 million to $150.9 million at December 31, 2010, from $159.4 million at December 31, 2009. The decrease is primarily due to a reduction in accounts payable of $4.5 million, or 35%, and a decrease in long term debt $4.0, or 3%, was caused by the regularly scheduled debt payments.

Table B
Condensed Statements of Revenues and Expenses and Changes in Net Assets
Years Ended December 31, 2009 and 2008
(000's)

	2010	2009	Dollar Change	Percentage Change
Operating Revenues				
Contract water	$ 5.9	$ 3.7	$ 2.2	59%
Noncontract water	7.4	0.2	7.2	100%
Groundwater banking	18.0	25.6	(7.6)	-30%
Electrical transfer & hookup	1.3	3.3	(2.0)	-61%
Other revenue	1.0	3.5	(2.5)	-71%
Grant revenue	3.2	0.2	3.0	1500%
	36.8	36.5	0.3	1%
Nonoperating Income				
Interest income	0.3	0.4	(0.1)	-25%
GA & GP service charges	3.8	4.1	(0.3)	-7%
Prior year income, net	2.2	2.5	(0.3)	-12%
Earnings from investments	(0.1)	(0.6)	0.5	-83%
Other income	0.5	0.3	0.2	67%
	6.7	6.7	-	0%
Total Revenues	43.5	43.2	0.3	1%
Operating Expenses				
Source of supply	8.6	10.2	(1.6)	-16%
Well operations	0.6	0.9	(0.3)	0%
Transmission & distribution	8.9	17.7	(8.8)	-50%
General and administration	2.8	3.4	(0.6)	-18%
Depreciation expense	6.1	5.3	0.8	15%
	27.0	37.5	(10.5)	-28%
Nonoperating Expenses				
Interest expense	7.4	5.4	2.0	37%
	7.4	5.4	2.0	37%
Total Expenses	34.4	42.9	(8.5)	-20%
Change in Net Assets	9.1	0.3	8.8	2933%
Net Assets, beginning of year	141.5	141.2	0.3	0%
Net Assets, end of year	$ 150.6	$ 141.5	$ 9.1	6%

While the Statement of Net Assets shows the change in financial position of the District, the Statements of Revenues and Expenses and Changes in Net Assets provides answers as to the nature and source of these changes.

The District's total revenues increased by $0.5 million to $43.7 million during the calendar year ended December 31, 2010, from $43.2 million during the calendar year ended December 31, 2009. As mentioned before, 2010 was a water delivery year and 2009 was a water return year. Total revenues in 2010 increased slightly over total revenues in 2009, but the types of revenues were different. In 2010, contract water increased by $2.2 million, or 59%, due to a larger State allocation and noncontract water increased by $7.2 million, or 100%. Ground water banking decreased $7.6 million, or 30%, due to less energy used for delivered water, and other decreased $2.5 million, or 71%, as a result of other types of water not being such supplemental and emergency water. Not related to the water was a decrease in electrical transfers and hookups of $2.5 million, or 61%, and grant revenue increased by $3.0 million or 1500%. Total nonoperating revenues increased $0.2 million or 3%, this increase was from a combination of several line items and can be seen on the Combined Statements of Revenues and Expenses and Changes in Net Assets.

Total expenses decreased $10.5 million to $34.1 million during the year ended December 31, 2010 from $42.9 million during the year ended December 31, 2009. The decrease in expenses is primarily due to a reduction in energy charges associated with the return of water to banking partners and a reduction of water costs seen under source of supply of $1.6 million or 16%. in the year ended December 31, 2010.

As of December 31, 2010, the District had invested $302.9 million in capital assets as shown in Table C.

Table C
Capital Assets
December 31, 2010 and 2009
(000's)

	2010	2009	Dollar Change	Percentage Change
Land	$ 24.0	$ 23.8	$ 0.2	1%
Source of Supply	13.1	13.1	-	0%
Transmission and Distribution	238.3	233.8	4.5	2%
General Plant and Equipment	2.8	2.0	0.8	40%
Communication equip.	0.02	0.02	-	0%
Autos and trucks	1.5	1.4	0.1	7%
Office equip.	0.7	0.7	-	0%
Field and misc. equip.	0.4	0.4	-	0%
Well drilling equip.	3.0	3.0	-	0%
Wells	0.3	0.3	-	0%
Construction in progress	18.8	19.4	(0.6)	-3%
Total capital assets	302.9	297.9	5.0	2%
Less: accumulated depreciation	67.5	61.4	6.1	10%
Total net capital assets	$ 235.4	$ 236.5	$ (1.1)	0%

As can be seen from the table above, Total Gross Capital Assets increased $5 million to $302.9 million at December 31, 2010, from $297.9 million at December 31, 2009. The increase is primarily due to an increase in Distribution assets due to the completions of several small projects.

Management's Discussion and Analysis
Table D
Debt
December 31, 2010 and 2009
(000's)

	2010	2009	Dollar Change	Percentage Change
Revenue bonds	$ 128.1	$ 131.3	$ (3.2)	-2%
Swap	3.3	3.3	-	0%
Other debt	15.3	15.6	(0.3)	-2%
Total debt	$ 146.7	$ 150.2	$ (3.5)	-2%

Revenue bonds are legally secured by the District's water banking revenue and District's general project and administrative charges. If the water banking revenue stream pledged to specific revenue bond is not sufficient to repay debt, the District is not legally obligated to appropriate other funds for debt service payments toward the debt.

Other debt represents District obligations paid out of its general fund. The District has no general obligations bonds at this time.

Total Debt decreased $3.5 million to $146.7 million during the year ended December 31, 2010 down from $150.2 million during the year ended December 31, 2009. The decrease is primarily due to the normal pay down of debt during the year.

The District received an AA- rating by Standard & Poors for the 2010 fixed rate debt issued for to replace variable debt.

Budgetary Comparison

The following table is a comparison of the Board approved budget for 2010 against actual.

Table E
Budget vs. Actual Comparison
Year Ended December 31, 2010
(000's)

	Actual	Budget	Change	Percentage Change
Operating Revenues				
Contract water	$ 5.9	$ 4.2	$ 1.7	40%
Noncontract water	7.4	0.1	7.3	7300%
Groundwater banking	18.0	15.0	3.0	20%
Electrical transfer & hookup	1.3	2.9	(1.6)	-55%
Other revenue	1.0	4.7	(3.7)	-79%
Grant revenue	3.2	2.6	0.6	23%
	36.8	29.5	7.3	25%
Nonoperating Income				
Interest income	0.3	0.5	(0.2)	-40%
GA & GP service charges	3.8	3.8	-	0%
Prior year income, net	2.2	0.8	1.4	175%
Earnings from investments	(0.1)	-	(0.1)	100%
Other income	0.5	0.5	-	0%
	6.7	5.6	1.1	20%
Total Revenue	43.5	35.1	8.4	0.3
Operating Expenses				
Source of supply	8.6	9.1	(0.5)	-5%
Well operations	0.6	-	0.6	100%
Transmission & distribution	8.9	9.6	(0.7)	-7%
General and administration	2.8	8.3	(5.5)	-66%
Depreciation expense	6.1	5.6	0.5	9%
	27.0	32.6	(5.6)	-17%
Nonoperating Expenses				
Interest expense	7.4	7.0	0.4	6%
Change in Net Assets	9.1	(4.5)	13.6	-302%
Net Assets, beginning of year	141.5	141.5	-	0%
Net Assets, end of year	$ 150.6	$ 137.0	$ 13.6	10%

Contacting the District Management

This financial report is designed to provide our customers and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District at P.O. Box 8043, Wasco, CA 93280.

Semitropic Water Storage District

Combined Statements of Net Assets
December 31, 2010 and 2009

ASSETS	*2010*	*2009*
Current Assets		
Cash and cash equivalents	$ 4,928,796	$ 5,952,313
Receivables		
Accounts receivable, trade	5,562,019	4,248,730
Grant reimbursements receivable	1,017,069	229,757
Other receivables	1,254,289	1,842,785
Other receivables, related party	880,566	567,580
General administrative and general project service charges receivable	2,914,858	2,660,104
	11,628,801	9,548,956
Other prepaid expenses and deposits	82,294	96,310
Total current assets	16,639,891	15,597,579
Noncurrent Assets		
Restricted assets		
Cash	9,246,853	10,172,132
Investments	1,622,094	676,013
Total restricted assets	10,868,947	10,848,145
Capital assets		
Property, plant and equipment, at cost	302,845,506	297,899,099
Less accumulated depreciation	67,458,049	61,354,440
Total capital assets, net	235,387,457	236,544,659
Other noncurrent assets		
Banked water inventory	4,321,472	3,575,632
Investment in Semitropic-Rosamond Water Bank Authority	27,309,692	27,542,850
Investment in Kern Water Bank Authority	3,044,120	2,776,215
Investment in Pioneer Project	1,204,270	1,152,711
Investment in Cross Valley Canal Project	3,050,831	2,852,334
Total other noncurrent assets	38,930,385	37,899,742
Total noncurrent assets	285,186,789	285,292,546
	$ 301,826,680	$ 300,890,125

See Notes to Combined Financial Statements.

LIABILITIES AND NET ASSETS	*2010*	*2009*
Current Liabilities		
Current maturities of long-term debt	$ 3,996,066	$ 3,491,222
Trade accounts payable	744,216	3,116,494
Customer deposits payable	1,383,256	3,983,541
Accrued liabilities	2,316,676	2,051,371
Total current liabilities	8,440,214	12,642,628
Long-Term Debt, less discount and current maturities	142,748,476	146,738,159
Total Liabilities	151,188,690	159,380,787
Commitments and Contingencies (see Note 10)		
Net Assets		
Invested in capital assets, net of related debt	88,642,914	78,457,610
Restricted for:		
Debt service	10,789,513	10,789,135
Retirement trust fund	79,434	59,010
Construction of capital assets	-	-
Unrestricted	51,126,129	52,203,583
	150,637,990	141,509,338
	$ 301,826,680	$ 300,890,125

Semitropic Water Storage District

Combined Statements of Revenue and Expenses
For the Years Ended December 31, 2010 and 2009

	2010	2009
Operating revenue:		
Contract water	$ 5,908,146	$ 3,773,336
Noncontract water	7,441,195	169,861
Groundwater banking	18,035,134	25,571,318
Electrical transfer and hookup charges	1,318,346	3,312,298
Other charges	967,993	3,495,085
	33,670,814	36,321,898
Operating expenses:		
Transmission and distribution	8,991,633	17,720,107
Well operations	573,604	915,014
Source of supply	8,565,622	10,152,806
General and administrative	2,783,559	3,350,640
Depreciation expense	6,103,609	5,338,828
	27,018,027	37,477,395
Operating income (loss)	6,652,787	(1,155,497)
Nonoperating income (expense):		
Grant revenue	3,230,535	229,757
Interest income	319,367	426,881
General administrative and general project service income	3,834,914	4,144,218
Interest expense	(7,399,923)	(5,426,708)
Equity in loss from water bank investments	(169,921)	(661,411)
Other income	283,897	186,031
Prior year income, net	2,209,153	2,469,772
Rental income	180,322	71,224
Gain on sale of assets	-	1,400
Loss on sale of investments	(12,479)	(6,325)
	2,475,865	1,434,839
Change in net assets	$ 9,128,652	$ 279,342

Semitropic Water Storage District

Combined Statements of Changes in Net Assets
For the Years Ended December 31, 2010 and 2009

	Net Assets
Balance, December 31, 2008	$ 141,229,996
Change in net assets	279,342
Balance, December 31, 2009	141,509,338
Change in net assets	9,128,652
Balance, December 31, 2010	$ 150,637,990

See Notes to Combined Financial Statements.

Semitropic Water Storage District

Combined Statements of Cash Flows
For the Years Ended December 31, 2010 and 2009

	2010	2009
Cash flows from operating activities:		
Receipts from customers	$ 38,886,567	$ 51,855,442
Payments to suppliers for goods and services	(23,210,213)	(26,902,979)
Payments to employees for services	(3,155,766)	(3,194,578)
Net cash provided by operating activities	12,520,588	21,757,885
Cash flows from capital and related financing activities:		
Payment for acquisition and construction of property, plant and equipment	(4,946,407)	(23,718,738)
Cash paid for interest on bonds and construction loans	(7,356,942)	(5,215,313)
Receipts from grants	2,443,223	-
Payments made for bond issuance costs	-	(759,886)
Proceeds of refunding bonds	-	54,582,623
Payment for redemption of refunded bonds	-	(50,000,000)
Payments on long-term debt	(3,527,820)	(2,825,427)
Net cash used in capital and related financing activities	(13,387,946)	(27,936,741)
Cash flows from investing activities:		
Purchase of investments	(946,081)	(676,013)
Proceeds from sale of investments	-	97,000
Contribution to investment in Kern Water Bank Authority	(204,668)	(200,100)
Contribution to investment in Pioneer Project	(51,559)	(82,492)
Contribution to CVC	(198,497)	-
Interest income	319,367	426,881
Net cash used in investing activities	(1,081,438)	(434,724)
Net decrease in cash and cash equivalents	(1,948,796)	(6,613,580)
Cash and cash equivalents at beginning of the year	16,124,445	22,738,025
Cash and cash equivalents at the end of the year	$ 14,175,649	$ 16,124,445

See Notes to Combined Financial Statements.

	2010	2009
Reconciliation of operating income (loss) to net cash provided by operating activities:		
Operating income (loss)	$ 6,652,787	$ (925,740)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:		
Depreciation	6,103,609	5,338,828
(Gain) loss on sale of investments	(12,479)	6,325
Gain on sale of assets	-	(1,400)
General administrative & general project service charges	3,834,914	4,144,218
Prior year income, net	2,209,153	2,469,772
Other income	464,219	257,255
Changes in operating assets and liabilities:		
Receivables and general administrative and general project service charges receivable	(1,292,533)	15,303,787
Other prepaid expenses & deposits	14,016	52,172
Banked water inventory	(745,840)	379,649
Accounts payable and accrued liabilities	(4,707,258)	989,822
Unearned water banking revenue	-	(6,256,803)
Net cash provided by operating activities	$ 12,520,588	$ 21,757,885
Current unrestricted cash	$ 4,928,796	$ 5,952,313
Noncurrent restricted cash	9,246,853	10,172,132
	$ 14,175,649	$ 16,124,445
Noncash investing and investing activities:		
Equity in income (loss) from water bank investments	$ 63,237	$ (661,411)

Note 1. Nature of Activities and Summary of Significant Accounting Policies

Principles of combination:

The combined financial statements include the accounts of Semitropic Water Storage District, Buttonwillow Improvement District of the Semitropic Water Storage District, Pond-Poso Improvement District of the Semitropic Water Storage District, Semitropic Wildlife Improvement District of the Semitropic Water Storage District and Semitropic Improvement District of the Semitropic Water Storage District. Inter-district accounts have been eliminated.

Nature of District's activities:

Semitropic Water Storage District (the District) was formed on August 27, 1958. It began as an irrigation district for the purpose of securing State Water Project supplies to reduce groundwater overdraft. The District, a special district of the State of California, is one of eight water storage districts in California and is the largest in Kern County. The District is governed by a Board of Directors consisting of seven members who are elected by rate payers to serve four-year terms. Semitropic Improvement District has been appointed as agent to administer contracts on behalf of Buttonwillow Improvement District, Pond-Poso Improvement District, Semitropic Wildlife Improvement District and Semitropic Water Storage District.

The District's service area is comprised of approximately 221,000 acres or 345 square miles in the northwestern portion of Kern County. Since its inception, Buttonwillow Improvement District, Pond-Poso Improvement District, Semitropic Improvement District and Semitropic Wildlife Improvement District were created to help administer and manage the course of action and policies of Semitropic Water Storage District.

Although Buttonwillow Improvement District, Pond-Poso Improvement District, Semitropic Improvement District and Semitropic Wildlife Improvement District are a part of the Semitropic Water Storage District, they are operated and reported on as Semitropic Improvement District. As such, Semitropic Water Storage District is generally not liable for any contracts entered into or commitments made by them.

Significant accounting policies are as follows:

Financial reporting:

The District has adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. Statement No. 34 established standards for external financial reporting for all state and local governmental entities, which includes a statement of net assets, a statement of activities and changes in net assets, and a statement of cash flows. It requires the classification of net assets into three components - invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

Invested in capital assets, net of related debt - This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.

Restricted net assets - This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets - This component of net assets consists of net assets that do not meet the definition of "restricted assets" or "invested in capital assets, net of related debt."

The District's Board of Directors had designated certain reserves as a component of Unrestricted Net Assets. These balances are detailed as of December 31, 2010 and 2009:

	2010	***2009***
Capital projects reserve fund	$ -0-	$ -0-

The capital projects reserve fund was earmarked by the Board of Directors for capital improvements to meet system reliability and future demand in the District.

Principles of presentation:

The District, utilizing GASB Statement No. 20 for enterprise funds, has the option to consistently follow pronouncements issued by the Financial Accounting Standards Board (FASB) subsequent to November 30, 1989. Unless FASB standards are specifically adopted by GASB, the District has not elected to follow FASB standards issued after that date.

When the District has both unrestricted and restricted resources available for District purposes, it is the District's practice to first expend unrestricted resources, subsequently utilizing restricted resources as needed.

The District has implemented Governmental Accounting Standards Board No. 40 (GASB Statement No. 40), *Deposits and Investments Risk Disclosures - an Amendment of GASB Statement No. 3.* This statement addresses common deposit and investment risks related to credit risks, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest rate risk, this statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. Deposit and investment policies related to the risks identified in this statement also are required to be disclosed.

Fund accounting:

The District utilizes accounting for enterprise entities that account for operations (a) that are financed and operated in a manner similar to private business enterprises - where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or, (b) where the governing body has decided that periodic determination of revenue earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

Basis of accounting:

The accompanying financial statements have been prepared on the accrual basis of accounting, in conformity with the uniform system of accounts prescribed for water districts by the Controller of the State of California. Under the accrual basis, revenues are recognized when earned and expenses are recognized when incurred regardless of the timing of cash payments or receipts.

Revenue recognition:

The District has three primary sources of revenue. From its inception, the District has recognized revenue from the sale of surface irrigation water to water users located within the District for the purpose of halting the groundwater overdraft. The District's water rates are supported by an annual applied water cost analysis and are approved by the District's board on an annual basis. Water rates are not subject to regulation by the California Public Utilities Commission or by any other local, state or federal agency. Revenue from these sales is recognized on the accrual basis as water is delivered.

Beginning in 1995, the District entered into several groundwater banking relationships with its Banking Partners, customers who are mostly water districts located in California, using available space within the District's groundwater basin to store water during wet years (years when there is abundant rainfall and surplus water available), and pumping it back to the Banking Partners during dry years (years with little rainfall and no surplus water). The District primarily stores Banking Partners' water using in-lieu recharge, which stores water by utilizing surface water "in-lieu" of pumping groundwater, thereby storing an equal amount in the groundwater basin. The District is paid an annual fee for operating and maintaining the project and earns revenue on a per acre-foot basis at the time water is stored and when water is returned to the respective districts. The District also receives revenue toward energy reimbursement when water is returned. Revenue for groundwater banking is recognized in the period when annual fees are billed and when water is stored or returned for each respective Banking Partner.

Finally, the District receives revenue from general administrative and general project service charges for landowners receiving benefit from District services. These charges are established by the Board of Directors for the period January through December of each year and are levied to landowners within the District on their county property tax statements based on uniform rates per acre. For the years ended December 31, 2010 and 2009, $3,834,914 and $4,073,696, respectively, was earned by the District for general administrative and general project service charges. If available from District funds, the Board may authorize an end of the year discretionary payment in proportion to the general project service charge to the same district landowners. For the years ended December 31, 2010 and 2009, there was no end of the year discretionary payment authorized by the District. The net of these items is reported as nonoperating revenue to the District for the same January through December period.

Other sources of revenue include interest income and miscellaneous revenue which is comprised of water wheeling income, materials sales and electrical services.

Allowance for delinquency provision:

In prior years, the allowance for delinquency provision for general administrative and general project service charges has been based on a percentage of assessments levied. The percentage is determined by collections from previous years. As of December 31, 2010, the District's management decided an allowance for delinquency provision for general administrative and general project service charges was not necessary.

Accounts receivable, trade:

Trade accounts receivable are stated at the amount management expects to collect from balances outstanding at year-end. Based on management's assessment of the credit history with customers having outstanding balances and current relationships with them, it has concluded that realization losses on balances outstanding at year-end will be immaterial; accordingly, no allowance for doubtful accounts is required.

Concentration of credit risk:

Credit is extended, in the form of accounts receivable, to landowners who are located in the District's service area.

Property, plant and equipment:

The District's property, plant and equipment are recorded at cost. Assets are capitalized when the cost is greater than $5,000 and the asset has a useful life greater than two years. Depreciation is computed using the straight-line method over the following estimated useful lives:

	Years
Source of supply	15-60
Transmission and distribution	15-60
General plant and equipment	3-60
Communication equipment	5-60
Autos and trucks	5
Office equipment	3-10
Field and misc. equipment	5-10
Well drilling equipment	15-60
Wells	15-20

Maintenance and repairs of property, plant and equipment are charged to operations and major improvements are capitalized. Upon retirement, sale or other disposition of property, plant and equipment, the cost and accumulated depreciation are eliminated from the accounts and gain or loss is included in operations.

Deposits and investments

Cash and cash equivalents:

The District considers cash equivalents to be all highly liquid debt instruments purchased with a maturity of three months or less. At December 31, 2010 and 2009, cash and cash equivalents include cash on hand and amounts deposited with banks, the County of Kern Treasurer and the State Treasurer's office.

The District invests any excess funds not needed for immediate needs into State of California managed Local Agency Investment Fund (LAIF), which is a permitted investment by both State law and the District’s investment policy. Created by state statute, the LAIF is a component of a pooled money program that is administered by the State Treasurer’s Office. The fund has regulatory oversight from the Local Investment Advisory Board, which is comprised of the State Treasurer as chair, the State Controller, and the Director of Finance. As the LAIF does not make share-value adjustments due to immaterial differences between fair value and cost, the District’s cost basis in the fund is reflected in cash and cash equivalents on the Combined Statements of Net Assets as of December 31, 2010 and 2009.

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 and 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.

Deposits with financial institutions:

Cash funds deposited with the State Treasurer's office are in a pooled money fund. Funds are pooled with other agencies throughout California. Investments are made in accordance with Government Code Sections 16430 and 16480. Cash funds are also deposited with the County of Kern's Local Agency Investment Fund (LAIF) and are appropriately collateralized by cash, investments and securities.

Pooled funds may be invested in: (1) direct obligations of the United States government, the payment of which the full faith and credit of the United States government is pledged, (2) certificates of deposit at savings and loan associations and federally insured banks when secured by acceptable collateral and, (3) savings accounts at savings and loan associations and banks, to the extent fully insured.

As a government agency, the California Government Code dictates guidelines toward the District’s investments in addition to the District’s investment policy, which has been approved by the Board of Directors. This policy provides the District’s treasurer with investment authority, summarizes authorized investments, and describes the District’s procedures and other limitations. The objective of the District’s investment policy is to maximize the yield of invested funds while assuring that investments are safe from loss, utilizing the “prudent person” policy of safety, legality and yield.

Below is a summary of the District’s cash and investment policies, credit risk and description of the District’s cash and investments. Separate internal accounts or funds have been created by the District to provide for specific events in accordance with bond covenants, trust agreements or certain regulations. These “restricted” accounts may have minimum balance requirements. The primary restrictions for these accounts are due to construction of capital assets, reserves for principal and interest on outstanding bonds and payments of the District's 401(k) and payroll obligations. All remaining cash and investments are unrestricted.

Cash and investments as of December 31, 2010 and 2009 are classified in the accompanying combined financial statements as follows:

	2010	2009
Current assets - cash	$ 4,928,796	$ 5,952,313
Noncurrent assets - restricted cash	9,246,853	10,172,132
Noncurrent assets - restricted investments	1,622,094	676,013
	$ 15,797,743	$ 16,800,458

Cash and investments as of December 31, 2010 and 2009 consisted of the following:

	2010	2009
Cash deposits	$ 8,058,682	$ 8,820,747
Deposits with Kern County	1,446,119	1,426,407
Deposits with LAIF	4,670,848	5,877,291
Investments	1,622,094	676,013
	$ 15,797,743	$ 16,800,458

Investments:

The District is permitted by both Board policy and State law to invest in various authorized investments, subject to a variety of limits and controls, including State of California bonds, U.S. Government Agency securities (Treasury and other federal agencies) and other securities (bankers' acceptances, negotiable certificates of deposit, etc.). The District investment portfolio is primarily comprised of holdings in Federal agency securities and U.S. Guarantees - GNMA's.

Disclosures relating to interest rate risk and credit risk:

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the District manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

Generally, 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. Presented below is the minimum rating required by the California Government Code, the District's investment policy, or debt agreement and the actual rating as of year-end for each investment type.

The minimum legal rating for the U.S. Government Agency Securities is A. The ratings for the District's U.S. Government Agency Securities at December 31, 2010 and 2009 are AAA.

As of December 31, 2010, the District had the following investments and maturities:

		Investment maturities		
	Fair Value	***Less Than 1 Year***	***1 Year to 5 Years***	***6 Years to 10 Years***
U.S. Govt. Agency Securities	$ 1,622,094	$ 1,622,094	$ -	$ -

As of December 31, 2009, the District had the following investments and maturities:

		Investment maturities		
	Fair Value	***Less Than 1 Year***	***1 Year to 5 Years***	***6 Years to 10 Years***
U.S. Govt. Agency Securities	$ 676,013	$ 676,013	$ -	$ -

Investment in Kern Water Bank Authority:

Upon adoption of the Monterey Agreement in 1997, the District obtained a 6.67% interest in Kern Water Bank Authority (KWBA) by reducing the District's annual entitlement water from 158,000 acre-feet to 155,000 acre-feet. This District is able to store water at the KWBA in wet years and draw water in dry years. The District's investment in Kern Water Bank Authority is accounted for using the equity method. Under this method, the District recognizes its share of the Authority's accrual basis income or loss. The District's equity in the earnings from this investment for the years ended December 31, 2010 and 2009 was $63,237 and $181,712, respectively. The earnings from this investment are included in nonoperating revenue on the combined statements of revenue and expenses.

The District paid for the construction of wells during the year ended December 31, 2009, for a total cost of $200,100.

Investment in Pioneer Project:

The Pioneer Project utilizes land that the Kern County Water Agency owns. The Pioneer Project Participation Agreement stipulates that certain member units have first priority utilizing the property for recharge and recovery. Recharge Participants are entitled to a first priority right of the stated recharge facilities, and Recovery Participants are entitled to a first priority right of the stated recovery facilities. The District is a Recovery Participant with a 14% allocation among this class of participants.

The District's investment in the Pioneer Project is accounted for using the equity method. Under this method, the District recognizes its share of the project's accrual basis income or loss.

The District paid for the construction of three wells for this project during the years ended December 31, 2010 and 2009, for a total cost of wells of $51,559 and $389,347, respectively.

Investment in Cross Valley Canal Project:

The Cross Valley Canal (CVC) serves as the Kern County Water Agency's primary conduit for water deliveries to and from the California Aqueduct. Construction has commenced on the CVC Expansion Project. The project is the largest component of the Phase II Grant Program and includes construction of the CVC/Friant-Kern Canal Intertie (Intertie). During 2009, the CVC conveyance capacity was expanded from 922 cubic feet per second (cfs) to 1,422 cfs (an increase of about 54 percent), plus an additional 500 cfs of capacity in the Intertie.

The District's investment in the Cross Valley Canal Project is accounted for using the equity method. Under this method, the District recognizes its share of the project's accrual basis income or loss.

The District made an additional capital contribution during the year ended December 31, 2010, for construction and engineering costs of $198,497.

Investment in Semitropic-Rosamond Water Bank Authority:

On July 28, 2008, the District entered into a Joint Powers Agreement with Valley Mutual Water Company, LLC, and Rosamond Community Service District to create the Semitropic-Rosamond Water Bank Authority (SRWBA).

Initially, the SRWBA is to consist of a "First Priority Right" to the following interests in the District's Stored Water Recovery Unit (SWRU) banking project that will provide: (1) 33,333 AF/year of SWRU Delivery Capacity, (2) 300,000 AF of SWRU Storage Capacity, and (3) 100,000 AF/year of SWRU Recovery and Return Capacity, together with rights to certain unused capacities in the SWRU and other elements of the Semitropic Water Bank, and the following rights in the Antelope Valley Water Bank (AVWB): (1) 100,000 AF/year of AVWB Delivery Capacity, (2) 500,000 AF of AVWB Storage Capacity, and (3) 100,000 AF/year of AVWB Recovery and Return Capacity.

As part of the agreement, the District recorded an investment in the amount of $20,000,000, which represents the District's equity ownership in the SWRBA. The District's investment in the SRWBA is accounted for using the equity method. Under this method, the District recognizes its share of the SRWBA's accrual basis income or loss. The District's equity in income (loss) from this investment for the years ended December 31, 2010 and 2009 was $(233,159) and $(843,123), respectively. The earnings from this investment are included in the nonoperating revenue category on the combined statements of revenue and expenses.

Cash flows:

Governmental Accounting Standards Board No. 9 states for purposes of preparing the statement of cash flows, all transactions that are not classified as capital and related financing activities, noncapital financing activities or investing activities are classified as operating activities. The adjustments to reconcile operating income to net cash provided by operating activities includes other income which consists primarily of general administrative and general project service charges and water contract income from prior years.

Use of estimates:

The preparation of financial statements in conformity with U.S. 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.

Reclassifications:

Certain reclassifications have been made to the December 31, 2009 financial statements in order to conform to the December 31, 2010 presentation.

Note 2. Water Received and Delivered

Detailed below is the Water Received and Delivered by the District. This information does not include water that is solely pumped and utilized by farmers. Rather, water information provided below represents water that is utilized by the District.

Water Received	***2010 (acre feet)***	***2009 (acre feet)***
Purchased from Kern County Water Agency		
Entitlement		
Current year allocation (40% and 35%)	77,500	62,000
Add borrowing (carryover) to next year	(35,799)	(35,374)
Add carryover from prior year	21,333	24,184
Agency adjustment to carryover	-	1,607
Subtotal	63,034	52,417
Other	515	268
Total Water Received - Kern County Water Agency	63,549	52,685
Total Water Received from Banking Partners	139,997	-
Total Water Received from Other Water Agencies	8,000	6,092
In-District Ground Water Extraction		
District Wells Pumped	10,614	66,726
Pumping agreement with landowners	-	65,136
Total Water Received - Ground Water Extraction	10,614	131,862
Out of District Ground Water (Kern Fan)		
Pioneer Project		9,017
	-	9,017
Total Water Received	222,160	199,656

	2010 (acre feet)	2009 (acre feet)
Water Delivered		
Delivered In-District		
Contract	80,850	57,984
Non-contract	103,376	2,527
In District spreading and overdraft correction	12,853	-
Supplemental Ag water	400	418
Other	954	1,673
Total Water Deliver - In-District	198,433	62,602
Recharge to Kern Fan Projects	15,623	-
Returned to Other Water Agencies	-	10,033
Returned to Banking Partners	-	90,045
Returned to Banking Partners exchange	-	29,967
	-	120,012
Losses	8,104	7,009
Total Water Delivered	222,160	199,656

Note 3. Restricted Assets

Reserve funds:

The District maintains several reserve funds under provisions of loan contracts and bond issuances and other restrictions. The amounts required for each fund are as follows:

	2010		2009	
	Amount Required	Amount on Deposit	Amount Required	Amount on Deposit
Bond and loan reserve fund	$ 10,789,513	$ 10,789,513	$ 10,789,135	$ 10,789,135
Retirement trust fund	79,434	79,434	59,010	59,010
	$ 10,868,947	$ 10,868,947	$ 10,848,145	$ 10,848,145

The provisions of the various loan contracts and reserve funds are as follows:

Bond and loan reserve fund:

The provisions of the District's various bond issuances and loans from the State of California, Department of Water Resources require the District to maintain reserves until the bonds have been redeemed, certain loan requirements are satisfied or until bond proceeds are exhausted.

Retirement trust fund:

The District funds a separate cash account for the 401(k) pension plan. Contributions to the District's pension plan are paid from this account.

Note 4. Property, Plant and Equipment

The following is a summary of changes in the District's property, plant and equipment for the years ended December 31, 2010 and 2009:

	Assets-At Cost				
	Balance 12/31/09	***Acquisitions***	***Retirements***	***Reclass/ Transfers***	***Balance 12/31/10***
Capital Assets not being depreciated:					
Land	$ -	$ 115,797	$ -	$ -	$ -
Construction in progress	1	4,721,267	-	(5,335,829)	-
Capital Assets being depreciated:					
Source of supply	0	-	-	-	-
Transmission and distribution	-	-	-	4,571,097	-
Communication equipment	0	-	-	-	-
Autos and trucks	0	86,780	-	-	-
Office equipment	0	-	-	-	-
Field and misc. equip.	0	-	-	-	-
Well drilling equip.	0	22,563	-	-	-
Wells	-	-	-	-	-
General plant and equipment	0	-	-	764,732	-
	$ 1	$ 4,946,407	$ -	$ -	$ -

	Accumulated Depreciation				
	Balance 12/31/09	***Depreciation Expense***	***Retirements***	***Reclass/ Transfers***	***Balance 12/31/10***
Source of supply	$ -	$ 332,968	$ -	$ -	$ -
Transmission and distribution	0	5,372,353	-	-	-
Communication equipment	-	-	-	-	-
Autos and trucks	-	54,072	-	-	-
Office equipment	-	35,492	-	-	-
Field and misc. equip.	(1)	8,052	-	-	-
Well Drilling	-	224,761	-	-	-
Wells	-	15,671	-	-	-
General plant and equipment	1	60,241	-	-	-
	$ -	$ 6,103,610	$ -	$ -	$ -

	Assets-At Cost				
	Balance 12/31/08	***Acquisitions***	***Retirements***	***Reclass/ Transfers***	***Balance 12/31/09***
Capital Assets not being depreciated:					
Land	$ -	$ 498,807	$ -	$ -	$ -
Construction in progress	1	23,185,511	-	(24,118,188)	1
Capital Assets being depreciated:					
Source of supply	0	-	-	-	0
Transmission and distribution	0	-	-	24,078,134	0
Communication equipment	0	-	-	-	0
Autos and trucks	0	14,721	-	-	0
Office equipment	0	19,699	-	-	0
Field and misc. equip.	0	-	-	-	0
Well drilling equip.	0	-	-	-	0
Wells	-	-	-	-	0
General plant and equipment	0	-	-	40,054	0
	$ 1	$ 23,718,738	$ -	$ -	$ 1

	Accumulated Depreciation				
	Balance 12/31/08	***Depreciation Expense***	***Retirements***	***Reclass/ Transfers***	***Balance 12/31/09***
Source of supply	$ -	$ 333,096	$ -	$ -	$ -
Transmission and distribution	0	4,613,646	-	-	0
Communication equipment	-	-	-	-	-
Autos and trucks	(1)	51,127	-	-	(1)
Office equipment	-	33,642	-	-	-
Field and misc. equip.	-	8,694	-	-	(1)
Well Drilling	-	224,760	-	-	-
Wells	-	15,670	-	-	-
General plant and equipment	-	58,193	-	-	-
	$ (1)	$ 5,338,828	$ -	$ -	$ (2)

Note 5. Long-Term Debt

Long-term debt at December 31, 2010 and 2009 was as follows:

	2010	***2009***
Contract payable, State of California, 3.4375%, unsecured, payable $33,735 semiannually including interest, due October 1, 2011 (proceeds were used for lining canals)	$ 65,821	$ 129,436
Contract payable, State of California, 3.0286%, unsecured, payable $167,545 semiannually including interest, due October 1, 2016 (proceeds were used for construction of the Water Conservation Element)	1,826,297	2,099,928
Contract payable, State of California, 2.8%, unsecured, payable $45,059 semiannually including interest, due October 1, 2015 (proceeds were used for construction of the Interconnection Pipeline)	420,003	496,981
Contract payable, State of California, 2.8%, unsecured, payable $124,725 semiannually including interest, due October 1, 2013 (proceeds were used to finance certain construction projects)	598,481	826,468
2006A Water Banking Revenue Bonds, 4.25-4.78%, collateralized by future groundwater banking revenue, principal payable annually, interest payable semiannually, due December 1, 2035 (proceeds were used to refund 2003 bonds and fund a portion of second phase of Stored Water Recovery Unit)	30,165,000	30,650,000
2004A Revenue Bonds, 2% - 5.5%, collateralized by future groundwater banking revenue, principal payable annually, interest payable semiannually, due December 1, 2035 (proceeds used to finance certain improvements of water banking project and fund reserve for the bonds)	45,005,000	45,605,000

	2010	2009
Contract payable, State of California, 2.4%, unsecured, payable $135,321 semiannually including interest, due May 2023 (proceeds used for construction of groundwater recharge project)	$ 3,007,437	$ 3,202,422
Contract payable, State of California, 2.6%, unsecured, payable $55,052 semiannually including interest, due August 15, 2023 (proceeds used for construction of groundwater recharge project)	1,208,127	1,285,327
Contract payable, State of California, 2.6%, unsecured, payable $161,076 quarterly including interest, due December 31, 2025 (proceeds used for construction of a water distribution system)	3,897,558	4,116,312
Contract payable, State of California, 2.4%, unsecured, payable $159,792 semiannually including interest, due April 1, 2025 (proceeds used for construction of a water distribution system)	4,303,587	4,516,058
2007 Revenue Bonds, 3.586%, collateralized by rights to deposits in investment accounts, principal payable semiannually, interest payable monthly, due May 15, 2017 (proceeds used for District's share of construction costs of CVC project)	3,460,225	3,977,424
2009A Refunding Revenue Bonds, interest rates vary over life of bonds between 2.5%-5.25%, collateralized by the District's general project service charges, principal payable annually, interest payable semi-annually, due December 1, 2038 (proceeds were used to refund 2008 bonds, fund reserve for the bonds, and pay for cost of issuance of bonds)	50,500,000	51,080,000
	144,457,536	147,985,356
2005 Interest Rate Swap, at cost (See Note 8)	3,327,000	3,327,000

		2010		2009
Less deferred amount on advance refunding of 2003 and 2005 bonds, net of accumulated amortization 2010, $146,227; 2009, $72,388	$	(1,982,303)	$	(2,056,142)
Plus (less) premium, discount, and costs of issuance on bonds, net of accumulated amortization 2010, $179,716; 2009, $148,858		942,309		973,167
Less current maturities		(3,996,066)		(3,491,222)
Long term debt, less discount and current maturities	$	142,748,476	$	146,738,159

The following is a summary of the long-term debt transactions for the years ended December 31, 2010 and 2009:

	Payable 12/31/09	*Debt Incurred*	*Debt Retired*	*Payable 12/31/10*
Bond principal	$ 131,312,424	$ -	$ (2,182,197)	$ 129,130,227
Loans, State of California	16,672,932	-	(1,345,623)	15,327,309
	$ 147,985,356	$ -	$ (3,527,820)	$ 144,457,536

	Payable 12/31/08	*Debt Incurred*	*Debt Retired*	*Payable 12/31/09*
Bond principal	$ 131,745,673	$ 51,080,000	$ (51,513,249)	$ 131,312,424
Loans, State of California	17,985,110	-	(1,312,178)	16,672,932
	$ 149,730,783	$ 51,080,000	$ (52,825,427)	$ 147,985,356

The annual requirements to amortize all debt outstanding as of December 31, 2010 are as follows:

Years Ending December 31,	*Principal*	*Interest*	*Total Debt Service*
2011	$ 3,996,066	$ 5,411,132	$ 9,407,198
2012	4,078,698	5,279,435	9,358,133
2013	4,139,726	5,141,581	9,281,307
2014	4,166,390	5,240,193	9,406,583
2015	4,348,502	6,019,530	10,368,032
2016-2020	21,218,954	27,014,179	48,233,133
2021-2025	26,279,200	22,326,855	48,606,055
2026-2030	28,845,000	16,043,656	44,888,656
2030-2035	38,215,000	8,179,888	46,394,888
2036-2039	9,170,000	931,750	10,101,750
	$ 144,457,536	$ 101,588,199	$ 246,045,735

Note 6. 2009A and 2008A Revenue Bonds

The District issued the 2008A Revenue Bonds on July 1, 2008, in the aggregate principal amount of $50,000,000. From the proceeds of the bonds, the District paid $16,825,000 to Wells Fargo Bank, as escrow agent, for deposit in an escrow fund pertaining to the advance refunding of the 2005 Revenue Bonds of the District; all in accordance with the terms of an escrow agreement between the District and the aforementioned bank. As a result, the 2005 Revenue Bonds are considered to be defeased and the liability for those bonds has been removed from the combined statement of net assets of the District at December 31, 2008.

During the year ended December 31, 2009, the District issued the 2009A Refunding Revenue Bonds in the aggregate principal amount of $51,080,000, plus a premium of $3,502,623. This issuance was to currently refund $50,000,000 of outstanding 2008A Revenue Bonds. The current refunding resulted in $937,311 of costs of issuance and deferred loss from advance refunding of the 2008A bonds. The premium, costs of issuance, and costs of issuance and deferred loss from the 2008A bonds refunding are reported in the accompanying financial statements as an addition or deduction from bonds payable, and are being charged to operations as a component of interest expense through the year 2039 using the straight-line method.

Note 7. 2009 Tax and Revenue Anticipation Notes

During the year ended December 31, 2010, in anticipation of the receipt of taxes, revenues and other moneys to be received by the District allocable to fiscal year 2010, the District issued through Wells Fargo Bank the 2010 Tax and Revenue Anticipation Notes (TRAN), for an amount not to exceed $5,000,000. Interest is at daily one-month LIBOR multiplied by 0.669, plus 2.065%, due monthly. The TRAN is collateralized by amounts on deposit in investment accounts. The outstanding balance on these notes at December 31, 2010 was $-0-. Any outstanding principal is due by March 1, 2011.

Note 8. Interest Rate Swaps

2005 Forward Starting Swap:

On October 27, 2005, the District entered into an off-market forward starting swap (2005 swap) that was competitively bid in anticipation of a projected future issuance of variable rate bonds to synthetically advance refund the District's 2003 and 2004 Bonds. The swap will commence September 1, 2014, and is based on a notional amount of $53,895,000. The pay-fixed, receive-variable swap generated debt service savings in the form of an upfront payment in the amount of $3,927,850, from the counterparty, SunTrust Bank (SunTrust), who was the highest bidder. This amount is recorded in the Combined Statement of Net Assets as long-term debt and is not adjusted to the fair value at each reporting date. During the year ended December 31, 2006, $600,850 of the swap upfront payment was paid back as part of the advance refunding of the 2003 Revenue Bonds of the District, leaving $3,327,000 to be amortized when the swap agreement commences.

The fixed swap rate of 5.12% that the District will pay represents the average interest rate of the District's existing coupons for the District's refunded bonds after the swap commencement date. The variable swap rate that the District will receive is equal to 69% of the 1 month LIBOR rate, which was calculated to estimate the District's future interest rate for its projected bond issuance. The swap's scheduled notional amounts are reduced until the swap's termination date of December 1, 2035, to mirror the existing principal reductions in the District's refunded bonds which the District estimates will approximate the principal reductions of the new variable rate bonds issued in the future.

Fair value

As of December 31, 2010, the 2005 swap had a negative fair value of $7,590,651. This fair value takes into consideration the prevailing interest rate environment, the specific terms and conditions of the transaction and any upfront payments that may have been received. The fair value was estimated using the zero-coupon method. The method calculated the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve are the market's best estimate of future spot interest rates. These payments were then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds on the date of each future net settlement on the swap.

Credit risk

Credit risk is the risk that SunTrust cannot fulfill the terms and obligations specified in the swap agreement. Since the swap had a negative fair value as of December 31, 2010, the District did not have exposure related to credit risk on its swap with SunTrust. However, the District would have exposure related to credit risk in the amount of the swap's positive fair value if interest rates increased to cause the fair value of the swap to become positive. This would occur at any time prior to the swap's termination of December 1, 2035. The credit ratings of SunTrust are Aa3, A+ and A+ by Moody's, S&P and Fitch, respectively. The swap agreement contains no collateral requirements for either party.

Basis risk

Basis risk, which the District is exposed to on its swap, is the risk when the variable interest rate paid by the District on its projected future variable rate bond issuance and the variable swap interest rate received from SunTrust differ. Specifically, the District is exposed to basis risk should the interest rate equal to 69% of the 1 month LIBOR rate be lower than the actual variable bond rate the District pays on its projected future variable rate bond issuance. Based on the significance and extent of any basis risk exposure, the purpose of the swap to generate debt service savings may not be realized.

Termination risk

Under certain terms of the respective contracts, either the District or SunTrust may terminate the swap from nonperformance from the other party. If the swap is terminated, the projected future issuance of variable rate bonds would no longer be hedged to a fixed rate. If the swap is terminated and the swap has a negative fair value, the District would be liable to SunTrust for a payment equal to the fair value of the swap. The additional termination events in the agreement are limited to credit related events only and the ratings triggers are substantially below the current credit rating of SunTrust and the District.

Market-access risk

The District will likely need to issue variable rate debt to coincide with the commencement date of September 1, 2014. Market access risk addresses whether the District has the ability to efficiently issue variable rate debt at the time of commencement.

2007 Swap:

During the year ended December 31, 2010, the District implemented GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments.* The table below summarizes activity during the reporting period and balances as of December 31, 2010:

Pay-fixed interest rate swap:

Change in fair value	$	(279,263)
Fair value at December 31, 2010	$	(279,263)
Notional amount at December 31, 2010	$	(3,460,225)

Objectives and terms

On April 24, 2007, the District entered into an off-market swap that was competitively bid in anticipation of a projected future issuance of variable rate bonds to synthetically advance refund the District's 2007 Bonds. The swap commenced November 15, 2007, and is based on a notional amount of $5,000,000. The pay-fixed, receive-variable swap will generate debt service savings over the life of the agreement from the counterparty, Wells Fargo Bank (Wells Fargo), who was the highest bidder.

The fixed swap rate of 3.586% that the District will pay represents the average interest rate of the District's existing coupons for the District's refunded bonds after the swap commencement date. The variable swap rate that the District will receive is equal to 67% of the 1 month LIBOR rate, which was calculated to estimate the District's future interest rate for its projected bond issuance. The swap's scheduled notional amounts are reduced until the swap's termination date of May 15, 2017, to mirror the existing principal reductions in the District's refunded bonds which the District estimates will approximate the principal reductions of the new variable rate bonds issued in the future.

Fair value

As of December 31, 2010, the swap had a negative fair value of $279,263. This fair value takes into consideration the prevailing interest rate environment, the specific terms and conditions of the transaction and any upfront payments that may have been received. The fair value was estimated using the zero-coupon method. The method calculated the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve are the market's best estimate of future spot interest rates. These payments were then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds on the date of each future net settlement on the swap.

Credit risk

Credit risk is the risk that Wells Fargo cannot fulfill the terms and obligations specified in the swap agreement. Since the swap had a negative fair value as of December 31, 2010, the District did not have exposure related to credit risk on its swap with Wells Fargo. However, the District would have exposure related to credit risk in the amount of the swap's positive fair value if interest rates increased to cause the fair value of the swap to become positive. This would occur at any time prior to the swap's termination of May 15, 2017. The credit ratings of Wells Fargo are Aa3, A+ and A+ by Moody's, S&P and Fitch, respectively. The swap agreement contains no collateral requirements for either party.

Interest rate risk

The 2007 swap is a pay-fixed, receive-variable cash flow hedge, hedging a portion of the District's variable rate debt. The District believes it has significantly reduced interest rate risk attributable to the principal amount being hedged by entering into the interest rate swap.

Basis risk

Basis risk, which the District is exposed to on its swap, is the risk when the variable interest rate paid by the District on its projected future variable rate bond issuance and the variable swap interest rate received from Wells Fargo differ. Specifically, the District is exposed to basis risk should the interest rate equal to 67% of the 1 month LIBOR rate be lower than the actual variable bond rate the District pays on its projected future variable rate bond issuance. Based on the significance and extent of any basis risk exposure, the purpose of the swap to generate debt service savings may not be realized.

Termination risk

Under certain terms of the respective contracts, either the District or Wells Fargo may terminate the swap from nonperformance from the other party. If the swap is terminated, the projected future issuance of variable rate bonds would no longer be hedged to a fixed rate. If the swap is terminated and the swap has a negative fair value, the District would be liable to

Wells Fargo for a payment equal to the fair value of the swap. The additional termination events in the agreement are limited to credit related events only and the ratings triggers are substantially below the current credit rating of Wells Fargo and the District.

Market-access risk

The District has issued variable rate debt to coincide with the commencement date of November 15, 2007. Market access risk addresses whether the District has the ability to efficiently issue variable rate debt at the time of commencement.

Rollover risk

The District is exposed to rollover risk on swaps that mature or may be terminated prior to the maturity of the associated financings. When these swaps terminate, or in the case of termination option, if the counterparty exercises its option, the District will not realize the synthetic rate offered by the swaps on the underlying issues. The District is exposed to rollover risk on the 2007 swap should it be terminated prior to the maturity of the associated findings.

Foreign currency risk

All derivatives are denominated in U.S. dollars and therefore, the District is not exposed to foreign currency risk.

Note 9. Self-Insurance

The District is a member of the Association of California Water Agencies, Joint Powers Insurance Authority (JPIA). JPIA is a group of California Water Districts who have pooled funds to provide self-insurance coverage as follows:

Type of Coverage	Limits per Occurrence Self-Insurance	Limits per Occurrence Excess Insurance
General liability/automobile liability	\$10,000-\$500,000	\$500,000-\$49,500,000
Property insurance	\$1,000-\$50,000	\$10,000-\$100,000,000

The District is in a group with a \$10,000 retention level (deductible) per occurrence for auto and general liability, \$1,000 per occurrence for property, and \$500 per occurrence on licensed vehicles. Claims over the retention levels are insured by the group up to the self-insurance limits (see above) and by policies purchased by JPIA from the Insurance Company of Pennsylvania, Lexington Insurance Company, and Appalachian Insurance Company for the excess.

JPIA bills the District a deposit premium at the beginning of each policy year, which is placed in a reserve fund to cover the self-insurance portion of any claim. Settlements and/or expenses related to claims during the year are charged against the reserve. If the balance of the reserve at the end of the year is deemed too low in relation to the amount of outstanding claims, the District is billed for additional premiums. When the claims are fully settled, any amounts remaining in the reserve are refunded to the District.

Note 10. Commitments and Contingencies

Water Supply Contract with Kern County Water Agency:

The District obtained its surface water supply in accordance with certain contracts signed between 1969 and 1974 with the Kern County Water Agency (Agency), amended to its current annual amount of 155,000 acre feet of entitlement surface water, through the year 2039. The Agency, in turn, obtained its surface water supply in 1963 when it signed a contract with the State of California, Department of Water Resources (DWR), to purchase annual surface water, currently contracted at 998,731 acre feet, through the State Water Project (SWP) through the year 2035.

The District's contract with the Agency provides for various separate charges, all of which are included in "Source of Supply" in Operating Expenses of the District's Combined Statement of Revenue and Expenses. The "fixed charge" component of the contract is not necessarily reduced by annual water supply deficiencies as the District is obligated to pay 100% of the annual fixed costs billed by the Agency. Under certain circumstances, fixed charges could be reduced by the DWR when the District receives less than its full entitlement in years of low water supply. Source of supply costs attributable to this contract were $8,310,330 and $8,751,862 for the years ended December 31, 2010 and 2009, respectively.

The District anticipated a 40% allocation of surface water entitlement from DWR in 2010. Accordingly, the Agency has provided the District with an estimate of both fixed and variable energy costs for 2010. A full entitlement, (155,000 acre feet) will be charged due to the depletion of the Ag Trust fund. The Agency estimates the District's 2010 water contract to be approximately $9,087,000.

On March 13, 2008, Judge Wanger of the Fresno Federal Court, ordered DWR to reduce the amount of SWP water exported by the Delta pumps. This order has significantly reduced the amount of water allocated and delivered to the District. Due to the pumping restrictions, the District received 30% of its entitlement for the 2009 water year and projected a 40% allocation for 2010.

On May 25, 2010, Judge Wanger of the Fresno Federal Court eased pumping restrictions that were set in place on March 13, 2008. The federal court granted a preliminary injunction on the biological opinion for salmon, stating that the federal agencies responsible for drafting the biological opinion must take in account human impacts and also demonstrate why certain water exports restriction were called for in the opinion. Accordingly, on June 22, 2010 the District's surface water entitlement increased from a projected a 40% allocation to a 50% allocation. With the late increase in 2010 State Water Allocation, the District adjusted operations to facilitate the receipt of banking partner water with unrestricted banking partner deliveries beginning July 1, 2010. In 2010, the District, in addition to our 50% allocation, received over 125,000 acre feet from banking partners.

Because of the continuing possibility of state water allocations being maintained at reduced levels for water users due to the impacts of the 2008 Wanger decision and the subsequent operational constraints placed upon the withdrawal of water from the Delta, the District has developed several programs to augment the Districts available water supply among which are, the utilization of wells, banking programs and the transfer of water from sources outside the District. Additionally, the District continues to work on the financial aspect of the problems in an attempt to reduce charges and increase the reliability of the water supply to water users, wherever possible.

Due to the continued uncertainty associated with the reliability of the States Delta Water supplies, the District conservatively estimated a 50% allocation from the State for 2011. On April 20, 2011, the State Department of Water Resources increased the surface water allocation to 80% for all State Water Contractors. To date the District has received requests to bank over 295,000 acre feet from our banking partners due to the significant increase in available 2011 surface water supply. With the Banking partner activity and the surface water supplies available to the District, the District expects to manage nearly 500,000 acre feet in 2011.

Uncalled assessments:

The Improvement Districts have levied assessments in prior years which have not been called. The uncalled assessments in the Improvement Districts serve as security on construction financing for Project Unit One in the Pond-Poso Improvement District and the Project Units One and Two in the Buttonwillow Improvement District. Uncalled assessments at December 31, 2010 and 2009 were $4,059,411.

As part of the Energy Development Element project approval vote on November 26, 1991, an assessment was authorized in the amount of $119 per acre on approximately 125,947 acres, for a total adjusted assessment of $14,987,729.

Although the assessments have been levied, they are uncalled and are not reflected as an asset and related liability in the combined financial statements. These assessments will not be recognized until such time as they are called by the District.

Construction projects:

The following table shows the approximate budget, year to date, remaining construction costs, and estimated completion date:

Construction Project	***Budget***	***Paid to Date***	***Balance Remaining***	***Estimated Completion Date***
Pond Poso Spreading Grounds	$ 3,178,197	$ 2,984,978	$ 193,219	February, 2011

Note 11. Retirement Plan

In 2007, the District made certain modifications to its defined contribution pension plan, currently entitled “Semitropic Water Storage District 401(k) Plan,” which is a 401(k) plan covering all eligible employees. The District administers this plan and can amend the Plan or its contributions at any time. The Plan consists of investments in mutual funds with John Hancock and Van Kampen American Capital Trust Company. The District contributes an amount equal to 10% of the employees' base salary each month to the employees' pension plan. Employees are required to contribute 4% of base salary each month to receive District contributions. To determine the base salary for the plan year, the rates applicable on January 1 are used throughout the plan year and adjusted during the year if a pay increase is given. An employee is eligible for participation in the retirement plan after six months of service. The District's contributions for each employee are 20% vested after two years of employment with vesting increasing 20% for each additional year of employment up to six years. The District's contributions are 100% vested after six years of employment. Unvested contributions and interest forfeited by employees who leave before six years of service are used to reduce the District's current-period contribution requirement.

The District's payroll and contributions for the years ended December 31, 2010 and 2009 were as follows:

	2010	***2009***
Total payroll	$ 3,194,435	$ 2,722,385
Base salary for computing contributions	$ 2,652,741	$ 2,606,299
District contributions	$ 265,274	$ 260,650
Employee contributions	$ 142,765	$ 141,098

BARBICH HOOPER KING
DILL HOFFMAN
ACCOUNTANCY CORPORATION

Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

Board of Directors
Semitropic Water Storage District
Wasco, California

We have audited the accompanying statements of net assets of Semitropic Water Storage District (District) as of and for the years ended December 31, 2010 and 2009 and the related statements of revenue, expenses and changes in net assets, and cash flows for the years then ended. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

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

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

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Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

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

This report is intended solely for the information and use of management the board of directors, the California State Controller's office, and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

BARBICH HOOPER KING
DILL HOFFMAN
Accountancy Corporation

BARBICH HOOPER KING

Bakersfield, California
June 17, 2011

Semitropic Water Storage District

Combined Schedules of Operating Expenses
Years Ended December 31, 2010 and 2009

	2010	2009	Increase (Decrease)
Transmission and distribution:			
Power	$ 5,165,071	$ 13,040,567	$ (7,875,496)
Salaries and wages	1,623,552	1,254,399	369,153
Employee benefits	976,810	815,490	161,320
Repairs and maintenance	591,110	1,082,675	(491,565)
Kern Water Bank and Pioneer Expenses	232,897	1,104,104	(871,207)
Fuel and oil	177,394	197,184	(19,790)
Payroll taxes	140,090	136,878	3,212
Operating supplies	45,932	41,729	4,203
Equipment rent	15,529	22,958	(7,429)
Utilities	15,348	18,880	(3,532)
Licenses and fees	3,977	3,523	454
Miscellaneous	2,555	666	1,889
Equipment maintenance	1,368	19	1,349
Answering service	-	1,035	(1,035)
	$ 8,991,633	$ 17,720,107	$ (8,728,474)
Well operations:			
Salaries	$ 210,625	$ 467,936	$ (257,311)
Employee benefits	175,478	218,069	(42,591)
Repairs and maintenance	123,524	128,541	(5,017)
Payroll taxes	47,594	43,910	3,684
Supplies	5,827	42,710	(36,883)
Equipment rent	5,558	3,855	1,703
Insurance	4,334	-	4,334
Licenses and fees	664	(290)	954
Well abandonment	-	10,283	(10,283)
	$ 573,604	$ 915,014	$ (341,410)

	2010	2009	Increase (Decrease)
Source of supply:			
Water	$ 8,565,622	$ 10,152,806	$ (1,587,184)
General and administrative:			
Salaries and wages	$ 1,086,455	$ 1,012,145	$ 74,310
Employee benefits	456,949	341,358	115,591
Consulting and computer support	156,736	276,174	(119,438)
Public relations	155,854	276	155,578
Financing and administration	148,546	319,588	(171,042)
Insurance	140,259	149,289	(9,030)
Legal	129,852	376,828	(246,976)
Dues	95,715	249,939	(154,224)
Office	76,758	55,689	21,069
Utilities	54,007	39,322	14,685
Payroll taxes	51,714	38,685	13,029
Accounting and auditing	42,980	46,532	(3,552)
Repairs and maintenance	42,704	55,550	(12,846)
Engineering	35,144	240,750	(205,606)
Equipment rent	30,101	22,848	7,253
Travel	29,879	54,521	(24,642)
Building services	13,786	13,309	477
Directors' fees and expense	12,012	17,417	(5,405)
Bank fees	11,500	11,684	(184)
Grant related costs	10,323	-	10,323
Marketing	2,049	4,009	(1,960)
Property taxes	236	8,709	(8,473)
Air gap program	-	9,925	(9,925)
Damage claim cost	-	6,093	(6,093)
	$ 2,783,559	$ 3,350,640	$ (567,081)
Depreciation expense	$ 6,103,609	$ 5,338,828	$ 764,781

Semitropic Water Storage District

Combined Schedule of Insurance Coverage
December 31, 2010

	Policy No.	Effective Date	Expiration Date
Joint Powers Insurance Authority - Association of California Water Agencies Property, Fidelity	Self-Insured	4/1/2010	4/1/2011
Joint Powers Insurance Authority - Association of California Water Agencies General, Auto, Public Officials Liability	Self-Insured	10/1/2010	10/1/2011
Bonds			
Western Surety	69311183	4/17/2008	4/17/2011
Western Surety	14558205	9/23/2008	9/23/2011
Western Surety	22171084	4/17/2008	4/17/2011
Western Surety	69485775	4/17/2008	4/17/2011
Western Surety	22185935	3/31/2006	4/1/2013
Western Surety	68970435	3/31/2006	3/31/2013
Great American	7909111	4/12/2006	4/12/2013
Great American	1506833	4/10/2006	4/11/2011

Annual Premium		Coverage
$	53,310	Property Insurance - all risk coverage $1,000 - $10,000 - combined single limit for each occurrence $50,000 - $100,000,000 - excess comprehensive liability - total insurance value $34,673,212 basic property and equipment ($5,000 deductible) - auto physical damage ($500 deductible) $100,000 - $500,000 - employee fidelity bond ($1,000 deductible)
$	91,955	Comprehensive Liability Insurance $ 10,000 - $500,000 - combined single limit for each occurrence $ 500,000 - $60,000,000 - excess comprehensive liability ($10,000 deductible) includes prior year retrospective premiums
$	340	$5,000 - public official bond - Jeff Fabbri
$	340	$5,000 - public official bond - Todd Tracy
$	340	$5,000 - public official bond - Theodore R. "Ted" Page
$	340	$5,000 - public official bond - Daniel Waterhouse
$	340	$5,000 - public official bond - Frederick Wegis
$	340	$5,000 - public official bond - James Crettol
$	313	$5,000 - public official bond - Philip W. Portwood
$	1,094	$50,000 - treasurer bond - Daniel Waterhouse

BARBICH HOOPER KING
DILL HOFFMAN
ACCOUNTANCY CORPORATION

Independent Auditor's Report on Compliance with Requirements That Could Have a Direct and Material Effect on each Major Program and on Internal Control over Compliance in Accordance with OMB Circular A-133

Board of Directors
Semitropic Water Storage District
Wasco, California

Compliance

We have audited Semitropic Water Storage District's (District) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the District's major federal programs for the year ended December 31, 2010. The District's major federal programs are identified in the accompanying schedule of expenditures of federal awards. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the District's management. Our responsibility is to express an opinion on the District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the District's compliance with those requirements.

In our opinion, the District, complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2010.

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Internal Control over Compliance

Management of the District is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the District's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of management, board of directors, California State Controller's office, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

BARBICH HOOPER KING
DILL HOFFMAN
Accountancy Corporation

Barbich Hooper King

Bakersfield, California
June 17, 2011

Semitropic Water Storage District

Schedule of Expenditures of Federal Awards
For the Year Ended December 31, 2010

Federal Grantor	*CFDA Number*	*Federal Expenditures*
United States Department of the Interior		
Bureau of Reclamation Programs		
Program: Water 2025	15.507	
Pond Poso Spreading and Recovery Facility-ARRA		$ 1,574,413
Planning, Design, and Permitting the Stored Water Recovery Unit of the Semitropic Water Storage District Groundwater Bank		294,934
Water for America Challenge Grant Program: Water Marketing and Efficiency Grants		273,876
Preventing Crisis and Conflict in the West - System Optimization Review		300,000
		$ 2,443,223