



East Orange County Water District
Annual Financial Report
June 30, 2007 and 2006



Our Mission Statement

“To provide the most cost effective, reliable, and highest quality water services for the present as well as the future by operating in the most cost efficient manner possible, keeping the cost of water to our customers affordable and provide a safe working environment for our employees. Serve the community in an open manner and, at all times, communicate and deliberate in public meetings where open discussions are promoted.”

East Orange County Water District Board of Directors as of June 30, 2007

Name	Title	Elected/ Appointed	Current Term
William VanderWerff	President	Elected	12/04 - 12/08
Douglas M. Chapman	Vice President	Elected	12/04 - 12/08
Richard E. Barrett	Director	Elected	12/06 - 12/10
Richard B. Bell	Director	Elected	12/06 - 12/10
Gary R. Veeh	Director	Elected	12/06 - 12/10

**William H. Redcay, General Manager
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October 20, 2007

Board of Directors
East Orange County Water District
Orange, California

Introduction

It is our pleasure to submit the Annual Financial Report for the East Orange County Water District (District) for the fiscal year ended June 30, 2007. District staff, following guidelines set forth by the Governmental Accounting Standards Board, prepared this financial report. The District is ultimately responsible for both the accuracy of the data and the completeness and the fairness of presentation, including all disclosures in this financial report. We believe that the data presented is accurate in all material respects. This report is designed in a manner that we believe is necessary in order to enhance your understanding of the District's financial position and activities.

This report is organized into two sections: (1) Introductory and (2) Financial. The Introductory section provides general information about the District's organization and activities, and provides information useful in assessing the District's financial condition. The Financial section includes the Independent Auditors' Report, Management's Discussion and Analysis of the District's basic financial statements, and the District's audited basic financial statements with accompanying notes.

Generally Accepted Accounting Principles (GAAP) requires that management provide a narrative introduction, overview, and analysis to accompany the financial statements in the form of a Management's Discussion and Analysis (MD&A) section. This letter of transmittal is designed to complement the MD&A and should be read in conjunction with it. The District's MD&A can be found immediately following the Independent Auditors' Report.

District Background

The East Orange County Water District was formed in December of 1961 and is operating under the County Water District Law, which is contained in Division 12 of the California Water Code, Sections 30000 - 33901. The District is an independent special district governed by its Board of Directors elected by the voters within the District's service area. Initially the District was formed to provide an agency, which would furnish imported water to the area within its boundaries. In July of 1985, the District assumed the operations of the County of Orange WWD No. 8 as the District's Retail Zone. The District's pipeline distribution system delivers water to five sub-agencies within its boundaries consisting of the Golden State Water Company, the City of Tustin, Orange Park Acres Mutual Water Company, the City of Orange and its own Retail Zone. All of the sub-agencies use groundwater with supplemental water supplied by the District from the Allen McCulloch Pipeline or the East Orange County Feeder No.2.

The District encompasses an area of approximately 100,000 acres and is a member of the Municipal Water District of Orange County, which is a member of the Metropolitan Water District of Southern California (Metropolitan) and therefore is entitled to receive Colorado River and Northern California imported water through the distribution facilities of the Metropolitan system.

Industry Outlook

California's water supply continues to pose many new and complex challenges for water suppliers in the state. In recent years, the District has been an active participant and leader in addressing these concerns. Through coordination and planning with other local and regional water suppliers, the District continues to engage in developing long-term solutions to the various water supply challenges.

Internal Control Structure

District management is responsible for the establishment and maintenance of the internal control structure that ensures that the assets of the District are protected from loss, theft, or misuse. The internal control structure also ensures that adequate accounting data are compiled to allow for the preparation of financial statements in conformity with generally accepted accounting principles. The District's internal control structure is designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that (1) the cost of a control should not exceed the benefits likely to be derived, and (2) the valuation of costs and benefits requires estimates and judgments by management.

Budgetary Control

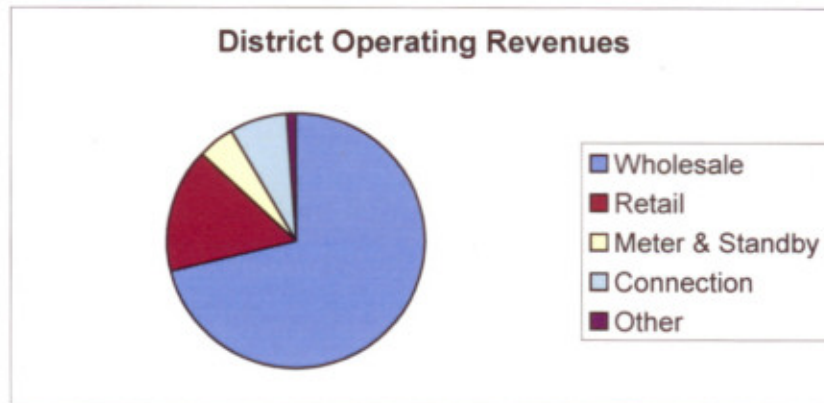
The District's Board of Directors annually adopts a balanced operating and capital budget prior to each new fiscal year. The budget authorizes and provides the basis for reporting and control of financial operations and accountability for the District's enterprise operations and capital projects. The budget is prepared on the cash basis of accounting, the District's interim financial statements are on a modified accrual basis and the final financial statements are prepared using the full accrual basis.

Financial Plan

This District is committed to provide its customers with a safe, reliable and efficient water system. The foundation for this commitment is based in the District's Capital Improvement Plan and the Financial Masterplan. These plans are reviewed annually as part of the District's budgeting process. The District's financial plan includes the establishment of reserve funds in accordance with the District's reserve practices. Reserve funds are set to ensure the continued orderly operation of the District's water systems, the providing of services to residents at established levels, and the continued stability of the District's rate structure. The purpose and structure of these funds are further discussed in the Management's Discussion and Analysis.

Water Rates and District Revenues

The District's policy objective is that all revenues from user charges generated from District customers must support all District operations including capital project funding. Water rates are user charges imposed on customers for services and are the primary component of the District's revenue. Water rates are composed of a commodity (usage) charge, and a fixed meter and standby service charge, and are reviewed on an annual basis as part of the budgeting process. The following chart reflects the District's operating revenue mix for the year ending June 30, 2007:



Debt Administration

While the District has no bonded indebtedness, the District does have an obligation under a separate note payable agreement. Additional information regarding this obligation can be found in the District's audited financial statements and accompanying notes.

Investment Policy

The Board of Directors annually adopts an investment policy that conforms to California State law, District ordinance and resolutions, prudent money management, and the "prudent person" standards. The objectives of the Investment Policy are safety, liquidity, and yield. District funds are normally invested in the State Treasurer's Local Agency Investment Fund, Certificates of Deposits, Government Agency Obligations or other specifically authorized investments.

Audit and Financial Reporting

State law and loan covenants require the District to obtain an annual audit of its financial statements by an independent certified public accountant. The accounting firm of Charles Z. Fedak & Company, CPAs has conducted the audit of the District's financial statements. Their unqualified Independent Auditor's Report appears in the Financial Section.

Risk Management

The District is a member of the Association of California Water Agencies – Joint Powers Insurance Authority (Authority). The purpose of the Authority is to arrange and administer risk management programs for the pooling of self-insured losses, and the purchase of excess insurance coverage.

Water Conservation Programs

The District has been implementing conservation management practices for many years. The District distributes materials that encourage water conservation. Additionally, the District has offered the following conservation programs through its affiliation with the Municipal Water District of Orange County:

- Residential and Multi-family low flush toilet distribution
- Residential Appliance Rebate Program
- Residential Drought-tolerant Landscape Classes

Other References

More information is contained in the Management's Discussion and Analysis and the Notes to the Basic Financial Statements found in the Financial Section of the report.

Respectfully submitted,

William H. Redcay
General Manager

Carl R. Schoonover
District Accountant/Treasurer