

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
SOUTHGATE WATER DISTRICT  
FISCAL YEAR 2009**

The Southgate Water 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, 2009. 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 - 2009

Budgetary Comparison Schedule - Budgetary Basis Non-GAAP - 2008

**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 in the following table.

	2007	2008	2009	'08-'09 Change	'08-'09%
Current Assets	\$605,241	\$493,347	\$415,073	(\$78,274)	-15.9%
Property, Plant & Equipment	\$34,520,699	\$35,519,350	\$35,547,754	\$28,404	0.1%
Other Assets	\$36,815,133	\$38,072,080	\$36,598,524	(\$1,473,556)	-3.9%
<b>Total Assets</b>	<b>\$71,941,073</b>	<b>\$74,084,777</b>	<b>\$72,561,351</b>	<b>(\$1,523,426)</b>	<b>-2.1%</b>
Current Liabilities	\$706,503	\$502,364	\$420,426	(\$81,938)	-16.3%
Long Term Liabilities	\$0	\$0	\$0	\$0	0.0%
<b>Total Liabilities</b>	<b>\$706,503</b>	<b>\$502,364</b>	<b>\$420,426</b>	<b>(\$81,938)</b>	<b>-16.3%</b>
Invested in Capital Assets	\$39,962,559	\$40,665,822	\$40,398,838	(\$266,984)	-0.7%
Restricted	\$0	\$0	\$0	\$0	0.0%
Unrestricted	\$31,272,011	\$32,916,591	\$31,742,087	(\$1,174,504)	-3.6%
<b>Total Net Assets</b>	<b>\$71,234,570</b>	<b>\$73,582,413</b>	<b>\$72,140,925</b>	<b>(\$1,441,488)</b>	<b>-2.0%</b>

The reduction in Current Assets, (as compared to 2007 and 2008), 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 improvements in 2009. During 2009 the District's largest capital investments were: 1) water line improvements at County Line Road and South Yosemite Street, and 2) continued development of the Geographic Information System. Other Assets reflects a decrease in the District's fiscal reserves due to capital and operational expenses. The decrease in Current Liabilities is reflective of normal variation over time.

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

	2007	2008	2009	'08-'09 Change	'08-'09%
Operating Revenue	\$74,337	\$51,420	\$18,792	(\$32,628)	-63.5%
Non-Op Revenue	\$2,211,557	\$2,011,566	\$371,897	(\$1,639,669)	-81.5%
<b>Total Revenues</b>	<b>\$2,285,894</b>	<b>\$2,062,986</b>	<b>\$390,689</b>	<b>(\$1,672,297)</b>	<b>-81.1%</b>
Depreciation Expense	\$1,292,989	\$1,341,542	\$1,425,477	\$83,935	6.3%
Govt. & Admin. Expense	\$568,957	\$652,324	\$748,528	\$96,204	14.7%
Other Operating Expense	\$829,166	\$835,140	\$983,408	\$148,268	17.8%
Non-Op Expense	\$0	\$0	\$0	\$0	0.0%
<b>Total Expenses</b>	<b>\$2,691,112</b>	<b>\$2,829,006</b>	<b>\$3,157,413</b>	<b>\$328,407</b>	<b>11.6%</b>
Income/Loss Before Contributions	(\$405,218)	(\$766,020)	(\$2,766,724)	(\$2,000,704)	261.2%
Capital Contributions	\$2,411,973	\$3,113,863	\$1,325,236	(\$1,788,627)	-57.4%
	\$2,006,755	\$2,347,843	(\$1,441,488)	(\$3,789,331)	-161.4%
<b>Net Assets - Beginning</b>	<b>\$69,227,815</b>	<b>\$71,234,570</b>	<b>\$73,582,413</b>	<b>\$2,347,843</b>	<b>3.3%</b>
<b>Net Assets - End</b>	<b>\$71,234,570</b>	<b>\$73,582,413</b>	<b>\$72,140,925</b>	<b>(\$1,441,488)</b>	<b>-2.0%</b>

The District funds its activities from interest earnings, new tap sales (included in Capital Contributions) and miscellaneous revenues. The District's property tax was eliminated several years ago. 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. The District has determined to augment its Operating Revenues through initiation, in 2010, of a service charge on the customers of the District.

Governmental and Administration Expense (14.7% increase) and Other Operating Expense (17.8 % increase) reflect increased operational and system repair costs. Income/Loss Before Contributions and Capital Contributions reflect the effects of the economic and development down-turn and the need to turn to the above referenced fiscal reserves. That situation is expected to recover with time. Even with the economic downturn, the overall health of the District remains strong as 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 2009, the District had invested \$55.5 million, (less \$20 million in accumulated depreciation), in a broad range of infrastructure, including four water reservoirs (with storage capacity of 11 million gallons), one pump station, approximately 235 miles of transmission and distribution lines, maintenance and administration facilities, vehicles, and equipment, as shown in the table below.

	2007	2008	2009	'08-'09 Change	'08-'09%
Water System	\$43,818,248	\$45,356,403	<b>\$46,918,316</b>	\$1,561,913	3.4%
Pumping & Storage	\$2,883,901	\$5,544,150	<b>\$5,544,150</b>	\$0	0.0%
Studies	\$103,263	\$103,263	<b>\$130,510</b>	\$27,247	26.4%
Capital Equipment	\$626,059	\$651,314	<b>\$687,413</b>	\$36,099	5.5%
Building & Land	\$1,516,297	\$1,812,001	<b>\$1,804,354</b>	(\$7,647)	-0.4%
Construction in Progress	\$2,865,168	\$676,351	<b>\$450,000</b>	(\$226,351)	-33.5%
<b>Subtotal</b>	<u>\$51,812,936</u>	<u>\$54,143,482</u>	<u><b>\$55,534,743</b></u>	<u>\$1,391,261</u>	<u>2.6%</u>
Accumulated Depreciation	(\$17,292,237)	(\$18,624,132)	<b>(\$19,986,989)</b>	(\$1,362,857)	7.3%
<b>Net Property, Plant and Equipment</b>	<b>\$34,520,699</b>	<b>\$35,519,350</b>	<b>\$35,547,754</b>	<b>\$28,404</b>	<b>0.1%</b>

This table reflects the results of the GASB 34 asset valuation and depreciation efforts. With completion of the pump station and reservoir improvements the capacity related projects set forth in the District's master plan have been 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 2008 or 2009 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 2007, 2008 and 2009.

	2007		2008		2009	
	Budget	Actual	Budget	Actual	Budget	Actual
System Devel Fees	\$1,531,440	\$2,071,564	\$1,397,280	\$1,585,408	\$1,111,950	\$515,374
Investment Income	\$1,229,314	\$2,211,557	\$1,445,982	\$2,011,566	\$1,084,442	\$371,897
Miscellaneous Income	\$45,000	\$78,245	\$50,000	\$50,914	\$45,000	\$18,792
<b>Total Revenues</b>	<b>\$2,805,754</b>	<b>\$4,361,366</b>	<b>\$2,893,262</b>	<b>\$3,647,978</b>	<b>\$2,241,392</b>	<b>\$906,063</b>
Admin & Operations	\$1,271,626	\$1,155,721	\$1,291,990	\$1,077,908	\$1,354,525	\$1,332,269
Professional Services	\$73,000	\$88,664	\$89,250	\$123,457	\$81,500	\$104,279
Debt Service	\$0	\$0	\$0	\$0	\$0	\$0
Capital Outlay	\$3,815,000	\$2,708,575	\$1,860,000	\$802,088	\$1,555,500	\$647,513
<b>Total Expenditures</b>	<b>\$5,159,626</b>	<b>\$3,947,960</b>	<b>\$3,241,240</b>	<b>\$2,003,398</b>	<b>\$2,991,525</b>	<b>\$2,084,061</b>
<b>Revenues Less Expenditures</b>	<b>(\$2,353,872)</b>	<b>\$413,416</b>	<b>(\$348,028)</b>	<b>\$1,644,580</b>	<b>(\$750,133)</b>	<b>(\$1,177,998)</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). While we had anticipated the need to expend monies from the District's reserves to cover capital improvements in 2007 and 2008, the actual expenditures were well within the revenues. The 2009 numbers reflect the greater than anticipated draw on reserves due to the lower than expected revenues. 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 water resource needs have been met, (through a well drafted water resource agreement with the Denver Water Department and adjudication of ground water as a backup resource).

*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.*