

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
SOUTHGATE SANITATION DISTRICT  
FISCAL YEAR 2008**

The Southgate Sanitation District (the "District") offers the readers of the District's financial statements this narrative overview and analysis of the District's financial performance during the Fiscal Year ended December 31, 2008. Please read it in conjunction with the financial statements.

**CONTENTS**

In addition to this Management Discussion and Analysis this annual report includes :

- ◆ Independent Auditor's Report
- ◆ Financial Statements - *The financial statements of the District report information about the District using accounting methods similar to those used by private sector companies. These statements offer short and long-term financial information about its activities.*
  - ◆ Statement of Net Assets - *The Statement of Net Assets provides information about the nature and amounts of investments in resources (assets) and obligations to District creditors (liabilities). It also provides the basis for computing the rate of return, evaluating the capital structure of the District and assessing the liquidity and financial flexibility of the District.*
  - ◆ Statement of Activities - *This statement measures the results of the District's operations over the past year and illustrates the manner in which it has funded its operations and activities. It is the basis for determining profitability and credit worthiness.*
  - ◆ Statement of Cash Flows - *The purpose of this statement is to provide information about the District's cash receipts and payments during the reporting period. This statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities.*
- ◆ Notes to the Financial Statements which explain in more detail much of the information in the financial statements.
- ◆ Supplementary Information, consisting of:
  - ◆ Budgetary Comparison Schedule - Budgetary Basis Non-GAAP - 2008
  - ◆ Budgetary Comparison Schedule - Budgetary Basis Non-GAAP - 2007

**FINANCIAL ANALYSIS OF THE DISTRICT**

One of the most important questions asked about the District's finances is "Is the District as a whole better off or worse off as a result of this year's activities?" The Statement of Net Assets and Statement of Activities work to answer that question.

A summary of the District's Statement of Net Assets is presented on the following page.

	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>'07-'08 Change</u>	<u>'07-'08 %</u>
Current Assets	\$4,028,453	\$2,005,284	\$1,422,127	(\$583,157)	-29.1%
Property, Plant & Equipment	\$21,735,446	\$24,369,809	\$24,318,962	(\$50,847)	-0.2%
Other Assets	\$28,380,643	\$30,790,719	\$33,965,310	\$3,174,591	10.3%
<b>Total Assets</b>	<u>\$54,144,542</u>	<u>\$57,165,812</u>	<u>\$59,706,399</u>	<u>\$2,540,587</u>	<u>4.4%</u>
Current Liabilities	\$1,216,382	\$1,473,921	\$1,143,297	(\$330,624)	-22.4%
Long Term Liabilities	\$0	\$0	\$0	\$0	0.0%
<b>Total Liabilities</b>	<u>\$1,216,382</u>	<u>\$1,473,921</u>	<u>\$1,143,297</u>	<u>(\$330,624)</u>	<u>-22.4%</u>
Invested in Capital Assets	\$21,735,446	\$24,369,809	\$24,318,962	(\$50,847)	-0.2%
Restricted	\$0	\$0	\$0	\$0	0.0%
Unrestricted	\$31,192,714	\$31,322,082	\$34,244,140	\$2,922,058	9.3%
<b>Total Net Assets</b>	<u>\$52,928,160</u>	<u>\$55,691,891</u>	<u>\$58,563,102</u>	<u>\$2,871,211</u>	<u>5.2%</u>

The reduction in Current Assets, (as compared to 2006 and 2007), is reflective of a tightening of cash management. Property, Plant and Equipment and Invested in Capital Assets reflect the rigorous application of the GASB Statement No. 34 standards to the capital asset schedule and to the calculation of depreciation; together with capital expenditures in 2008. During 2008 the District's largest capital investments were: 1) continuation of the 2006 Sanitary Sewer Improvement Program, 2) video and sonar inspection of the District's 1.25 mile long wastewater tunnel (favorable findings), and 3) continued development of the Geographic Information System. Other Assets reflects an increase in the District's fiscal reserves due to conservative budgeting and better than expected tap sales. The decrease Current Liabilities is reflective of normal variation over time.

A summary of the District's activities and changes in net assets is presented below.

	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>'07-'08 Change</u>	<u>'07-'08 %</u>
Operating Revenue	\$123,376	\$677,101	\$195,117	(\$481,984)	-71.2%
Non-Op Revenue	\$2,280,956	\$2,868,549	\$2,743,762	(\$124,787)	-4.4%
<b>Total Revenues</b>	<u>\$2,404,332</u>	<u>\$3,545,650</u>	<u>\$2,938,879</u>	<u>(\$606,771)</u>	<u>-17.1%</u>
Depreciation Expense	\$986,588	\$1,066,345	\$1,172,941	\$106,596	10.0%
Govt. & Admin. Expense	\$563,559	\$565,828	\$565,828	\$0	0.0%
Other Operating Expense	\$673,229	\$511,022	\$623,998	\$112,976	22.1%
Non-Op Expense	\$12,597	\$12,486	\$12,808	\$322	2.6%
<b>Total Expenses</b>	<u>\$2,235,973</u>	<u>\$2,155,681</u>	<u>\$2,375,575</u>	<u>\$219,894</u>	<u>10.2%</u>
Income/Loss Before Contributions	\$168,359	\$1,389,969	\$563,304	(\$826,665)	-59.5%
Capital Contributions	\$1,930,338	\$1,373,762	\$2,307,907	\$934,145	68.0%
	<u>\$2,098,697</u>	<u>\$2,763,731</u>	<u>\$2,871,211</u>	<u>\$107,480</u>	<u>3.9%</u>
<b>Net Assets - Beginning</b>	<u>\$50,829,463</u>	<u>\$52,928,160</u>	<u>\$55,691,891</u>	<u>\$2,763,731</u>	<u>5.2%</u>
<b>Net Assets - End</b>	<u>\$52,928,160</u>	<u>\$55,691,891</u>	<u>\$58,563,102</u>	<u>\$2,871,211</u>	<u>5.2%</u>

The District funds its activities from interest earnings, new tap sales (included in Capital Contributions), a small property tax, a small charge collected on the District's behalf by the City of Englewood, and miscellaneous revenues. The District's property tax has been progressively reduced over the years and is now less than \$1 per \$1,000 of assessed valuation. Capital projects are funded by tap fees (included in Capital

Contributions) augmented by existing reserve funds. The decrease in Operating and Non-Operating revenues is reflective of the decline in the economy and in the pace of new development. Through prudent budgeting and accumulation of operational and capital reserves the District is able to maintain established programs at the optimal level of service.

Total Expenses (10.2% increase) reflects increased operational and system repair costs, together with the addition of one new employee. Income Before Contributions (59.5% decrease) reflects the effects of the economic and development down-turn. That situation is expected to recover with time. Capital Contributions (68.0% increase) reflects the tail end of the development activity ahead of the economic down-turn. The overall health of the District is reflected in the Net Assets - End.

As you review the Financial Statements you will note that the District has early implemented Government Accounting Standards Board Statement No. 40 (GASB 40) relative to disclosures of deposit and investment risk on the District's cash and investments. You will find that the District invests under the provisions and restraints of a written Investment Policy and conforms to the requirements of the Colorado Public Deposit Protection Act (PDPA) relative to use of eligible public depositories. While the District limits its investments to the more conservative and higher rated instruments allowed under the Colorado Statutes, there is opportunity for diversification and the investment portfolio has been laddered to take advantage of any up-turn in the investment market.

## CAPITAL ASSETS

At the end of 2008, the District had invested \$42.07 million, (less \$17.75 million in accumulated depreciation), in a broad range of infrastructure, including: approximately 225 miles of collection and transmission lines, one tunnel, maintenance and administration facilities, vehicles, and equipment as shown in the following table.

	2006	2007	2008	'07-'08 Change	'07-'08 %
Sewer System	\$34,208,644	\$37,709,758	<b>\$38,273,430</b>	\$563,672	1.5%
Studies	\$557,822	\$557,822	<b>\$557,822</b>	\$0	0.0%
Capital Equipment	\$906,599	\$913,104	<b>\$938,359</b>	\$25,255	2.8%
Building & Land	\$1,444,571	\$1,444,571	<b>\$1,740,272</b>	\$295,701	20.5%
Construction in Progress	\$263,092	\$328,219	<b>\$556,038</b>	\$227,819	69.4%
<b>Subtotal</b>	<u>\$37,380,728</u>	<u>\$40,953,474</u>	<u><b>\$42,065,921</b></u>	<u>\$1,112,447</u>	<u>2.7%</u>
Accumulated Depreciation	(\$15,645,282)	(\$16,583,665)	<b>(\$17,746,959)</b>	(\$1,163,294)	7.0%
<b>Net Property, Plant and Equipment</b>	<b>\$21,735,446</b>	<b>\$24,369,809</b>	<b>\$24,318,962</b>	(\$50,847)	-0.2%

This table fully reflects the results of the GASB 34 asset valuation and depreciation efforts. The increase in Construction in Progress is also a reflection of the above referenced capital improvements. With completion of the 2006 Sanitary Sewer Program the capacity related projects set forth in the District's master plan will be fully satisfied. The District's capital focus now shifts entirely to capital preservation, rehabilitation and replacement in the context of its 100 year useful life study and long term fiscal modeling. To enhance that focus on infrastructure sustainability the District will institute new asset management tracking, evaluation, and programming tools in 2010.

## LONG TERM DEBT

The District has no long term debt and does not anticipate a need to issue new debt in the foreseeable future.

## BUDGETARY HIGHLIGHTS

As required by State Law, the District adopts a budget and appropriates funds for the following year by December 15, of each year. If an amendment is necessary, the Board will approve a supplemental appropriation at a public hearing and file it with the State of Colorado. Budget to actual statements are included as Supplemental Information in the audited financial statements. There were no supplemental appropriations made to the 2007 or 2008 budgets.

The District operates within the context of a 50 year fiscal model and 5 year budgetary projections. The Board of Directors and Management are attentive and fiscally prudent. The District has been successful in meeting the needs of its constituents within the restraints of the tax and budgetary limitations of Colorado's TABOR Amendment.

The following table presents the District's budget and actual expenditures for 2006, 2007 and 2008.

	2006		2007		2008	
	Budget	Actual	Budget	Actual	Budget	Actual
System Devel Fees	\$1,381,600	\$1,142,223	\$625,625	\$1,059,827	\$551,250	\$1,833,597
Investment Income	\$742,141	\$1,270,480	\$1,121,656	\$1,972,769	\$1,341,204	\$1,761,527
Property Tax	\$821,696	\$811,322	\$831,544	\$817,368	\$868,107	\$847,854
Rates & Charges	\$90,818	\$71,367	\$94,903	\$105,251	\$98,565	\$8
Miscellaneous Income	\$1,619,863	\$251,163	\$1,618,500	\$650,262	\$1,303,200	\$329,490
<b>Total Revenues</b>	<b>\$4,656,118</b>	<b>\$3,546,555</b>	<b>\$4,292,228</b>	<b>\$4,605,477</b>	<b>\$4,162,326</b>	<b>\$4,772,476</b>
Admin & Operations	\$1,412,722	\$1,196,974	\$1,851,071	\$1,013,647	\$1,735,623	\$1,098,891
Professional Services	\$67,000	\$52,411	\$73,000	\$75,689	\$89,250	\$103,743
Debt Service	\$0	\$0	\$0	\$0	\$0	\$0
Capital Outlay	\$3,061,500	\$868,020	\$9,150,000	\$3,407,797	\$6,635,000	\$647,785
<b>Total Expenditures</b>	<b>\$4,541,222</b>	<b>\$2,117,405</b>	<b>\$11,074,071</b>	<b>\$4,497,133</b>	<b>\$8,459,873</b>	<b>\$1,850,419</b>
<b>Revenues Less Expenditures</b>	<b>\$114,896</b>	<b>\$1,429,150</b>	<b>(\$6,781,843)</b>	<b>\$108,344</b>	<b>(\$4,297,547)</b>	<b>\$2,922,057</b>

System Development Fees have been unpredictable in recent years due to the fluctuating market conditions. On average we continue to have favorable results. Lower investment yields and market valuation are evident in the Investment Income line, (reflective of the overall economy). At Miscellaneous Income you see, in 2008 budgeting of anticipated refunds from the Big Dry Creek Interceptor (BDCI) Joint Venture for engineering and construction of capital improvements to the Interceptor. The timing of the engineering efforts, together with necessary revisions to the administration of the BDCI Joint Venture, caused the work to be delayed and therefore caused the anticipated expenditure (Capital Outlay) and refund (Miscellaneous Revenue) to be delayed. Capital improvements were funded for the full amount of the contract (in accordance with the laws of the State of Colorado) even though a very large part of that work would occur in 2009. The 2009 budget provides funds for the carry-over portion of the capital projects. Expenditures were well within the budget for all years. The annual fluctuation for Capital Outlay is evident. With recognition that capital improvements are usually multi-year undertakings, (and that the schedule can be affected by many things), the District budgets

for possible maximum expenditure in any given year and re-budgets the unexpended portion, (for in-progress projects), the following fiscal year to continue the capital program.

## **ECONOMIC CONSIDERATIONS**

The District is located in the economically attractive southeast corridor of the Denver metropolitan area and has growth potential for some time to come. Most of the District's infrastructure is in place. The District's wastewater treatment needs have been secured through intergovernmental agreement with the City of Englewood.

*Duane Tinsley,*  
District Manager

*Note: This Discussion and Analysis contains some forward-looking statements giving our current expectations or forecasts of future events. You can identify these statements by the fact that they do not relate strictly to historical or current facts and include words such as "anticipate", "estimate", "project", "intend", "plan", "believe", "hope", and other words and terms of similar meaning in connection with any discussion of future operating or financial performance. In particular, these include statements relating to future revenues, capital expenditures, the impact of new accounting pronouncements, and other statements regarding matters that are not historical facts or statements of current condition. There are important factors that could cause actual results to differ materially from those expressed or implied by such forward-looking statements. We undertake no obligation (and expressly disclaim any such obligation) to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.*