



**ANNUAL STOCKHOLDERS' REPORT  
FISCAL YEAR 2015-2016  
&  
NOTICE OF  
ANNUAL STOCKHOLDERS' MEETING  
FEBRUARY 23, 2017**





May 11, 1952 – October 9, 2016

It is with great sadness that we announce the passing of our beloved employee, Barbara Karady. Barbara was a dedicated and valued employee at Valencia Heights Water Company (VHWC) with over 24 years of service. She was a highly knowledgeable employee with consistent work ethic that will be a great example for all of us to remember. She will be greatly missed and we will always remember her with love and admiration. All of us here at VHWC are proud to have known her and worked with her.

Barbara was set to retire in May 2017 but died unexpectedly. She is survived by her daughter and son, who were her absolute pride and joy, Bari (Sam) and Jacob (Jaime) along with three grandchildren, Jayden, Theodore and Bella.

## CUSTOMER SHUT-OFF VALVE NOTICE

In emergency situations, it is crucial that all properties have an operating shut-off valve installed at the home and at the customer side of the meter. The shut-off valve near the home controls the water going into the home, and the shut-off valve located on the property-side of the meter controls the water coming into the property. Not all properties have shut-off valves on their property, and it is important for each resident to know whether or not a shut-off valve exists on their property. If a shut-off valve does not exist, Valencia Heights Water Company (VHWC) highly recommends that they are installed.

When a shut-off valve, as described above does not exist on your property, it is recommended that you call Valencia Heights Water Company (VHWC) **before** turning any valve within the meter box. The valve in the meter box closest to the street is company property. Turning the Company valve and causing damage to it could result in significant cost to the property owner.

All facilities owned or maintained by VHWC, including but not limited to reservoirs, wells, pump stations, main water lines, fire hydrants, water meters and/or radios are not to be tampered with by anyone other than authorized VHWC personnel. If you are unsure if the equipment belongs to you or the water company, it is recommended that you call VHWC (626-332-8935). Our field staff is available 24 hours a day. If there is any damage or repairs needed as a result of your actions, you, the owner will be responsible for the cost of the repairs.

When water service has been shut off at a property, for any reason, it will not be restored until the property's existing issue is resolved whether it is repairs, past-due bill, or new buyer requirements. Once a meter is shut off by VHWC personnel, service can only be restored by VHWC personnel. If a meter is tampered with by **anyone** other than VHWC personnel, then a **\$500 Tampering Fee** may be charged to the shareholder or consumer account. If a meter is tampered with, it will be locked off or may be removed at the expense of shareholder or consumer until all fees (labor & materials), and past-due bills are paid; and if required, all documents be submitted to transfer water stock. The reinstallation of the meter will be at the expense of the shareholder or consumer account.

### California Penal Code Section 498

"Any person who, with intent to obtain for himself or herself utility service without paying the full lawful charge therefor, or with intent to enable another person to do so, or with intent to deprive any utility of any part of the full lawful charge for utility services it provides, commits, authorizes, solicits, aids, or abets any of the following shall be guilty of a misdemeanor."

The below situations are two (2) examples of tampering:

- Prevents any utility meter, or other device used in determining the charge for utility services, from accurately performing its measuring function by tampering or by any other means.
- Tamper with any property owned by or used by the utility to provide utility service.

After 45 years of serving the community, Norman Richman has retired from the Valencia Heights Water Company Board of Directors. During those years, Norman put in countless hours as a Board member, always putting the communities' best interest first. Norm joined the Board in 1971 and served as Board Chairman many times throughout his career. During the rate setting process he would always ask the question: "Are these rates equitable to the consumer and the Company." He took a special interest in establishing fair and equitable water rates, eventually developing a tiered water rate structure, the first of its kind for a water company, nearly 30 years ago.

Norm was a strong advocate for Capital Improvements and making sure funds were available to maintain the water system. During the past 45 years, Mr. Richman was a fervent driving force for Valencia Heights Water Company, an advocate for the Company and most of all an advocate for the Stockholder. Norm's vision and leadership will be admired and missed.

I would like to personally thank him for his leadership and mentoring during my tenure as General Manager.



VHWC Board Members and GM honoring Norm with a plaque for his 45 years of service. Left: Robert Ghirelli, Curtis Feese, Eugene Jacobs, Dave Michalko, Norman Richman and Wayne Partee

# ANNUAL STOCKHOLDERS' MEETING

**DAY:** Thursday

**DATE:** February 23, 2017

**TIME:** 7:00 p.m.

**LOCATION:** **South Hills Country Club**  
2655 South Citrus Street  
West Covina, CA 91791

***Your vote is important!***

*Please remember to mail the enclosed proxy card  
before February 16, 2017.*

*Your vote is necessary for the Board to conduct  
its business.*

***We look forward to seeing you at the meeting!***

**PLEASE SIGN THE ENCLOSED PROXY CARD** and return it as soon as possible with your vote indicated. This allows the required business of the Company to be properly conducted. Should you attend the meeting, you may vote in person.

The Board of Directors and Management solicit your affirmative proxy vote for any and all matters presented at the Annual Meeting for approval.

**The Board of Directors Proposed for Election is as Follows:**

Sylvia Beltran	Incumbent/Senior Project Coordinator/ Arellano Associates
Curtis Feese	Incumbent/ Attorney S.C. Gas, Retired
Robert Ghirelli	Incumbent/ Assistant G.M., Orange Co. Sanitation District
Eugene Jacobs	Incumbent/General Contractor
Daniel Liese	Incumbent/Principal/of AEPC Group, LLC
Wayne Partee	Incumbent/Pres., CEO of Partee Insurance Associates, Inc.
Ronald Wheeler	Incumbent/Facilities Manager, MWD of So. Cal., Retired

**PLEASE SIGN THE PROXY CARD EXACTLY AS YOUR NAME(S) APPEAR(S) ON THE CARD.**

**IF STOCK IS JOINTLY-HELD THEN ALL OWNERS MUST SIGN THE PROXY CARD.**

**\*\*PLEASE RETURN SIGNED PROXY CARD\*\*  
BY THURSDAY, FEBRUARY 16, 2017**

# VALENCIA HEIGHTS WATER COMPANY

West Covina, California

Los Angeles County

## **BOARD OF DIRECTORS**

<b><u>MEMBER</u></b>	<b><u>OFFICE</u></b>	<b><u>TERM EXPIRES</u></b>	<b><u>YEARS OF SERVICE</u></b>
Robert Ghirelli	Chairman	February 17, 2017	4
Ronald Wheeler	Vice-Chairman	February 17, 2017	8
Curtis Feese	Treasurer	February 17, 2017	17
Wayne Partee	Secretary	February 17, 2017	20
Sylvia Beltran	Director	February 17, 2017	1
Eugene Jacobs	Director	February 17, 2017	20
Daniel Liese	Director	February 17, 2017	12

## **ADMINISTRATION**

David Michalko	General Manager	30
Gloria Galindo	Executive Administrator	14

## **OFFICE**

Elizabeth Lopez	Customer Service Assistant	1
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## **FIELD**

Tim Pacheco	Water System Supervisor	14
Ernest Romero	Water Tech II	7
Chad Latourelle	Water Tech I	5

# **VALENCIA HEIGHTS WATER COMPANY**

## **Annual Stockholders' Meeting**

**Thursday, February 23, 2017**

**7:00 - 8:00 p.m.**

**South Hills Country Club**

**2655 South Citrus Street - West Covina, CA 91791**

## **A G E N D A**

1. Open Meeting
2. General Manager's Report
  - a. Projects
  - b. Water Supply
3. Report for a Quorum
4. Call to Order
5. Approval of Minutes of February 17, 2016
6. Approval of the Financial Statements
  - a. Report from the Investment Committee
7. Ratification of Actions Taken by the Board for Year-Ending October 31, 2016
8. Election of the Board
  - a. Nomination of Directors
  - b. Motion to Close Nominations
  - c. Election of Directors
9. Discussions, Questions and Answers
10. Other Business
11. Motion to Adjourn



**VALENCIA HEIGHTS WATER COMPANY**  
**ANNUAL STOCKHOLDERS' MEETING MINUTES**  
**Mesa Elementary School, West Covina, CA 91791**  
**Wednesday, February 17, 2016, 7:00 p.m.**

- Present:** D. Liese, Chairman; B. Ghirelli, Vice-Chairman; C. Feese, Treasurer; Wayne Partee, Secretary; G. Jacobs, Director; N. Richman, Director; R. Wheeler, Director
- Staff:** D. Michalko, General Manager; B. Karady, Executive Administrator; G. Galindo, Customer Support
- Stockholders:** Sandy Feese, Ann Lee, Kevin McCann, Elsbeth Schultheiss, Adolf Schultheiss, Dave Minto
- Others:** Aida Babayan, Merrill Lynch; N. Schultheiss

The Chairman, Daniel Liese welcomed everyone and introduced the Board of Directors; the General Manager, Dave Michalko; and Staff, Barbara Karady, Gloria Galindo. D. Liese welcomed and thanked everyone for coming.

1. Open Meeting  
The Chairman opened the meeting at 7:00 p.m., welcomed and thanked everyone for attending.
2. General Manager's Report
  - a. Water Supply  
The General Manager reported on the drought, and how it is affecting the local water supply, and that there is a high likelihood that additional rationing will occur if it continues to be dry.
3. Report for a Quorum  
The Chairman asked if there was a quorum present. G. Galindo reported that a quorum was present as follows:

2442 Shares Outstanding

1222 Shares Required for a Quorum

1881 Shares Present and/or Voting
4. Call to Order  
After hearing that a quorum was present, the Chairman called the meeting to order.  
The Annual Shareholders' Meeting was called to order at 7:10 p.m.

**Annual Stockholders' Meeting Minutes**

February 17, 2016

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5. Approval of Minutes of February 18, 2015  
The Chairman asked if there were any comments on the 2015 Annual Meeting Minutes. Since there were no comments, the Chairman asked for the approval of the minutes.
- Motion by R. Ghirelli and seconded by R. Wheeler to approve the minutes of February 18, 2015.  
Motion passed.
- |         |     |
|---------|-----|
| For     | 870 |
| Against | 58  |
| Abstain | 953 |
6. Approval of the Financial Statements
- a. Report from the Investment Committee (Guest Aida Babayan, Merrill Lynch)  
The Chairman asked for a motion to approve of the Financial Statements for 2014-2015.
- Motion by W. Partee and seconded by K. McCann to approve the Financial Statements as presented.  
Motion passed.
- |         |     |
|---------|-----|
| For     | 870 |
| Against | 58  |
| Abstain | 953 |
7. Ratification of Actions Taken by the Board for the Year-Ending October 31, 2015  
The Chairman asked for a motion to ratify the actions taken by the Board for year-ending October 31, 2015.
- Motion by K. McCann and seconded by A. Schultheiss to ratify the Board's actions for year-ending October 31, 2015.  
Motion passed.
- |         |     |
|---------|-----|
| For     | 870 |
| Against | 58  |
| Abstain | 953 |
8. Election of Directors  
The Chairman opened nominations for the current Board.
- Motion by W. Partee and seconded by D. Minto to open nominations.  
Motion passed.
- |         |     |
|---------|-----|
| For     | 870 |
| Against | 58  |
| Abstain | 953 |

**Annual Stockholders’ Meeting Minutes**

February 17, 2016

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- Motion by D. Minto and seconded by W. Partee to close nominations.  
Motion passed

For	870
Against	58
Abstain	953

- Motion by D. Minto and seconded by W. Partee to elect the current slate of Directors.  
Motion passed

For	870
Against	58
Abstain	953

9. Discussions, Questions and Answers  
There were no questions brought before the Board at this time.

10. Other Business  
There was no other business to come before the Board.

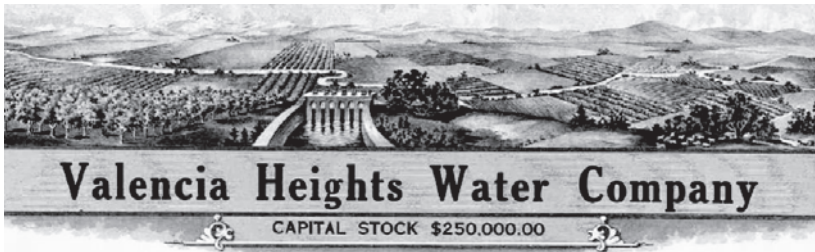
11. Motion to Adjourn  
The Chairman asked for a motion to adjourn the Annual Shareholders’ Meeting at 7:18 p.m.
- Motion by D. Minto and seconded by K. McCann to adjourn the 2016 Annual Shareholders’ Meeting.  
Motion passed.

For	870
Against	58
Abstain	953

Respectfully Submitted,

<hr/> Wayne Partee - Secretary	<hr/> Date
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# MANAGER'S REPORT



*INCORPORATED NOVEMBER 1912 UNDER THE LAWS OF THE STATE OF CALIFORNIA*

Last year I wrote:

“As Californians look forward to the likelihood of a wet winter, this is not the time to throw out what you, our customers, have been practicing for the last several years.” As you know, the wet winter never materialized in Southern California. Therefore, for a second straight year, we asked that everyone cut their water use by 25 percent, due to the Executive Order, put in place by the Governor and the State Water Resources Control Board (SWRCB). The 25 percent conservation was again achieved by reducing outdoor watering to just two days per week.

You as a community, have done an excellent job reducing both water use and water waste. It continues to be nearly a full-time job for one staff member to assist our customers with leaks and unexplained usages. We have saved millions of gallons of water by reducing water use and water waste, helping to preserve our local groundwater supply. The Board would like to thank everyone for all their efforts. This water saved is water that we did not need to pump from the ground, allowing us to leave it in the ground for another day.

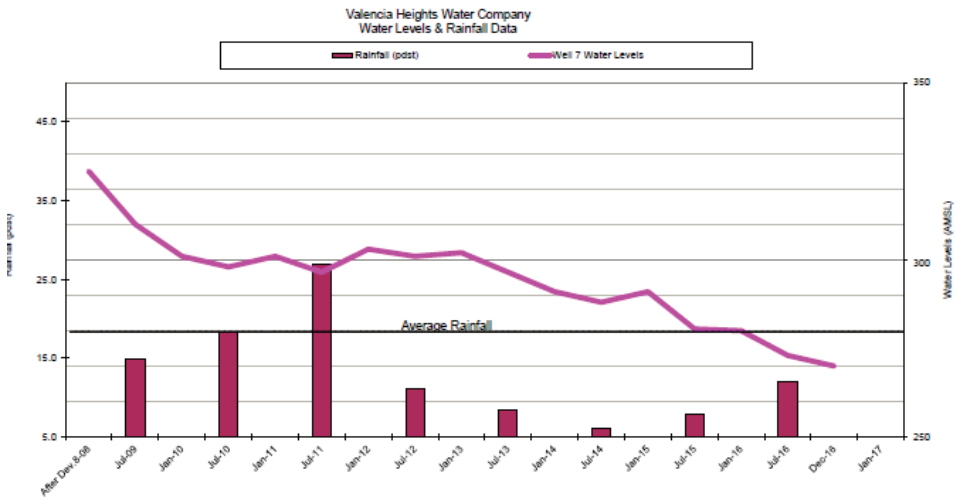
## **Supply Projections**

So, what do supplies look like for 2017? The Main San Gabriel Basin (Basin) is down over 500,000 acre-feet. This is the Groundwater Basin in which the Company pumps. If the Basin were a surface water lake, in which you could see the water, it would spread from San Dimas to Pasadena, and would be down more than 50 feet. For those of you who drive on the 605 Freeway, notice that the mining pits no longer have water in them. The reservoirs in the San Gabriel Canyon, which hold about 85,000 acre-feet. have not been filled from rainfall and snow melt in several years.

The basin is at a record low and has reached a critical level for the Basin to meet the needs of the residents of the San Gabriel Valley. As a result, the Main San Gabriel Basin Watermaster (Watermaster), the Court appointed entity created to

manage the Basin, has developed a plan to purchase import water to help augment the lack of Stormwater run-off. This program will cost the producers more than \$30,000,000 annually to help offset the lack of local Stormwater. The Company’s portion of this cost will start at approximately a \$0.10 per unit surcharge on your water bill to approximately a \$0.36 per unit of water used surcharge. For the average customer, that uses an average of 40 units of water a month, the cost will range from; \$4 a month in 2017 to \$14.40 a month by 2022. The benefit of the assessment is to manage the Basin in a way to ensure a reliable water supply in the future without the need for mandatory conservation like we have seen the last several years.

Below is a table showing the drop in the ground water level at the Company’s Well No. 7.



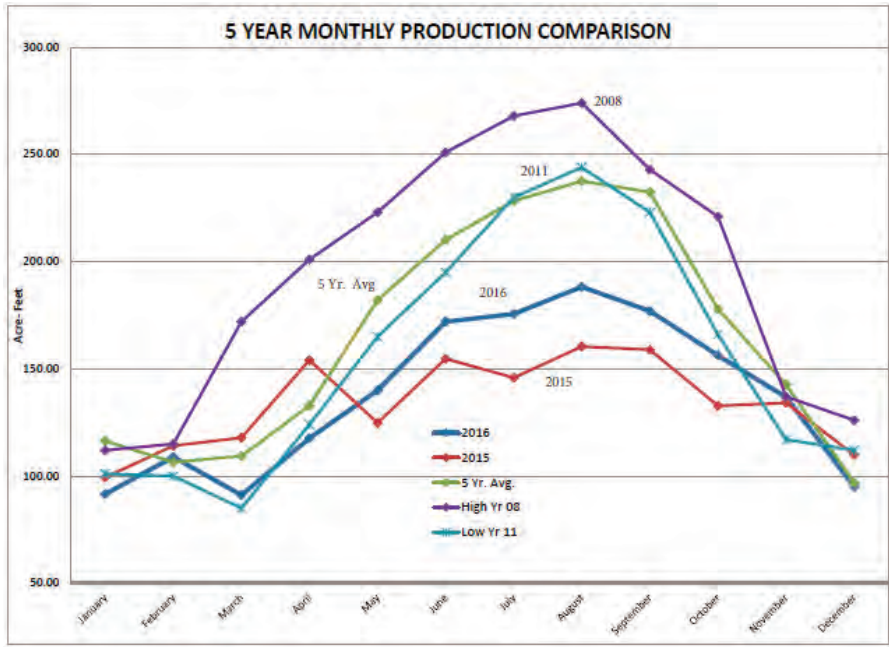
Currently, the water level in Well No. 7 stands at 267 feet above mean sea level. This is a drop of another 10 feet from this same time last year. The Company continues to diversify its water supply options to save the ground water in the areas of the Company wells until such time that the Basin level begins to recover. As part of the annual planning and budget process the Board reviews these options to ensure a safe and reliable water supply. This philosophy has helped to maintain groundwater levels in the area of the Company wells. However, these changes in water supply options do come with an additional cost, but first and foremost is a reliable water supply for the consumer.

## State Drought Regulations

As I mentioned earlier, our customers met and even exceeded in some months, the mandatory reductions the State placed on the Company for 2016. At this time, it is unclear what regulations will still be in place for 2017. So far this rainy season has

brought promise to all of California. However, we will not know the full extent of the winter months until Spring, and if rainfall is at best, “normal” there will remain, some level of mandatory conservation. Only after additional wet years occur, do we foresee “drought” regulations going away. The State is currently working on permanent conservation regulations limiting outdoor water use. It is still too early to know the effect of the new regulations, and will likely take most of 2017 before they can be approved and enacted.

The table below shows just how dramatic the summer water usage was reduced in our area.



## Water Rates

In September 2016, as part of the budget process, the Board approved rate increases for each of the next two years. The first became effective November 2016. This increase averaged about 5% system-wide. The second increase will become effective November 2017 and will be about 5.5%. However, based on current water supplies and sales, this could be revised during the September 2017 budget process. Some of these rate increases are a consequence of the drought and reduced water sales. However, they are also attributed to the continuing increased cost of doing business, and most importantly the robust Capital Improvement projects in the coming years. The Company continues to look at, and use, technology to improve efficiency in operations, communication with the consumer and billing. While there may be some upfront cost associated with this philosophy, there are significant long-term savings in these investments.

## **Capital Improvement Plans**

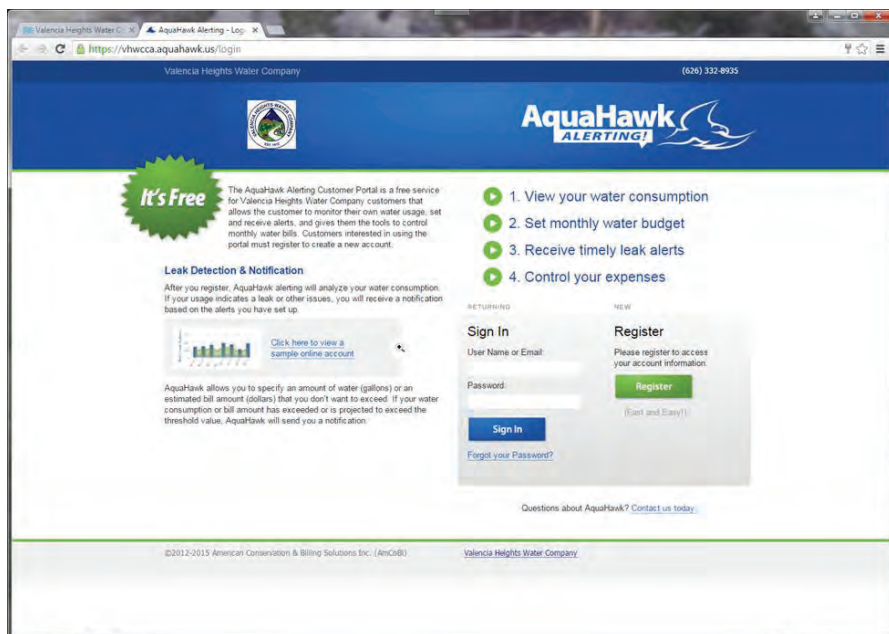
Enclosed in the Annual Report is the 5-year Capital Improvement Plan. There are a few significant changes from last year that I wish to point out. First, we have been carrying-over several projects that are now complete, or nearing completion. The big change in this plan is the Reservoir No. 2 Transmission Line and Pump Station Rehab Project. This work was originally spread over two (2) years and has now been combined into one project for cost-efficiency. By combining the projects and shutting down the site for a few months, there are significant reductions in the temporary work that would otherwise be required. However, with that being said, the Board decided to apply for a State Revolving Fund (SRF) loan through SWRCB, for 100 percent of the cost of the project. The SRF loan will enable the Company to borrow funds for twenty years at less than two (2) percent interest. The SRF loan allows the Company to maintain its' reserves for other projects or unforeseen emergencies. The annual repayment of the SRF loan for this project over the next 20 years is about \$90,000.

Additional projects currently in progress are;

- The replacement of the wood roof at Reservoir No.3, with a steel roof and structure.
- The replacement of 1250 feet of old 6-inch water line with new 8-inch waterline in the 2400-2500 blocks of Buenos Aires Drive, (from Dameral Drive, west to just short of Lorencita Drive).
- The replacement of the old steel line in Lorencita Drive, east of Monte Verde, through to the City of West Covina section of Lorencita Drive.
- Lastly, the SCADA system. The current SCADA system will not allow for upgrades due to the dramatic change in technology over the past 15 years. The new System, being supplied by a leader in water system integration, will allow for continued upgrades and replacement as necessary, unlike the current technology. The SCADA system is the heart of the water system, it controls all the pumps and reservoirs within the water system and notifies the operators when there is any type of problem. The SCADA system also provides site security, a critical component in this day and age. A portion of this project will be funded by the SRF loan discussed above.

The complete 5-year plan is on page 17 of the report. This plan is updated annually based on the Companys' most current needs, and review of the water system operations.

## Website and Links



Below is a brief explanation of the AquaHawk System and the benefits it provides. You will find the link under **“View Water Usage” or “Take Control of Your Water Bill”**.

Each year, we would like to continue directing your attention to the Company’s website [vhwc.org](http://vhwc.org). We hope that the website will be a useful tool to communicate with our customers. One such tool is for water outages. If water service appears to be out at your property, please check the website to see if there is an outage affecting your area. Staff will make every attempt to post the most updated information regarding the location and duration of an outage on the website. This information is posted on the upper right-hand corner of the homepage of the website. It is our goal to have the information posted within 30 minutes of an outage, and we will update the website when new information is available. Once the outage is posted, this is a helpful tool to check on the repair progress and/or estimated completion time. We hope that the site will help keep you informed about current water outages, and when service will be restored. You can also follow us on Twitter @[valenciaheights](https://twitter.com/valenciaheights) as another source of information. We will periodically send tweets about any useful information; as well as any water outages in the water system. To help our customers know what is going on, especially during outages and emergencies, we ask that every one of our customers sign up to follow @[valenciaheights](https://twitter.com/valenciaheights) on Twitter.



You are now able to view and pay your water bill online. Credit card payments can be made online through a link on the website ([vhwc.org](http://vhwc.org)). Credit cards **will not** be accepted at the office. Also, customers can now monitor their water usage online with the goal of reducing unexplained water loss, by using the **AQUAHAWK** System.

AquaHawk Alerting allows our customers to take control of their water bill and water usage through monitoring and alerting. Register your water account by visiting our website, [vhwc.org](http://vhwc.org). Once your water account is registered, you will have access to your daily usage, set alerts on your account, and much more. By setting alerts, you will be notified by text or email if the water bill has exceeded a user-selected, specific dollar or usage amount, or if water has been running continuously at your property. Also, by registering your account, and giving the most current contact information, VHWC will be able to contact you during any emergency situation. Since the inception of Aquahawk, the Company has been able to notify many customers of possible leaks or continual usage at their properties. If a customer signs up directly, you will be notified much quicker, which will provide greater savings for you, of both money and water. To register your account, please visit our website at [vhwc.org](http://vhwc.org) and follow the link.

## **Water Pressure and Regulators**

A common call received at the office is about water pressure and pressure regulators. The area that the Company provides water service to, varies greatly in elevation. Since the water lines must traverse up and down the hills, pressure can vary greatly from one block to the next. Water pressure within your home should be sufficient at about 50 pounds per square inch (psi), and pressure greater than **60 psi** can cause damage to appliances within the home. The pressure at your water meter can range from **40 psi to 160 psi**, but will not vary more than 5psi. For this reason, it is critical that you monitor and maintain the pressure regulator at your property. Pressure regulators should last three (3) to five (5) years; however, there is no guarantee how long it will last. The pressure within the water system seldom varies and **cannot** be adjusted by the Water Company. The pressure at your property is determined by the location (elevation) of the reservoir from which you are served. If you notice any change in the pressure within your home, you should consider contacting a plumber to have your pressure regulator serviced. Building codes require that all homes have a pressure regulator, and it is the **homeowner's responsibility** to service, maintain or replace the pressure regulator as needed.

## **New Mutual Association**

The Company continues to assist with the growth and development of CalMutuals. The Association continues to grow and catch the eye, and earn the respect of the State Legislature. In 2016, CalMutuals, formed JPRIMA, the Joint Powers Risk and Insurance Management Authority.

This authority will provide insurance to Mutuals and other water agencies throughout the State, and will also be the primary funding source for both organizations. The Associations website is [www.calmutuals.org](http://www.calmutuals.org). Please take a minute to see what is happening in the world of Mutual Water Companies. There are over 500 Mutual Water Companies in the State, and it is important that there be support and a voice for Mutuals in the State.

Finally, as in the past, the following pages contain two years of audited financial statements. Please take a few moments to review them and bring your questions to the Annual Meeting. This years' Annual Stockholders' Meeting will be held at South Hills Country Club, on Thursday, February 23, 2017, at 7 p.m. We look forward to your attendance to discuss the business and success of the Company.

*Sincerely,  
Dave Michalko  
General Manager*

# VALENCIA HEIGHTS WATER COMPANY

## Capital Improvement Projects 2017-2021

### 2017

Buenos Aires Waterline	\$ 200,000
Lorencita Drive Waterline	\$ 150,000
SCADA Upgrades	\$ 275,000
Emergency Preparedness Equipment/Electrical	\$ 50,000
Capital Debt Payment(s) (Reservoir #2)	\$ 130,000
Mapping/Miscellaneous System Work	\$ 15,000
<b>Total</b>	<b><u><u>\$ 820,000</u></u></b>

### 2018

Pick-up Truck Replacement	\$ 35,000
Well No. 7 Rehab	\$ 100,000
Reservoir 5 Transmission Line Replacement	\$ 175,000
Emergency Preparedness Equipment	\$ 50,000
Capital Debt Payment(s) (Reservoir #2)	\$ 130,000
Miscellaneous System Work/Electrical	\$ 40,000
<b>Total</b>	<b><u><u>\$ 530,000</u></u></b>

### 2019

Reservoir No. 6A Inside Rehab	\$ 125,000
Waterline, Lorencita to Buenos Aires	\$ 250,000
Capital Debt Payment(s) (Reservoir #2)	\$ 130,000
Miscellaneous System Work/Electrical	\$ 40,000
<b>Total</b>	<b><u><u>\$ 545,000</u></u></b>

### 2020

Reservoir No. 6B Inside Rehab	\$ 125,000
Golden Bough Line	\$ 250,000
Capital Debt Payment(s) (Reservoir #2)	\$ 90,000
Miscellaneous System Work	\$ 10,000
<b>Total</b>	<b><u><u>\$ 475,000</u></u></b>

### 2021

Parkview Water Line (under freeway)	\$ 300,000
Holt Avenue Line Phase 1, east	\$ 150,000
Capital Debt Payment(s) (Reservoir #2)	\$ 90,000
Miscellaneous System Work	\$ 10,000
<b>Total</b>	<b><u><u>\$ 550,000</u></u></b>

**Estimated Cost Over 5 Years \$ 2,920,000**

**Average Cost Per Year \$ 584,000**

### Additional/Future Projects

Emergency Portable Generator(s) and Set-up  
 Buenos Aires Line, Limecrest to Damerl  
 Additional Reservoir Resurfacing  
 Potential Treatment Facility/Softening/Perchlorate  
 6" Line at the End of Buenos Aires

Buenos Aires and Lorencita Lines  
 Cameron and Grand Crossing  
 Additional Waterline Replacements  
 Service Line Replacements (System-Wide)  
 Virginia Avenue Mainline

**VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)**

**FINANCIAL STATEMENTS**

**WITH REPORT ON AUDIT  
BY INDEPENDENT CERTIFIED  
PUBLIC ACCOUNTANTS**

**OCTOBER 31, 2016 AND 2015**

**VALENCIA HEIGHTS WATER COMPANY**  
**(A California Mutual Water Company)**

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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
Valencia Heights Water Company  
West Covina, California

We have audited the accompanying financial statements of Valencia Heights Water Company (a nonprofit organization) (the Company), which comprise the statements of financial position as of October 31, 2016 and 2015, and the related statements of operations, comprehensive income, changes in members' equity and cash flows for the years then ended, and the related notes to the financial statements.

### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditors' Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of October 31, 2016 and 2015, and the results of its operations and comprehensive income, changes in its members' equity and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*White Nelson Hill Evans LLP*

Irvine, California

January 6, 2017

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

STATEMENTS OF FINANCIAL POSITION

October 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 1,154,405	\$ 1,029,896
Investments	2,218,883	1,688,279
Accounts receivable	249,736	216,321
Interest receivable	15,884	11,089
Inventory	68,025	66,868
Note receivable, current portion	-	63,266
	<u>3,706,933</u>	<u>3,075,719</u>
TOTAL CURRENT ASSETS		
	<u>5,287,489</u>	<u>5,268,293</u>
PROPERTY, PLANT AND EQUIPMENT, NET		
	<u>5,287,489</u>	<u>5,268,293</u>
OTHER ASSETS:		
Deposit	6,250	6,250
Investment in Covina Irrigating Company	918,890	918,890
Deferred compensation plan assets	110,797	98,768
Water rights	720,000	720,000
Prepaid water	423,793	215,893
Deferred income taxes receivable	-	399
Note receivable, net of current portion	-	468,407
	<u>2,179,730</u>	<u>2,428,607</u>
TOTAL OTHER ASSETS		
	<u>2,179,730</u>	<u>2,428,607</u>
TOTAL ASSETS	<u>\$ 11,174,152</u>	<u>\$ 10,772,619</u>

(Continued)

See accompanying notes to financial statements.



VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

STATEMENTS OF FINANCIAL POSITION  
(CONTINUED)

October 31, 2016 and 2015

	2016	2015
LIABILITIES AND MEMBERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$ 125,438	\$ 184,509
Income taxes payable	40,153	1,390
Note payable, current portion	37,881	31,642
	<u>203,472</u>	<u>217,541</u>
TOTAL CURRENT LIABILITIES	<u>203,472</u>	<u>217,541</u>
LONG-TERM LIABILITIES:		
Deferred income taxes payable	492	-
Deferred compensation vested liability	110,797	98,768
Compensated absences	45,238	53,948
Notes payable, net of current portion	80,364	23,369
	<u>236,891</u>	<u>176,085</u>
TOTAL LONG-TERM LIABILITIES	<u>236,891</u>	<u>176,085</u>
TOTAL LIABILITIES	<u>440,363</u>	<u>393,626</u>
MEMBERS' EQUITY:		
Contributions in aid of construction, net of amortization	1,545,578	1,618,231
Common stock - 10,000 shares authorized; \$100 par value; 1,004 and 1,032 shares issued and outstanding as of October 31, 2016 and 2015, respectively	100,400	103,200
Class A common stock - 10,000 shares authorized; \$100 par value; 1,443 shares issued and outstanding as of October 31, 2016; 1,406 shares issued and outstanding as of October 31, 2015	144,300	140,600
Additional paid-in capital	1,217,095	1,107,295
Accumulated other comprehensive income (loss)	12,342	(4,120)
Retained earnings	7,714,074	7,413,787
	<u>10,733,789</u>	<u>10,378,993</u>
TOTAL MEMBERS' EQUITY	<u>10,733,789</u>	<u>10,378,993</u>
TOTAL LIABILITIES AND MEMBERS' EQUITY	<u>\$ 11,174,152</u>	<u>\$ 10,772,619</u>

See accompanying notes to financial statements.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

STATEMENTS OF OPERATIONS

For the years ended October 31, 2016 and 2015

	2016	2015
OPERATING REVENUES:		
Water sales and services	\$ 2,695,918	\$ 2,533,996
OPERATING EXPENSES:		
Utility plant operation expenses:		
Purchased water	684,980	542,173
Purchased power	217,565	209,509
Leased water rights	60,219	116,787
Operations	96,753	78,271
Water testing	6,318	7,932
Vehicles	27,476	29,972
Repairs and maintenance	91,861	112,028
Total utility plant operation expenses	<u>1,185,172</u>	<u>1,096,672</u>
Depreciation	<u>265,389</u>	<u>259,684</u>
General and administrative expenses:		
Salaries and benefits	635,328	591,612
Directors' fees	27,250	28,150
Professional services and permitting	121,302	47,662
Office expenses and utilities	62,665	63,427
Insurance	30,902	30,789
Taxes and licenses	51,227	50,283
Assessments	53,129	51,645
Total general and administrative expenses	<u>981,803</u>	<u>863,568</u>
TOTAL OPERATING EXPENSES	<u>2,432,364</u>	<u>2,219,924</u>
INCOME FROM OPERATIONS	<u>263,554</u>	<u>314,072</u>
OTHER INCOME (EXPENSE):		
Investment income:		
Interest and dividend income	74,756	50,746
Net realized gains (losses)	(10,271)	(3,773)
Investment expenses	(640)	(450)
Total investment income	<u>63,845</u>	<u>46,523</u>
Other income	25,435	25,040
Interest expense	(694)	(1,245)
TOTAL OTHER INCOME (EXPENSE)	<u>88,586</u>	<u>70,318</u>
INCOME BEFORE TAXES	352,140	384,390
PROVISION FOR INCOME TAXES - CURRENT	<u>(51,853)</u>	<u>(9,990)</u>
NET INCOME	<u>\$ 300,287</u>	<u>\$ 374,400</u>

See accompanying notes to financial statements.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

STATEMENTS OF COMPREHENSIVE INCOME

For the years ended October 31, 2016 and 2015

	2016	2015
NET INCOME	<u>\$ 300,287</u>	<u>\$ 374,400</u>
OTHER COMPREHENSIVE INCOME, NET OF TAX:		
Unrealized gains (losses) on securities available for sale:		
Unrealized holding gains (losses) arising during period	28,329	(21,995)
Tax (expense) or benefit	<u>(2,504)</u>	<u>1,944</u>
	<u>25,825</u>	<u>(20,051)</u>
Adjustment for reclassification of gains and losses included in net income:		
Realized gains (losses)	(10,271)	(3,773)
Tax (expense) or benefit	<u>908</u>	<u>334</u>
	<u>(9,363)</u>	<u>(3,439)</u>
Total unrealized gains (losses) on securities available for sale, net of tax	<u>16,462</u>	<u>(16,612)</u>
COMPREHENSIVE INCOME	<u><u>\$ 316,749</u></u>	<u><u>\$ 357,788</u></u>

See accompanying notes to financial statements.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

STATEMENTS OF CHANGES IN MEMBERS' EQUITY

For the years ended October 31, 2016 and 2015

	Number of Shares *	Common Stock	Contributions in Aid of Construction	Additional Paid In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance - October 31, 2014, as Restated	2,414	\$ 241,400	\$ 1,688,022	\$ 814,495	\$ 7,039,387	\$ 12,492	\$ 9,795,796
Net income	-	-	-	-	374,400	-	374,400
Net unrealized losses arising during the year, net of tax	-	-	-	-	-	(16,612)	(16,612)
Contributions	4	-	12,125	-	-	-	12,125
Stock issued	24	2,400	-	292,800	-	-	295,200
Amortization	-	-	(81,916)	-	-	-	(81,916)
Balance - October 31, 2015	2,442	243,800	1,618,231	1,107,295	7,413,787	(4,120)	10,378,993
Net income	-	-	-	-	300,287	-	300,287
Net unrealized gains arising during the year, net of tax	-	-	-	-	-	16,462	16,462
Contributions	-	-	9,152	-	-	-	9,152
Stock issued	9	900	-	109,800	-	-	110,700
Amortization	-	-	(81,805)	-	-	-	(81,805)
Balance - October 31, 2016	2,451	\$ 244,700	\$ 1,545,578	\$ 1,217,095	\$ 7,714,074	\$ 12,342	\$ 10,733,789

\* During the years ended October 31, 2016 and 2015, respectively, 28 and 21 shares of Common Stock were retired and re-issued as Class A Common Stock.

See accompanying notes to financial statements.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

STATEMENTS OF CASH FLOWS

For the years ended October 31, 2016 and 2015

	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 300,287	\$ 374,400
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	265,389	259,684
Amortization of premiums/(discounts) on investments	6,374	6,459
(Increase) decrease in operating assets:		
Accounts receivable	(33,415)	20,470
Interest receivable	(4,795)	(4,034)
Other receivable	-	209,418
Inventory	(1,157)	3,342
Prepaid water	(207,900)	-
Deferred income taxes receivable	399	(399)
Increase (decrease) in operating liabilities:		
Accounts payable	(59,071)	5,550
Income taxes payable	38,763	33
Deferred income taxes payable	492	(1,211)
Compensated absences	(8,710)	8,704
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>296,656</u>	<u>882,416</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(235,377)	(301,226)
Principal proceeds from installment sale of land	531,673	74,170
Proceeds from sale or maturity of investments	207,679	176,606
Purchases of investments	(728,195)	(844,555)
NET CASH USED BY INVESTING ACTIVITIES	<u>(224,220)</u>	<u>(895,005)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Principal payments on note payable	(58,627)	(31,194)
Issuance of stock	110,700	295,200
NET CASH PROVIDED BY FINANCING ACTIVITIES	<u>52,073</u>	<u>264,006</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	124,509	251,417
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>1,029,896</u>	<u>778,479</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 1,154,405</u>	<u>\$ 1,029,896</u>
SUPPLEMENTAL DISCLOSURES:		
Noncash investing and financing activities:		
Capital expenditure funded by capital lease borrowings	\$ 121,860	\$ -
Contributions in aid of construction	\$ 9,152	\$ 12,125
Cash paid for interest	\$ 439	\$ 1,245
Cash paid for income taxes	\$ 13,102	\$ 9,957

See accompanying notes to financial statements.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

NOTES TO FINANCIAL STATEMENTS

October 31, 2016 and 2015

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

A. Method of Accounting:

The financial statements are presented using the accrual basis of accounting. Revenues are recognized when they are earned and expenses are recognized when the related goods or services are delivered. Contributions in aid of construction are recorded when received.

B. Cash and Cash Equivalents:

For purposes of the statements of cash flows, cash and cash equivalents have been defined as cash and other highly liquid investments purchased with an original maturity of 90 days or less. Cash and cash equivalents consist of demand deposits in the amount of \$1,154,405 and \$1,029,896 at October 31, 2016 and 2015, respectively.

C. Investments:

Valencia Heights Water Company (the Company) considers all federally insured certificates of deposit with original maturities of more than three months as investments. The Company expects to hold the certificates of deposit to maturity, and therefore, they are reported at cost.

Marketable securities held by the Company are classified as available-for-sale securities. Available-for-sale securities are recorded at fair value in investments on the statements of financial position, with the change in fair value during the period excluded from earnings and recorded net of tax as a component of other comprehensive income.

The Company's investment in the common stock of the Covina Irrigating Company, in which the Company holds less than a 20 percent interest, is recorded at cost (See Note 4).

D. Fair Value:

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. The fair value is based on the assumptions used by market participants when pricing the asset or liability, which include observable and unobservable inputs. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability based on market data obtained from independent sources. Unobservable inputs reflect a Company's own assumptions about the assumptions market participants would use in pricing the asset or liability. There is a three-tiered fair value hierarchy that maximizes the use of observable inputs and prioritizes financial assets and liabilities measured with such inputs (See Note 12).

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

NOTES TO FINANCIAL STATEMENTS  
(CONTINUED)

October 31, 2016 and 2015

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. Accounts Receivable:

The Company assesses the need for an allowance for doubtful accounts based upon historical losses and a review of past due accounts at year-end. The Company considers accounts receivable to be fully collectible. Accordingly, no allowance for doubtful accounts has been recorded.

F. Inventory:

Inventory consists primarily of parts and materials used for construction and repair. Inventory is recorded at cost on the first-in, first-out method.

G. Property, Plant and Equipment:

Property, plant and equipment of \$5,000 or more, with an expected useful life of more than one year, are recorded at cost and currently depreciated over estimated lives ranging from 3 to 40 years using the straight-line method.

Contributed property, plant and equipment are recorded at the cost of property constructed and are currently amortized over estimated lives ranging from 20 to 40 years using the straight-line method. Amortization is recorded as a reduction of contributions in aid of construction in members' equity.

H. Contributions in Aid of Construction:

Contributions in aid of construction represent the unamortized balance of property, plant and equipment contributed to the Company by property owners or developers desiring services that require capital expenditures or capacity commitments.

I. Income Tax Status:

The Company is exempt from federal income taxes under Internal Revenue Code Section 501(c)(12). However, for California income tax purposes, the Company is taxed only for nonbusiness related income.

The Company's Forms 990, Return of Organization Exempt from Income Tax, for the years ended October 31, 2013, 2014 and 2015 are open to review by the Internal Revenue Service. The Company's Forms 100, California Corporation Franchise or Income Tax Return, for the years ended October 31, 2012 through 2015 are open to review by the California Franchise Tax Board.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

NOTES TO FINANCIAL STATEMENTS  
(CONTINUED)

October 31, 2016 and 2015

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

J. Concentrations of Credit Risk:

The Company maintains its cash deposit accounts at several financial institutions. At October 31, 2016 and 2015, accounts at each institution are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. At October 31, 2016, the Company's cash deposits exceeded the limits covered by the FDIC by \$134,422. At October 31, 2015, the Company's cash deposits did not exceed the limits covered by the FDIC.

The Company also maintains investments with a brokerage firm that are covered by the Securities Investor Protection Corporation (SIPC). The Company's accounts are insured by SIPC up to \$500,000 at October 31, 2016, and up to \$1,000,000 at October 31, 2015.

K. Estimates:

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

2. ORGANIZATION AND NATURE OF SERVICES:

The Company was incorporated in the State of California on November 8, 1912. The Company is a privately held mutual water company formed to furnish water services for the benefit and use of its members.



VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

NOTES TO FINANCIAL STATEMENTS  
(CONTINUED)

October 31, 2016 and 2015

3. PROPERTY, PLANT AND EQUIPMENT:

Changes in property, plant and equipment for the year ended October 31, 2016 were as follows:

	Balances at November 1, 2015	Additions	Deletions	Balances at October 31, 2016
Property, plant and equipment, not being depreciated/amortized:				
Land and land rights	\$ 171,150	\$ -	\$ -	\$ 171,150
Construction in progress	<u>106,514</u>	<u>434,874</u>	<u>(295,934)</u>	<u>245,454</u>
Total capital assets, not being depreciated/amortized	<u>277,664</u>	<u>434,874</u>	<u>(295,934)</u>	<u>416,604</u>
Property, plant and equipment, being depreciated/amortized:				
Office equipment and maps	86,315	-	(600)	85,715
Machinery, treatment and pumping equipment	1,115,212	31,251	-	1,146,463
Building and structures	250,789	-	-	250,789
Vehicles, tools and equipment	193,910	146,170	-	340,080
Storage tanks and reservoirs	1,113,284	41,475	-	1,154,759
Transmission and distribution	5,954,491	9,154	-	5,963,645
Wells	1,128,947	-	-	1,128,947
SCADA computer equipment	<u>161,800</u>	<u>-</u>	<u>-</u>	<u>161,800</u>
Total property, plant and equipment being depreciated/amortized	10,004,748	228,050	(600)	10,232,198
Less accumulated depreciation/amortization	<u>(5,014,119)</u>	<u>(347,194)</u>	<u>-</u>	<u>(5,361,313)</u>
Total property, plant and equipment being depreciated/amortized, net	<u>4,990,629</u>	<u>(119,144)</u>	<u>(600)</u>	<u>4,870,885</u>
Property, plant and equipment, net	<u>\$ 5,268,293</u>	<u>\$ 315,730</u>	<u>\$ (296,534)</u>	<u>\$ 5,287,489</u>

Depreciation and amortization expense for the year ended October 31, 2016 was \$347,194. Depreciation expense of \$265,389 was recorded as an operating expense and amortization expense of \$81,805 was recorded as a reduction of contributions in aid of construction in members' equity.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

NOTES TO FINANCIAL STATEMENTS  
(CONTINUED)

October 31, 2016 and 2015

3. PROPERTY, PLANT AND EQUIPMENT (CONTINUED):

Changes in property, plant and equipment for the year ended October 31, 2015 were as follows:

	Balances at <u>November 1, 2014</u>	<u>Additions</u>	<u>Deletions</u>	Balances at <u>October 31, 2015</u>
Property, plant and equipment, not being depreciated/amortized:				
Land and land rights	\$ 171,150	\$ -	\$ -	\$ 171,150
Construction in progress	<u>493,533</u>	<u>232,787</u>	<u>(619,806)</u>	<u>106,514</u>
Total capital assets, not being depreciated/amortized	<u>664,683</u>	<u>232,787</u>	<u>(619,806)</u>	<u>277,664</u>
Property, plant and equipment, being depreciated/amortized:				
Office equipment and maps	81,015	5,300	-	86,315
Machinery, treatment and pumping equipment	936,671	178,541	-	1,115,212
Building and structures	250,789	-	-	250,789
Vehicles, tools and equipment	193,910	-	-	193,910
Storage tanks and reservoirs	1,061,584	51,700	-	1,113,284
Transmission and distribution	5,491,675	462,816	-	5,954,491
Wells	1,128,947	-	-	1,128,947
SCADA computer equipment	<u>161,800</u>	<u>-</u>	<u>-</u>	<u>161,800</u>
Total property, plant and equipment being depreciated/amortized	9,306,391	698,357	-	10,004,748
Less accumulated depreciation/amortization	<u>(4,672,519)</u>	<u>(341,600)</u>	<u>-</u>	<u>(5,014,119)</u>
Total property, plant and equipment being depreciated/amortized, net	<u>4,633,872</u>	<u>356,757</u>	<u>-</u>	<u>4,990,629</u>
Property, plant and equipment, net	<u>\$ 5,298,555</u>	<u>\$ 589,544</u>	<u>\$ (619,806)</u>	<u>\$ 5,268,293</u>

Depreciation and amortization expense for the year ended October 31, 2015 was \$341,600. Depreciation expense of \$259,684 was recorded as an operating expense and amortization expense of \$81,916 was recorded as a reduction of contributions in aid of construction in members' equity.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

NOTES TO FINANCIAL STATEMENTS  
(CONTINUED)

October 31, 2016 and 2015

4. INVESTMENT IN COVINA IRRIGATING COMPANY:

The Company owns 453.25 shares of capital stock of Covina Irrigating Company (CIC) as of October 31, 2016 and 2015. At October 31, 2015, each share entitled the owner to delivery of approximately 0.75 acre-feet of water. At October 31, 2016, each share entitled the owner to delivery of approximately 1.00 acre-feet of water. This investment is recorded at cost since the Company owns less than 20% of the capital stock and does not have the ability to exercise significant influence over CIC's operating and financial policies.

5. WATER RIGHTS:

The Company owns 1,061 adjudicated water rights as of October 31, 2016 and 2015. Each water right entitles the owner to delivery of approximately one acre-foot of water each year. Adjudicated rights have been subjected to comprehensive litigation in the courts, are typically quantified and are actively managed for optimization and sustainability of the resource. Water rights are carried on the books at cost.

In order to stabilize the cost of water, the Company has also leased water rights from some of the stockholders of Covina Irrigating Company. These water rights ensure a source of water to supplement the Company's ground water supply and enhance water quality as part of the Company's water supply permit. Leased water rights contracts for the periods July 1, 2015 through June 30, 2016 and July 1, 2014 through June 30, 2015 totaled \$79,459 and \$107,175, respectively. Most payments are made on a quarterly basis. Payments on these leases during 2016 totaled \$59,504 and are included in operating expenses in the accompanying statements of operations. As of October 31, 2016, the Company did not renew these leases.

6. PREPAID WATER:

The Company makes purchases of cyclic storage water to offset the increasing cost of replacement water which is currently at \$621 per acre-foot. As of October 31, 2016, 1,186 acre-feet of this water is reflected as prepaid water of \$423,793 in long-term assets for future years, as no amount is projected to be used in 2017. As of October 31, 2015, 836 acre-feet of this water is reflected as prepaid water of \$215,893 in long-term assets for future years.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

NOTES TO FINANCIAL STATEMENTS  
(CONTINUED)

October 31, 2016 and 2015

7. NOTE RECEIVABLE:

Pursuant to a purchase, exchange and sale agreement signed in March of 2001, the Company received a \$1,215,000 promissory note from the City of West Covina for the sale of Maverick Field to the City. The sale was consummated when escrow closed in June 2003. The note bears interest at a rate that is adjustable every three years to the then current, two-year, treasury bill rate plus 0.5%. The rate for the three years ended October 31, 2013 had been 0.873%. Effective November 1, 2013, the rate has been adjusted to 0.809%. It is secured by a deed of trust on the land. Principal and interest are receivable monthly over a twenty-year period. The monthly amount had been \$6,109. Effective November 1, 2013, the new monthly amount is \$6,090. During 2016, payment was collected in full. The balance of the note receivable as of October 31, 2015 was \$531,673.

8. NOTES PAYABLE:

On January 5, 1999, the Company entered into a sublease agreement with Walnut Valley Water District. The principal balance at October 31, 2015 was \$55,011. Principal and interest payments of \$16,219 have been due semiannually, on February 1 and August 1, maturing in 2018. Originally, interest had been paid at a rate of 4.47% per year. In April 2012, the terms of the note were revised and the interest rate was changed to a variable interest rate based on 0.50% above a simple average of the "average purchase yield to maturity", as determined by Walnut Valley Water District for each semiannual period. During the years ended October 31, 2016 and 2015, the average interest rate incurred by the Walnut Valley Water District was 1.69%. On January 20, 2016, the Board of Directors approved the final note payment. As of October 31, 2016, the note was paid in full.

On September 15, 2016, the Company entered into an equipment finance agreement with a bank. The original amount of the note is for \$64,974. The note is collateralized by specific equipment. The note calls for monthly principal and interest payments of \$1,935, bears an effective interest rate of 4.85%, and matures in August 2019. The outstanding balance at October 31, 2016 totaled \$61,359.

During October 2016, the Company financed the purchase of a vehicle with a separate lender. The original amount of the note is \$56,886. The promissory note is collateralized by specific equipment. The note bears interest at 1.13%, calls for monthly principal and interest payments of \$1,608, and matures in November 2019. The outstanding balance at October 31, 2016 totaled \$56,886.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

NOTES TO FINANCIAL STATEMENTS  
(CONTINUED)

October 31, 2016 and 2015

8. NOTES PAYABLE (CONTINUED):

Minimum future principal payments under the notes payable are as follows for the years ending October 31:

2017	\$ 37,881
2018	40,672
2019	<u>39,692</u>
Total	<u>\$ 118,245</u>

9. COMMON STOCK:

The Company has two classifications for its common stock. Class A common stock refers to shares of stock, issued after January 1, 1991, that are appurtenant to a parcel of land. One share of Class A common stock is issued to each parcel of land less than 28,500 square feet. A maximum of two shares is issued to each owner of land exceeding 28,500 square feet. Regular common stock is non appurtenant to land ownership and was issued prior to 1991.

Shares are issued to property owners upon purchase of land within the Company's jurisdiction. Shares are canceled if forfeited through foreclosure of the property or prolonged failure to pay for water services provided.

10. RETIREMENT PLANS:

The Company sponsors a defined contribution 401(k) pension plan for the benefit of its employees. Pre-tax employee and employer contributions are held in trust and invested by a third-party trustee, and therefore, are not reported in the accompanying financial statements. Company contributions to the Plan for the years ended October 31, 2016 and 2015 were \$30,043 and \$28,070, respectively.

The Company also sponsors a Section 457 deferred compensation plan (the 457 Plan). Company contributions to the 457 Plan were suspended effective July 1, 2010. At October 31, 2016 and 2015, the vested deferred compensation plan assets totaled \$110,797 and \$98,768, respectively. These amounts were reported both as an asset and liability in the accompanying financial statements, as the Company administers the 457 Plan.

11. COMPENSATED ABSENCES:

Employees of the Company are entitled to paid vacation and personal leave. Amounts accruable are dependent on length of service and current pay rate. At October 31, 2016 and 2015, the Company's accumulated compensated absence liability totaled \$45,238 and \$53,948, respectively.

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

NOTES TO FINANCIAL STATEMENTS  
(CONTINUED)

October 31, 2016 and 2015

12. FAIR VALUE MEASUREMENTS:

At October 31, 2016, the Company's investments are reported at fair value in the accompanying balance sheets as follows:

	Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Investments:			
Corporate bonds	\$ 1,032,835	\$ 1,032,835	\$ -
Municipal bonds	411,940	411,941	-
Mutual funds	<u>774,107</u>	<u>774,107</u>	-
	2,218,883	2,218,883	-
Deferred compensation plan assets:			
Mutual funds	<u>110,797</u>	<u>110,797</u>	-
	<u>\$ 2,329,680</u>	<u>\$ 2,329,680</u>	<u>\$ -</u>

At October 31, 2015, the Company's investments are reported at fair value in the accompanying balance sheet as follows:

	Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Investments:			
Corporate bonds	\$ 737,479	\$ 737,479	\$ -
Municipal bonds	304,924	304,924	-
Mutual funds	<u>645,876</u>	<u>645,876</u>	-
	1,688,279	1,688,279	-
Deferred compensation plan assets:			
Mutual funds	<u>98,768</u>	<u>98,768</u>	-
	<u>\$ 1,787,047</u>	<u>\$ 1,787,047</u>	<u>\$ -</u>

VALENCIA HEIGHTS WATER COMPANY  
(A California Mutual Water Company)

NOTES TO FINANCIAL STATEMENTS  
(CONTINUED)

October 31, 2016 and 2015

12. FAIR VALUE MEASUREMENTS (CONTINUED):

Accounting standards establish a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. This hierarchy consists of three broad levels: Level 1 inputs consist of unadjusted quoted prices in active markets for identical assets and have the highest priority, Level 2 inputs consist of observable inputs other than quoted prices for identical assets, and Level 3 inputs have the lowest priority. The Company uses appropriate valuation techniques based on the available inputs to measure the fair value of its investments. When available, the Company measures fair value using Level 1 inputs because they generally provide the most reliable evidence of fair value. Level 3 inputs were only used when Level 1 or Level 2 inputs were not available. The three levels are defined as follows:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.

Level 3: Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

The preceding methods described may produce a fair value calculation that may not be indicative of the net realizable value or reflective of future fair values. Furthermore, although management believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at that reporting date.

13. RELATED PARTY TRANSACTIONS:

During the years ended October 31, 2016 and 2015, a company owned by a member of the Board of Directors, brokered an insurance policy for the Company. Premiums paid to the insurance company for the years ended October 31, 2016 and 2015 totaled \$30,902 and \$33,908, respectively. During the years ended October 31, 2016 and 2015, total compensation for the Board Member's services rendered for the year totaled \$4,723 and \$4,239, respectively.

14. COMMITMENTS:

During 2015, the Company had entered into various agreements for professional services, at total costs approximating \$147,000. At October 31, 2015, the remaining commitment related to these contracts totaled \$115,800. As of October 31, 2016, the services were complete and the commitment was paid in full.

VALENCIA HEIGHTS WATER COMPANY  
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NOTES TO FINANCIAL STATEMENTS  
(CONTINUED)

October 31, 2016 and 2015

15. LOAN MANAGEMENT ACCOUNT:

At October 31, 2015, the Company had available an uncommitted revolving loan management account with a bank, providing for maximum borrowings of up to \$850,000. The account was payable on demand, and variable rate advances bear interest at LIBOR plus a spread as determined by the bank upon draw, and was collateralized by the investments with the bank. The loan management account also provides available letters of credit of up to \$200,000 each. At October 31, 2015, there was no balance due on the line of credit, nor have any letters of credit been issued. As of October 31, 2016, the revolving loan management account was terminated. Subsequent to October 31, 2016, the Company obtained a new line of credit with a different bank, which is secured by the Company's investments held in an account with that bank.

16. SUBSEQUENT EVENTS:

The Company has evaluated subsequent events through January 6, 2017, the date on which the financial statements were available to be issued.



## **\*\* IMPORTANT INFORMATION \*\***

### **CHLORAMINES:**

From time to time, Valencia Heights Water Company's (VHWC) water may contain chloramines for disinfection. Chloramines are a combination of chlorine and ammonia. This is due to disinfection by-product regulations, and in the water supplied by Covina Irrigating Company (CIC) and Metropolitan Water District (MET). While chloramines serve the same purpose as chlorine, the chloraminated water must be treated prior to and for the use with the following:

- **Dialysis Equipment, and**
- **Exotic Fish Tanks & Ponds**

**IF THIS APPLIES TO YOU: PLEASE CONTACT THE APPROPRIATE PROFESSIONAL AND VHWC TO ADDRESS THE ISSUE.**

#### **Valencia Heights Water Company**

3009 East Virginia Avenue  
West Covina, CA 91791-2252

**Phone:** (626) 332-8935 or (626) 332-3577

**Fax:** (626) 332-9441

**Website:** [vhwc.org](http://vhwc.org)

**Email:** [info@vhwc.org](mailto:info@vhwc.org)

#### **Office Hours:**

**Monday – Thursday:** 8 a.m. to 6 p.m.

**Fridays:** **CLOSED**

### **AUTOMATIC/RECURRING PAYMENTS**

The Automatic/Recurring Payment Application can be accessed through the [vhwc.org](http://vhwc.org) website, and also at 3009 E. Virginia Avenue, West Covina. Submit the signed and dated application, along with a voided check, to our office, and your monthly water bill payment amount will automatically deduct from your checking account. No need to worry about late or shut off fees. It's a great payment offer, so please take advantage of this time-saving approach to paying your water bill.

For our customers who currently pay their water bills through their bank's "Bill Pay" service, please consider changing to the Automatic/Recurring Payment service with VHWC. The change would save the Company time and money in processing bill pay checks. **We would greatly appreciate it if you would change to VHWC'S Auto Pay Service.**

### **BILLING & PAYMENTS:**

- Water bills are mailed near or on the fifth (5th) of every month in envelopes with a return envelope enclosed.
- **Water bill payments are due on the 25th of every month.**
- Please remember to include your remittance stub with your payment.
- Past Due Notices are mailed, in envelopes, on the next business day after the 25th of every month.
- We accept Cashier and Personal Checks, Money Orders, and Cash. For your convenience, payments can be left at our office during regular business hours, or you can use the front door mail-slot to drop payments after-hours and holidays.
- We offer Automatic/Recurring Payments (applications are available online @ [vhwc.org](http://vhwc.org) and in the office); **Credit Card Payments are available only through our website: [vhwc.org](http://vhwc.org)**
- **If you are unable to make your payment by the 25th, and to prevent a \$30 late fee, please call the office before the 25th to set-up a payment arrangement. With just a phone call, you can prevent a \$30 late fee.**

**VALENCIA HEIGHTS WATER COMPANY**  
3009 East Virginia Avenue  
West Covina, CA 91791-2252

PRESORTED  
FIRST-CLASS MAIL  
U.S. POSTAGE  
PAID  
Covina, California  
Permit No. 8PS



**Proxy Card Enclosed**  
**Return Card by February 16, 2017**