

NAPA SANITATION DISTRICT

AUDIT REPORT

**FOR THE FISCAL YEAR
ENDED JUNE 30, 2009**

NAPA SANITATION DISTRICT

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Napa Sanitation District
Napa, California

We have audited the accompanying basic financial statements of Napa Sanitation District (the District) as of and for the year ended June 30, 2009, as listed in the table of contents. 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 audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform our audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 Napa Sanitation District, as of June 30, 2009, and the changes in its financial position and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 3, 2009, 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 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.

Board of Directors
Napa Sanitation District
Napa, California

The Management's Discussion and Analysis, the schedule of Funding Status – CALPERS, and the schedule of funding progress for the District's other Post Employment Benefit (OPEB) plan, as listed in the table of contents, are not a required part of the basic financial statements, but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and do not express an opinion on it.

Gallina LLP

Roseville, California
December 3, 2009

MANAGEMENT'S DISCUSSION AND ANALYSIS

NAPA SANITATION DISTRICT

Management's Discussion and Analysis (Unaudited) June 30, 2009

This section of the District's Annual Financial Statements presents our discussion and analysis of the District's financial performance during the fiscal year ended June 30, 2009. Please read it in conjunction with the District's Financial Statements, which follow this section.

FINANCIAL HIGHLIGHTS

- The District's assets exceeded liabilities at the close of the 2008-2009 fiscal year by \$130,681,105 (*net assets*). Of this amount, \$11,084,031 (*unrestricted net assets*) may be used to meet ongoing obligations to citizens and creditors, \$4,113,801 is restricted for debt service and capital projects and \$115,483,273 is invested in capital assets, net of related debt.
- Current year results reflect operating income of \$768,915, an decrease of \$511,610 from prior year. Operating expenses increased by \$1,218,128 while operating revenue increased by only \$706,518.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the District's Basic Financial Statements. The Statement of Net Assets (pages 8-9), the Statement of Revenues, Expenses, and Changes in Net Assets (page 10), and the Statement of Cash Flows (pages 11-12) provide information about the activities of the District. The financial statements also include various footnote disclosures, which further describe the District activities.

Napa Sanitation District Condensed Statement of Net Assets

	<u>2009</u>	<u>2008</u>
Assets		
Current and other assets	\$ 20,800,239	\$ 20,523,414
Capital assets	150,122,789	149,063,638
Total Assets	<u>170,923,028</u>	<u>169,587,052</u>
Liabilities		
Current and other liabilities	3,145,323	3,093,914
Long term liabilities	37,096,600	37,099,070
Total Liabilities	<u>40,241,923</u>	<u>40,192,984</u>
Net Assets		
Invested in capital assets, net	115,483,273	114,093,003
Restricted	4,113,801	9,956,816
Unrestricted	11,084,031	5,344,249
Total Net Assets	<u>\$ 130,681,105</u>	<u>\$ 129,394,068</u>

NAPA SANITATION DISTRICT

Management's Discussion and Analysis (Unaudited) June 30, 2009

During the fiscal year ended June 30, 2009, net assets increased by \$1,287,037 mostly attributable to the addition of capital assets.

The District reports positive balances in all three components of net assets. Net assets invested in capital assets, net of related debt continues to increase as a result of further additions to the utility plant. Restricted net assets decreased due to increased amounts used for utility plant expansion.

Napa Sanitation District

Condensed Statement of Revenues, Expenses and Changes in Net Assets

	2009	2008	Change	% Change
Operating revenues				
Sewer Charges	\$ 16,880,761	\$ 14,051,455	\$ 2,829,306	20.14%
Connection fees	820,914	2,867,635	(2,046,721)	-71.37%
Other charges for services	220,163	296,230	(76,067)	-25.68%
Total operating revenues	<u>17,921,838</u>	<u>17,215,320</u>	<u>706,518</u>	<u>4.10%</u>
Operating expenses				
Wastewater collection, treatment and reclamation	4,099,066	4,410,654	(311,588)	-7.06%
Depreciation	6,186,381	5,356,732	829,649	15.49%
Administration and general	6,867,476	6,167,409	700,067	11.35%
Total operating expenses	<u>17,152,923</u>	<u>15,934,795</u>	<u>1,218,128</u>	<u>7.64%</u>
Operating Income (Loss)	<u>768,915</u>	<u>1,280,525</u>	<u>(511,610)</u>	<u>-39.95%</u>
Non-Operating Revenue (Expense)				
Interest income	458,788	886,312	(427,524)	-48.24%
Interest expense	(1,811,855)	(1,755,331)	(56,524)	3.22%
Gain (loss) on asset disposal	(79,933)	(9,656)	(70,277)	727.81%
Other revenues (expenses)	1,487,933	475,951	1,011,982	212.62%
Total non-operating revenue (expense)	<u>54,933</u>	<u>(402,724)</u>	<u>457,657</u>	<u>-113.64%</u>
Net income (loss) before capital contributions	823,848	877,801	(53,953)	-6.15%
Capital contributions	<u>463,189</u>	<u>1,018,890</u>	<u>(555,701)</u>	<u>-54.54%</u>
Change in net assets	<u>1,287,037</u>	<u>1,896,691</u>	<u>(609,654)</u>	<u>-32.14%</u>
Net Assets, Beginning of Year	<u>129,394,068</u>	<u>127,497,377</u>	<u>1,896,691</u>	<u>1.49%</u>
Net Assets - End of Year	<u>\$ 130,681,105</u>	<u>\$ 129,394,068</u>	<u>\$ 1,287,037</u>	<u>0.99%</u>

For the fiscal year ended June 30, 2009, operating revenue increased by \$706,518 while operating expenses increased by \$1,218,128 due to increased depreciation and administration and general expenses, due to the recognition of \$414,000 in other post employment benefits expense. The increase in operating revenue is due to the last of three 15% Sewer Service Charge increases authorized by the Board on August 2, 2006. It allowed the District to eliminate its deficit and fully support the fiscal needs of the District in maintaining a safe, healthy and reliable wastewater system.

NAPA SANITATION DISTRICT

Management's Discussion and Analysis (Unaudited)
June 30, 2009

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

The District has a five-year capital improvement program and publishes a capital budget annually in conjunction with the District's budget process. The capital program is reviewed and updated on an annual basis.

As of June 30, 2009, the District's investment in capital assets amounted to \$150,122,789 (net of accumulated depreciation), an increase of \$1,059,151. This investment in capital assets includes land, building and improvements, equipment, construction in progress, donated sewer lines and other contributed assets.

The table below provides a comparison of the District's capital assets for the current and prior years.

Napa Sanitation District Capital Assets, Net of Accumulated Depreciation

	<u>2009</u>	<u>2008</u>	<u>\$ Change</u>
Land	\$ 7,436,649	\$ 7,436,649	\$ --
Buildings and improvements	110,141,229	106,805,167	3,336,062
Equipment	4,867,638	5,303,254	(435,616)
Construction in progress	4,760,927	5,793,656	(1,032,729)
Donated sewer lines and other contributed assets	22,916,346	23,724,912	(808,566)
	<u>\$150,122,789</u>	<u>\$149,063,638</u>	<u>\$ 1,059,151</u>

Major capital projects for the fiscal year include the following:

- Winter Biosolids Removal Project
- E. Spring Street Sewer Line Rehabilitation Phase I
- Aeration Blower Replacement Project
- SCADA Upgrades – Phase 3

For additional information on capital assets, see Note 3 on page 20.

NAPA SANITATION DISTRICT

Management's Discussion and Analysis (Unaudited)
June 30, 2009

Long Term Obligations

At June 30, 2009, the District's total long-term debt outstanding was \$38,451,328, compared to \$38,780,478 in the prior year. This amount was comprised of \$378,945 of compensated absences, \$27,765,000 of certificates of participation, \$8,770,000 of variable rate demand bonds and \$1,537,383 in notes payable.

The District obtained additional loans totaling \$833,046 from the State Revolving Loan Fund for sewer improvement projects and made repayments totaling \$1,191,598 on other outstanding debt.

For additional information on long-term debt, see Note 4 on pages 21 and 22.

FUTURE PROJECTIONS

Revenue Projections

The District receives a variety of revenues from many sources, most of which must be accounted for separately and their identity kept intact. Revenue projections illustrated in the FY 09/10 Budget are estimated using historical data, economic indicators, and in-house plans for service delivery to help predict future revenues. Trends in regional development, environmental factors, and interest rates are also examined. When the available sources of information are combined, we produce an accurate but fiscally conservative picture of the District's FY 09-10 Projected Revenues.

FY 09/10 District Revenues from all sources, total revenues, are expected to be \$20,033,056. When compared to FY 08/09 Budget, the FY 09/10 total revenues are projected lower by \$714,535. Specifically, Operating Fund revenues are projected higher by \$338,611. This additional revenue is derived from the Sewer Use Charge category of revenue. The Capital Improvement Fund revenue is projected lower by \$1,053,146. This reduced revenue is due to the development downturn resulting in reduced Connection Fees revenue to the District.

Expense Projections

Overall, Operating and Capital expenses for the District are expected to be \$23,380,882 (excluding transfers between funds). There are several new Capital Projects totaling \$2,553,888 included in the FY 09/10 CIP Budget. These Projects are programmed in the 10-year Capital Improvement Program and Financial Master Plan. When these new projects are combined with ongoing Capital Projects the result is a total Capital Project Budget of \$9,354,236 for FY09/10. This amount when compared to the FY08/09 Capital Project Budget represents a reduction of \$2,074,328.

NAPA SANITATION DISTRICT

Management's Discussion and Analysis (Unaudited)
June 30, 2009

Financial Status

The financial condition of the District remains sound but is impacted by the current downturn in the local development sector of our economy. The reduction of revenue to the District, as a result of reduced demand for new connections to the system, will require special emphasis be placed on the ongoing review of the Capital Improvement Plan by District Management and the District Board.

Otherwise, energy and chemical costs in general will continue to rise and as such will require regular monitoring by staff. Likewise, the cost of employee benefits continues to rise for the District. Specifically health benefits, which adversely impact current employee and retiree costs, are a major contributor to escalating costs in the area of salaries and benefits.

An actuarial analysis of "Other Post Employment Benefits" is completed and will be presented to the Board for review and subsequent action in early FY 09/10. This action is an attempt to identify and plan for the future cost of the District's retiree medical plan.

REQUESTS FOR INFORMATION

The financial report is designed to provide a general overview of the District's finances for all those with interest in them. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Napa Sanitation District, 935 Hartle Court, P.O. Box 2480, Napa, California 94558.

BASIC FINANCIAL STATEMENTS

NAPA SANITATION DISTRICT

Statement of Net Assets

June 30, 2009

ASSETS

Current Assets:

Cash in County treasury	\$ 15,344,734
Imprest cash	300
Assessments receivable	444,595
Accounts receivable (net)	356,841
Other receivables	6,945
Inventory	142,817
Prepaid expenses	1,703

Total Current Assets 16,297,935

Restricted Cash and Investments:

Toilet retrofit program	16,946
With fiscal agent	3,154,411
Plant expansion account	959,390

Total Restricted Cash and Investments 4,130,747

Other Assets:

Deferred charges	<u>371,557</u>
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Capital Assets:

Nondepreciable	12,197,576
Depreciable, net	<u>137,925,213</u>

Total Capital Assets 150,122,789

Total Assets \$ 170,923,028

(continued)

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

NAPA SANITATION DISTRICT

Statement of Net Assets (continued)

June 30, 2009

LIABILITIES

Current Liabilities:

Accounts payable	\$ 830,668
Salaries and benefits payable	251,302
Current portion of compensated absences	211,370
Current portion of long-term debt	<u>1,279,290</u>

Total Current Liabilities 2,572,630

Current Liabilities Payable from Restricted Assets:

Interest payable	<u>572,693</u>
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Non-Current Liabilities:

Liability for compensated absences	167,575
Other post employment benefit (OPEB) obligation	414,388
Long-term debt, net of unamortized original issue discount	<u>36,514,637</u>

Total Non-Current Liabilities 37,096,600

Total Liabilities 40,241,923

NET ASSETS

Invested in capital assets, net of related debt	115,483,273
Restricted for debt service and construction projects	4,113,801
Unrestricted	<u>11,084,031</u>

Total Net Assets 130,681,105

Total Liabilities and Net Assets \$ 170,923,028

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

NAPA SANITATION DISTRICT

Statement of Revenues, Expenses and Changes in Net Assets For the Year Ended June 30, 2009

Operating Revenues:

Sewer charges	\$ 16,880,761
Connection fees	820,914
Other charges for services	220,163
Total Operating Revenues	<u>17,921,838</u>

Operating Expenses:

Insurance	229,389
Salaries and benefits	6,124,036
Materials, supplies and repairs	1,412,892
General and administrative	322,416
Contractual services	1,816,576
Utilities	1,046,642
Depreciation	6,186,381
Amortization	14,591
Total Operating Expenses	<u>17,152,923</u>

Operating Income	<u>768,915</u>
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Non-Operating Revenue (Expense):

Lease income	527,622
Taxes	(31,457)
Gain (loss) on disposal of assets	(79,933)
Interest income	458,788
Interest expense	(1,811,855)
Other revenue (expense)	991,768

Total Non-Operating Revenues (Expenses)	<u>54,933</u>
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Income (Loss) Before Capital Contributions	823,848
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Capital contributions	<u>463,189</u>
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Change in Net Assets	1,287,037
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Total Net Assets - Beginning of Year	<u>129,394,068</u>
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Total Net Assets - End of Year	<u>\$ 130,681,105</u>
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The accompanying notes are an integral part of these financial statements.

NAPA SANITATION DISTRICT

Statement of Cash Flows For the Year Ended June 30, 2009

Cash Flows from Operating Activities:

Receipts from customers	\$ 17,753,134
Payments to suppliers	(4,906,311)
Payments to employees	(5,648,383)
Net cash flows provided (used) for operating activities	<u>7,198,440</u>

Cash Flows from Noncapital Financing Activities:

Tax expense	(31,457)
Other revenue	991,768
Lease income	527,622
Net cash flows provided (used) for noncapital financing activities	<u>1,487,933</u>

Cash Flows from Capital and Related Financing Activities:

Payments of principal on long-term debt	(358,552)
Purchase of capital assets	(7,057,305)
Capital contributions	195,029
Interest paid	(1,807,630)
Net cash provided (used) for capital and related financing activities	<u>(9,028,458)</u>

Cash Flows from Investing Activities:

Interest Income	<u>512,368</u>
Net cash flows provided (used) for investing activities	<u>512,368</u>

Net increase (decrease) in cash and cash equivalents 170,283

Cash and cash equivalents, beginning of the year 19,305,498

Cash and cash equivalents, end of the year \$ 19,475,781

Reconciliation of Cash and Cash Equivalents to the Statement of Net Assets:

Cash and cash equivalents in current assets	\$ 15,345,034
Cash and cash equivalents in restricted assets	<u>4,130,747</u>

Total Cash and Cash Equivalents \$ 19,475,781

(continued)

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

NAPA SANITATION DISTRICT

Statement of Cash Flows (continued)
For the Year Ended June 30, 2009

Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:	
Operating income (loss)	<u>\$ 768,915</u>
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	6,186,381
Amortization	14,591
Changes in Assets and Liabilities:	
(Increase) decrease in accounts receivable	(185,170)
(Increase) decrease in other receivables	16,466
(Increase) decrease in inventory	(9,221)
(Increase) decrease in prepaid expenses	(1,703)
Increase (decrease) in accounts payable	(67,472)
Increase (decrease) in salaries and benefits payable	31,863
Increase (decrease) in other post employment benefits liability	414,388
Increase (decrease) in compensated absences payable	<u>29,402</u>
 Total Adjustments to Operating Income	 <u>6,429,525</u>
 Net cash provided (used) by operating activities	 <u><u>\$ 7,198,440</u></u>
 Noncash, investing, capital and financing activities:	
Contribution of capital assets	<u><u>\$ 268,160</u></u>

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

NOTES TO BASIC FINANCIAL STATEMENTS

The notes provided in the financial section of this report are considered an integral and essential part of adequate disclosure and fair presentation of this report. The notes include a summary of significant accounting policies for the District, and other necessary disclosure of pertinent matters relating to the financial position of the District. The notes express significant insight to the financial statements and are conjunctive to understanding the rationale for presentation of the financial statements and information contained in this document.

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 1: **Summary of Significant Accounting Policies**

The financial statements of the Napa Sanitation District (District) are prepared in accordance with Generally Accepted Accounting Principles (GAAP). The District applies all relevant Government Accounting Standards Board (GASB) pronouncements. Proprietary funds apply Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails.

A. Reporting Entity

The Napa Sanitation District (District) was organized as a County Sanitation District under the California Health and Safety Code in November 1945 to provide the necessary sewerage service to the City of Napa as well as adjacent areas of Napa County. The District is responsible for wastewater collection, treatment and disposal/reuse within most of the city limits of the City of Napa as well as adjacent areas of Napa County.

The District is not a component unit of the County of Napa. The District is legally separate and fiscally independent of the County of Napa. The District includes all activities (operations of its administrative staff and District officers) considered to be a part of the District. The District reviewed the criteria developed by the Governmental Accounting Standards Board (GASB) in its issuance of Statement No. 14, *The Financial Reporting Entity*, as amended by Governmental Accounting Standards Board (GASB) Statement No. 39, *Determining Whether Certain Organizations Are Component Unites – an amendment of GASB Statement No. 14*, to determine whether the District is financially accountable for other entities. The District has determined that no other outside entity meets the required criteria, and therefore, no agency has been included as a component unit in the financial statements. In addition, the District is not aware of any entity that would be financially accountable for the District that would result in the District being considered a component unit of that entity.

B. New Accounting Pronouncements

The District has adopted new accounting and financial reporting standards issued by the Governmental Accounting Standards Board (GASB) in the current year. GASB Statement No. 45, *Accounting and Financial Reporting by Employers of Postemployment Benefits Other than Pensions (OPEB)*, and GASB Statement No. 47, *Accounting for Termination Benefits*, GASB Statement No. 45 establishes standards for the measurement, recognition and display of OPEB expenses/expenditures, related assets and liabilities, note disclosures and, if

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 1: **Summary of Significant Accounting Policies** (continued)

B. New Accounting Pronouncements (continued)

applicable, required supplementary information in the financial reports of state and local government employers. GASB Statement No. 45 is effective for the fiscal year ended June 30, 2009.

The District also adopted GASB Statement No. 47 which provides guidance on how employers should account for benefits associated with either voluntary or involuntary terminations. For termination benefits provided through an existing defined benefit OPEB plan, the provisions of this Statement should be implemented simultaneously with the requirements of GASB Statement No. 45.

C. Basis of Presentation and Method of Accounting

The District accounts for its activities as a single enterprise fund, and the financial statements are accounted for on a flow of economic resources measurement focus, using the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when the related liability is incurred, regardless of the timing of related cash flows.

Operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as subsidies and investment earnings, result from nonexchange transactions or ancillary activities.

Nonexchange transactions, in which the District gives (or receives) value without directly receiving (or giving) equal value in exchange, include grants, entitlements and donations. In accordance with GASB No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, revenues from grants, entitlements and donations are recognized in the fiscal year in which all eligible requirements have been satisfied.

D. Cash, Investments and Equivalents

The District has adopted Governmental Accounting Standards Board (GASB) Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. The District's cash is pooled with the County of Napa's cash for investment purposes. It has been determined that the fair value of the County's cash in total compared to cost is not materially different, so that no adjustment has been reported on these financial statements.

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 1: **Summary of Significant Accounting Policies** (continued)

D. Cash, Investments and Equivalents (continued)

Cash, short-term investments and restricted investments are stated at cost, which approximates current fair value.

For purposes of the statement of cash flows, the District considers all cash and investments with original maturities of three months or less when purchased and their equity in the County Treasurer's Investment Pool, which is payable on demand, as cash and cash equivalents.

E. Receivables

Receivables consist mostly of fees charged for sewer services and reclaimed water sales. Management believes its receivables to be fully collectible, and accordingly, no allowance for doubtful accounts is required.

F. Inventory

Inventories consist of operating materials and supplies held for consumption, and are recognized as an expense at the time inventory is used. The District carries inventory at the lower of cost or market, on a first in, first out (FIFO) basis.

G. Deferred Charges

Deferred charges represent the cost of issuance of the 1998 certificates of participation payable, and of the installment purchase contract entered into on June 1, 2001 with the WasteReuse Finance Authority.

H. Restricted Assets

Amounts shown as restricted assets have been restricted by either bonds, by law or contractual obligations to be used for specified purposes, such as servicing bonded debt and construction of capital assets.

Restricted assets include water and sewer connection fees. The resolution establishing the authority for water and sewer connection fees restricts the use of these fees to the construction, acquisition, or financing of capital assets.

I. Capital Assets

All purchased capital assets are valued at cost where historical records are available and at an estimated historical cost where no historical records exist. Donated capital assets are valued at their estimated fair market value on the date received. The

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 1: **Summary of Significant Accounting Policies** (continued)

I. **Capital Assets** (continued)

District's policy is to include in construction-in-progress capitalized interest costs of related borrowings, net of interest earned on unspent proceeds of the related borrowings, as well as capitalized amortization of deferred charges and original issue discount. No interest costs or amortization were capitalized for the year ended June 30, 2009.

The District defines capital assets as assets with an initial individual cost of more than \$5,000 and an estimated useful life in excess of one year. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset life are not capitalized. Depreciation is computed using the straight-line method over the estimated useful lives of the various classes of plant and equipment as follows:

	<u>Useful Life</u> <u>(Years)</u>
Buildings and improvements	5-50
Equipment	5-50
Donated sewer lines and other contributed assets	50

J. **Compensated Absences**

Earned vacation may be accumulated by all personnel up to a maximum of twice their annual vacation leave on June 30th. Sick leave is accumulated without restriction as to maximum hours. District employees may not receive compensation for accumulated sick leave upon termination of employment, but can convert up to 48 hours of sick leave to personal leave after accumulated sick leave exceeds 500 hours. Any unused personal leave is forfeited on June 30th for non-management employees.

Management employees can accumulate up to a maximum of 96 hours by June 30th. Earned management leave time may be accumulated by management employees up to a maximum of twice their annual management leave time on June 30th.

The total estimated contingent liability for vested compensated absences at June 30, 2009 was \$378,945. The current portion of the liability was determined as 100% of earned compensated time and personal leave, and 50% of earned vacation and management leave.

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 1: **Summary of Significant Accounting Policies** (continued)

K. Net Assets

The District's financial statements utilize a net assets presentation. Net assets comprise the various net earnings from operating and non-operating revenues, expenses and contributions of capital. Net assets are classified in the following three components: invested capital assets (net of related debt), restricted and unrestricted.

- *Invested in Capital Assets, Net of Related Debt* – This category groups all capital assets, including infrastructure, into one component of net assets. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction or improvement of these assets reduce the balance in this category.
- *Restricted Net Assets* – This category presents external restrictions imposed by creditors, grantors, contributors or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation. For the District, this category represents restrictions for debt service and construction projects.
- *Unrestricted Net Assets* – This category represents net assets of the District, not restricted for any project or other purpose.

When both restricted and unrestricted net assets are available, unrestricted resources are used only after the restricted resources are depleted.

L. Use of Estimates

Management of the District has made certain estimates and assumptions relating to the reporting of assets and liabilities to prepare these financial statements in conformity with generally accepted accounting principles. Actual results could differ from those estimates.

M. Amortization

Deferred charges and original issue discount related to the 1998 certificates of participation are being amortized using the straight-line method over 30 years. Amortization was capitalized until the Wastewater Project was completed on April 17, 2002, and expended thereafter. Deferred charges related to the installment purchase contract entered into on June 1, 2001 with the WateReuse Finance Authority are being amortized using the straight-line method over 27 years.

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 2: **Cash and Investments**

Cash and investments shown in the statement of net assets represents the District's share of the County of Napa's cash and investment pool and restricted cash held with fiscal agents. The District voluntarily participates in the County's cash and investment pool. Interest earnings from this pool are transferred to the District on a quarterly basis based on the District's average daily balance. The County has an investment committee, which performs regulatory oversight for its pool as required by California Government Code Section 27134.

Required disclosure information regarding categorization of investments and other deposit and investment risk disclosures can be found in the County of Napa's comprehensive annual financial report and may be obtained by contacting the County Auditor-Controller's Office at 1195 Third Street, Room B-10, Napa, California 94559.

The District has adopted Napa County's investment policy.

At June 30, 2009, the District also had a \$16,946 bank balance on deposit with a financial institution. This amount is fully insured by federal depository insurance.

At June 30, 2009, total cash and investments held by the District were as follows:

	<u>Unrestricted</u>	<u>Restricted</u>	<u>Total</u>
Cash held in County treasury	\$ 15,344,734	\$ 959,390	\$ 16,304,124
Cash in bank	--	16,946	16,946
Petty cash	300	--	300
Investments with fiscal agent	--	3,154,411	3,154,411
Total	<u>\$ 15,345,034</u>	<u>\$ 4,130,747</u>	<u>\$ 19,475,781</u>

Cash with fiscal agent investments were as follows:

	<u>Interest Rates</u>	<u>Maturities</u>	<u>Par Value</u>	<u>Book Value</u>	<u>Fair Value</u>	<u>Weighted Average Maturity (Years)</u>
Cash with Fiscal Agent						
Westdeutsche term deposit	Variable	5/1/2028	\$ 798,160	\$ 798,160	\$ 798,237	18.84
Federated Mutual Funds	Variable	On Demand	2,356,251	2,356,251	2,356,250	--
Total			<u>\$ 3,154,411</u>	<u>\$ 3,154,411</u>	<u>\$ 3,154,487</u>	<u>4.77</u>

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements June 30, 2009

Note 2: **Cash and Investments** (continued)

Required disclosures for the District's deposit and investment risks for the cash held in the County Treasury at June 30, 2009, were as follows:

Credit risk	Not rated
Custodial risk	Not applicable
Concentration of credit risk	Not applicable
Interest rate risk	See disclosure above

Note 3: **Capital Assets**

Changes in the District's capital assets and accumulated depreciation for the year ended June 30, 2009 is summarized as follows:

	Balance June 30, 2008	Additions	Retirements	Transfers and Adjustments	Balance June 30, 2009
Capital assets, not being depreciated:					
Land	\$ 7,436,649	\$ --	\$ --	\$ --	\$ 7,436,649
Construction in progress	5,793,656	1,328,289	(20,518)	(2,340,500)	4,760,927
Total capital assets, not being depreciated	13,230,305	1,328,289	(20,518)	(2,340,500)	12,197,576
Capital assets, being depreciated:					
Structures and improvements	139,399,834	5,556,892	(232,578)	2,328,190	147,052,338
Vehicles and equipment	10,536,291	172,124	(656,993)	12,310	10,063,732
Donated assets	49,123,324	268,160	--	--	49,391,484
Total capital assets, being depreciated	199,059,449	5,997,176	(889,571)	2,340,500	206,507,554
Less accumulated depreciation for:					
Structures and improvements	(32,594,667)	(4,514,471)	198,029	--	(36,911,109)
Vehicles and equipment	(5,233,037)	(595,184)	632,127	--	(5,196,094)
Donated assets	(25,398,412)	(1,076,726)	--	--	(26,475,138)
Total accumulated depreciation	(63,226,116)	(6,186,381)	830,156	--	(68,582,341)
Total capital assets, being depreciated net	135,833,333	(189,205)	(59,415)	2,340,500	137,925,213
Total capital assets, net	\$ 149,063,638	\$ 1,139,084	\$ (79,933)	\$ --	\$ 150,122,789

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements June 30, 2009

Note 4: Long-Term Debt

Individual issues of Bonds, Notes and Certificates of Participation outstanding at June 30, 2009:

	<u>Maturity</u>	<u>Interest Rates</u>	<u>Annual Principal Installments</u>	<u>Original Issue Date</u>	<u>Original Issue</u>	<u>Outstanding 6/30/2009</u>
1998 Certificates of Participation Series A Purpose: Wastewater Project	2028	4.00%-5.00%	\$555,000-\$2,120,000	1/25/1999	\$ 34,520,000	\$ 27,765,000
WateReuse Installment Purpose: Construction of Water Reservoir Facilities	2028	Not to exceed 12.00%	\$265,000-\$605,000	6/1/2001	\$ 11,165,000	\$ 8,770,000
State Revolving Fund – SRF Purpose: Summit Avenue/Ora Drive	2022	2.50%	\$34,421-\$58,777	12/13/2003	\$ 901,376	\$ 704,337
State Revolving Fund – SRF Purpose: East Spring Street/ Montecito Boulevard Sewer Improvement Project Phase I	2029	0.00%	\$32,509	4/1/2009	\$ 650,177	\$ 650,177
State Revolving Fund – SRF Purpose: East Spring Street/ Montecito Boulevard Sewer Improvement Project Phase II	2029	0.00%	\$9,144	4/1/2009	\$ 182,869	\$ 182,869

The following represents the changes in long-term debt during the year:

	<u>Balance July 1, 2008</u>	<u>Additions</u>	<u>Retirement</u>	<u>Balance June 30, 2009</u>	<u>Amounts Due Within One Year</u>
SRF Loan	\$ 745,935	\$ 833,046	\$ (41,598)	\$ 1,537,383	\$ 84,290
WateReuse	9,105,000	--	(335,000)	8,770,000	345,000
1998 COP	28,580,000	--	(815,000)	27,765,000	850,000
Less: Unamortized Original Issue Discount	(293,047)	--	14,591	(278,456)	--
Compensated Absences	349,543	342,750	(313,348)	378,945	211,370
	<u>\$ 38,487,431</u>	<u>\$ 1,175,796</u>	<u>\$ (1,490,355)</u>	<u>\$ 38,172,872</u>	<u>\$ 1,490,660</u>

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 4: **Long-Term Debt** (continued)

As of June 30, 2009, annual debt service requirements to maturity are as follows:

Year Ending June 30:	Business-type Activities					
	SRF Loan		WaterReuse		1998 COP	
	Principal	Interest	Principal	Interest -a	Principal	Interest
2010	\$ 84,290	\$ 17,608	\$ 345,000	\$ 240,818	\$ 850,000	\$ 1,355,338
2011	85,357	16,542	355,000	230,671	890,000	1,315,075
2012	86,449	15,450	365,000	220,238	930,000	1,271,850
2013	87,570	14,330	375,000	209,519	975,000	1,226,606
2014	88,716	13,182	390,000	198,371	1,020,000	1,179,225
2015-2019	461,834	47,662	2,135,000	812,637	5,915,000	5,064,375
2020-2024	434,908	14,340	2,500,000	476,634	7,545,000	3,389,875
2025-2029	208,259	--	2,305,000	101,472	9,640,000	1,252,000
	<u>\$ 1,537,383</u>	<u>\$ 139,114</u>	<u>\$ 8,770,000</u>	<u>\$ 2,490,360</u>	<u>\$ 27,765,000</u>	<u>\$ 16,054,344</u>

a) Interest was calculated using 2008-2009 rates.

Note 5: **District Employees Retirement Plan (Defined Benefit Pension Plan)**

A. Plan Description

The Napa Sanitation District contributes to the California Public Employees Retirement System (PERS), an agent multiple-employer public employees' retirement system that acts as a common investment and administrative agent for participating public entities with the State of California. Copies of PERS annual financial report may be obtained from their Executive Office – 400 P Street, Sacramento, California 95814.

B. Funding Policy

The District makes the contributions required of District employees on their behalf and for their account. The rates are set by statute and therefore generally remain unchanged from year to year. The present actuarially determined rates of annual covered payment are as follows:

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 5: **District Employees Retirement Plan (Defined Benefit Pension Plan)** (continued)

B. Funding Policy (continued)

Category	Member Rates as a Percentage of Wages
Local miscellaneous members	8%

State statutes establish the contribution requirements of the plan members and the employer contribution rate is established and may be amended by PERS.

Annual Pension Cost

For the fiscal year ended June 30, 2009, the District's annual pension cost was \$1,258,088 and the District actually contributed \$1,258,088. The required contribution for the fiscal year ended June 30, 2009 was determined as part of the June 30, 2006 actuarial valuation using the entry age normal actuarial cost method with the contributions determined as a percent of pay. The actuarial assumptions include (a) 7.75% investment rate of return (net of administrative expenses); (b) projected salary increases that vary by duration of service ranging from 3.25% to 14.45%; and (c) a 3.25% increase overall payroll. Both (a) and (b) included an inflation component of 3.0%.

The actuarial value of the District's assets was determined using a technique that smoothes the effect of short-term volatility in the market value of investments over a two to five year period depending on the size of the investment gains and/or losses. The District's excess assets are being amortized as a level percentage of projected payroll on a closed basis.

Three-Year Trend Information

Fiscal Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
6/30/07	\$1,231,374	100%	\$ --
6/30/08	1,250,881	100%	--
6/30/09	1,258,088	100%	--

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 5: **District Employees Retirement Plan (Defined Benefit Pension Plan)** (continued)

C. Deferred Compensation Plan

All permanent employees of the District are eligible to participate in a District sponsored deferred compensation plan (the Plan) created in accordance with Internal Revenue Code Section 457. The Plan provides for the deferral of a portion of the employees' compensation until retirement, termination, or certain other covered events. The funds are invested on behalf of the employees through an administrator in various instruments including mutual funds, money market funds, and others.

Prior to 1999, all amounts of compensation deferred under the Plan, all property and rights purchased with those amounts and all income attributable to those amounts were (until paid or made available to the employee or other beneficiary) solely the property and rights of the District (without being restricted to the provisions of benefits under the Plan), and subject to the claims of the District's general creditors.

Due to a change in Federal law concerning deferred compensation plans, the Board of Directors amended the Plan. In accordance with the new law, the District set up a trust to hold assets and earnings of the deferred compensation plan for the exclusive benefit of the participants.

Government Accounting Standards Board Statement No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans* requires governments to report Section 457 plans in the financial statements if the assets are held by a government unit in a trustee capacity or as an agent for individuals. Currently, the District has minimal administrative involvement, does not perform the investing function for the plan and, therefore, is not considered to have fiduciary responsibility for the plan or hold the plan in a trustee capacity.

The County of Napa Auditor-Controller's office prepares the District's payroll and remits all required deposits to the third-party administrators.

Note 6: **Other Post-Employment Benefits (OPEB)**

Plan Description: The District offers medical, vision and life insurance premium benefits to eligible retirees through the California Public Employees Retirement System (PERS) health program. The contribution requirements of the plan members and the District are established and may be amended by the District

Under the current health plan, the District pays for coverage of the retiree plus an eligible spouse. To be eligible, the retiree must retire directly from the District at age 50 or later and have a minimum of five years of service. Employees that are hired on and after September 1, 2004 have reduced benefits.

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 6: **Other Post-Employment Benefits (OPEB)** (continued)

As of June 30, 2009, the District had 35 retirees receiving benefits at a cost of approximately \$237,412.

Annual OPEB Cost and Net OPEB Obligation: The annual required contribution (ARC) is an amount actuarially determined in accordance with the parameters of GASB Statement 45 – *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions*. The District’s ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize the unfunded actuarial liability over a period of 30 years. The following table shows the components of the District’s annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the District’s net OPEB obligation to the Retiree Healthcare Plan:

For fiscal year 2008-09, the District contributed \$237,412, or 36.4%, of the actuarially required contributions, to the retiree healthcare program.

Annual OPEB Cost and Net OPEB Obligation

Annual required contribution	\$ 651,800
Interest on net OPEB obligation	--
Adjustment of annual required contribution	--
Annual OPEB cost	<u>651,800</u>
Contributions made	<u>237,412</u>
Change in net OPEB obligation (asset)	414,388
Net OPEB obligation (asset) beginning of year	--
Net OPEB obligation (asset) end of year	<u><u>\$ 414,388</u></u>

The District’s Annual OPEB Cost, the percentage of Annual OPEB Cost contributed to the Plan (as described in the funding policy above), and the Net OPEB Obligation for fiscal year 2008-09 is as follows:

Fiscal Year Ended	Annual OPEB Cost	Actual Employer Contribution	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation (Asset)
6/30/2009	\$ 651,800	\$ 237,412	36.42%	\$ 414,388

In future years, three year trend information will be presented. Fiscal year 2008-09 was the first year of implementation of GASB Statement 45, and the District elected to implement prospectively; therefore prior year comparative data is not available.

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 6: **Other Post-Employment Benefits (OPEB)** (continued)

Funded Status and Funding Progress

The funded status of the plan, based on an actuarial valuation as of January 1, 2008, the plan's most recent actuarial valuation date, was as follows:

Actuarial accrued liability (AAL)	\$ 6,737,000
Actuarial value of plan assets	--
Unfunded actuarial accrued liability (UAAL)	<u>\$ 6,737,000</u>
Funded ratio (actuarial value of plan assets/AAL)	0%
Covered payroll	4,045,900
UAAL as percentage of covered payroll	166.51%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the January 1, 2008 actuarial valuation, the entry age normal actuarial cost method was used. The actuarial assumptions included a 5% investment rate of return, an inflation rate of 3% per year, and an increase in covered payroll at the rate of 3.25% per year. The OPEB plan's unfunded actuarial liability is being amortized by level percent of payroll contributions over 30 years. The remaining amortization period at June 30, 2009, was 30 years.

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 7: **Related Party Transactions**

Pursuant to an agreement between the County of Napa and the District, the County provides Management Information Services and Accounting Services to the District. During the year ended June 30, 2009, the District paid the County the following amounts for these services:

Information Technology Services	\$	273,323
Accounting Services		33,937

Note 8: **Risk Management**

The District is exposed to various risks of loss related to torts; thefts of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disaster. The District joined together with other entities to form the Special District Risk Management Authority (SDRMA), a public risk entity pool currently operating as a common risk management and insurance program for 414 member entities. The purpose of SDRMA is to spread the adverse effects of losses among the member entities and to purchase excess insurance as a group, thereby reducing its cost. A Board composed of one representative from each member agency governs SDRMA. The Board controls the operations of SDRMA including selection of management and approval for operating budgets, independent of any influence by member entities. A copy of the audit report may be obtained from SDRMA at 1112 I Street, Suite 300, Sacramento, California 95814.

The District is also a member of the California Sanitation Risk Management Authority (CSRMA) a public risk sharing pool. The District's workers compensation claims are handled by CSRMA. A Board composed of one representative from each member agency governs CSRMA. The Board controls the operations of CSRMA including selection of management and approval for operating budgets, independent of any influence by member entities. A copy of the audit report may be obtained from CSRMA at the Authority's web site at www.csrma.org.

In addition to SDRMA, the District also carries commercial insurance coverage for general liability and property damage. Settled claims for SDRMA or commercial insurance have not exceeded coverage in any of the past three fiscal years.

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements June 30, 2009

Note 8: **Risk Management** (continued)

The following is a summary of the insurance policies carried by the District for the fiscal year ended June 30, 2009:

<i>Comprehensive Business Policy</i>		
SDRMA – Specialty National Insurance Co.	General property	\$ 1,000,000,000
SDRMA	Special property coverage	Various
SDRMA	General liability	2,500,000
SDRMA – Continental Casualty Co.	Boiler and machinery	100,000,000
SDRMA	Auto, personal injury & property damage liability	2,500,000
SDRMA	Uninsured/underinsured motorists	750,000
SDRMA	Errors and omissions liability	2,500,000
SDRMA	Employment practices liability	2,500,000
SDRMA	Employee benefits liability	2,500,000
SDRMA – Fidelity and Deposit of Maryland	Public employees/officials dishonesty blanket coverage	400,000
SDRMA – American Safety Indemnity Co.	Public officials personal liability	500,000
 <i>Workers' Compensation Program</i>		
CSRMA – Employers Reinsurance Corp.	Initial workers' compensation	750,000
CSRMA – Employers Reinsurance Corp.	Excess workers' compensation	Statutory
CSRMA – Employers Reinsurance Corp.	Employer's liability	1,000,000
 <i>Pollution Legal Liability</i>		
Harbor Insurance Co.		5,000,000

Note 9: **Capital Contributions**

A portion of the construction costs for sewer lines completed by the District were paid for by outside parties. The donated portion of these assets is recorded as capital contributions and is reported at estimated fair value.

Note 10: **Subsequent Events**

On October 15, 2009, the Napa Sanitation District Public Financing Corporation, a blended component unit, issued \$9,120,000 in Adjustable Rate Refunding Revenue Certificates of Participation, Series 2009A, with the purpose of refunding the 2001 WateReuse Installment variable rate debt. The debt matures on August 1, 2028, with mandatory prepayments annually. The Napa Sanitation District pledged all revenue to cover debt service.

NAPA SANITATION DISTRICT

Notes to Basic Financial Statements
June 30, 2009

Note 10: **Subsequent Events** (continued)

Also on October 15, 2009, the Napa Sanitation District Public Financing Corporation, a blended component unit, issued \$26,675,000 in Refunding Revenue Certificates of Participation, Series 2009 B, with the purpose of refunding the 1998 Certificates of Participation Series A. The bonds mature from August 1, 2010 through 2028. The Napa Sanitation District pledged all revenue to cover debt service.

The Series 2009A debt was issued on parity with the Series 2009B debt, with superior obligations not allowed.

Note 11: **New Accounting Pronouncements**

The GASB has issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, which may have a significant impact on the District's financial reporting process. The District has determined that this statement will not have a significant impact on the District's reporting process. GASB Statement No. 51 establishes accounting and financial reporting requirements for intangible assets including easements, water rights, timber rights, patents, trademarks and computer software. GASB No. 51 will be effective for the fiscal year ending June 30, 2010.

The GASB has issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. This statement establishes accounting and financial reporting requirements for derivative instruments entered into by state and local governments. The requirements of this new statement are effective for financial statements for periods beginning after June 15, 2009. The District does not use derivative instruments.

REQUIRED SUPPLEMENTARY INFORMATION

NAPA SANITATION DISTRICT

Required Supplementary Information
For the Year Ended June 30, 2009

FUNDING STATUS – CALPERS

Funded Status of CalPERS Plan

The funded status of the District's plan, including the actuarial value of the plan's assets and the actuarial accrued liability, is no longer available, except on a pooled basis. Additional information can be obtained from CalPERS, 400 P Street, Sacramento, California 95814.

NAPA SANITATION DISTRICT

Required Supplementary Information
For the Year Ended June 30, 2009

SCHEDULE OF FUNDING PROGRESS – POSTEMPLOYMENT BENEFIT PLAN

The table below shows an analysis of the actuarial value of assets as a percentage of the actuarial accrued liability and the unfunded actuarial accrued liability as a percentage of the annual covered payroll as of June 30:

In future years, three year trend information will be presented. Fiscal year 2008-09 was the first year of implementation of GASB Statement 45, and the District elected to implement prospectively; therefore prior year comparative data is not available.

Actuarial Valuation Date	(1) Actuarial Value of Plan Assets	(2) Actuarial Accrued Liability (AAL)	(3) Funded ratio	(4) Unfunded Actuarial Accrued Liability (UAAL) (2) - (1)	(5) Annual Covered Payroll	(6) UAAL as a Percentage of Covered Payroll (4) ÷ (5)
1/1/2008	\$ --	\$ 6,737,000	0.00%	\$ 6,737,000	\$ 4,045,900	166.51%

OTHER REPORT



**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

Board of Directors
Napa Sanitation District
Napa, California

We have audited the financial statements of the Napa Sanitation District as of and for the year ended June 30, 2009, and have issued our report thereon dated December 3, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects Napa Sanitation District's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Board of Directors
Napa Sanitation District
Napa, California

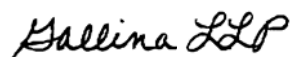
Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any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

Compliance and Other Matters

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

We noted certain matters that we reported to management of the Napa Sanitation District in a separate letter dated December 3, 2009.

This report is intended solely for the information of the Napa Sanitation District, management, the Board of Directors, others within the entity, and federal and state awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.



Roseville, California
December 3, 2009