



## **PIMA COUNTY, ARIZONA**

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# *Pima County Department of Wastewater Management*

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**For the Fiscal Year Ended  
June 30, 2005**

Pima County  
Department of Wastewater Management  
Report on Audit of Financial Statements  
Year Ended June 30, 2005

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## INDEPENDENT AUDITORS' REPORT

The Board of Supervisors  
of Pima County, Arizona

We have audited the accompanying financial statements of the Pima County Department of Wastewater Management, as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the management of Pima County Department of Wastewater Management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements of the Pima County Department of Wastewater Management are intended to present the financial position, and the changes in financial position and cash flows of only that portion of the business-type activities and major funds of Pima County, Arizona that is attributable to the Pima County Department of Wastewater Management. They do not purport to, and do not, present fairly the financial position of Pima County, Arizona, as of June 30, 2005, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Pima County Department of Wastewater Management, as of June 30, 2005, and the respective changes in its financial position and its cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the financial statements of the Pima County Department of Wastewater Management. The accompanying financial information listed as Supplementary Schedules in the table of contents is presented for purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

  
HEINFELD, MEECH & CO., P.C.  
Certified Public Accountants

September 20, 2005

Pima County  
 Department of Wastewater Management  
 Statement of Net Assets - Enterprise Fund  
 June 30, 2005

Assets

Current assets:

Cash and cash equivalents	\$ 30,790,923
Interest receivable	86,963
Accounts receivable, net	8,077,010
Due from other Pima County funds	58,776
Due from other governments	530,158
Inventory of materials and supplies	2,814,893
Prepaid expenses	26,243
Total current assets	42,384,966

Noncurrent assets:

Restricted assets:

Cash and cash equivalents:

Restricted for construction	2,629,898
Restricted for debt service	1,305,703
Restricted for operation and maintenance	3,511,265
Held in escrow as construction contract retentions	844,424

Interest receivable	45
Total restricted assets	8,291,335

Capital assets, net of accumulated depreciation where applicable:

Land and other improvements	12,397,849
Solid waste transfer stations, net	1,495,551
Conveyance systems, net	322,144,855
Treatment facilities, net	181,106,962
Equipment, net	6,864,910
Construction in progress	63,324,807
Total capital assets, net	587,334,934

Deferred financing costs	847,787
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Total noncurrent assets	596,474,056
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Total assets	\$ 638,859,022
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(Continued)

See accompanying notes to financial statements

Pima County  
 Department of Wastewater Management  
 Statement of Net Assets - Enterprise Fund  
 June 30, 2005  
 (Continued)

Liabilities

Current liabilities:

Accounts payable	\$ 4,157,326
Accrued payroll and employee benefits	3,724,926
Due to other Pima County funds	107,589
Due to other governments	12,648
Interest payable	1,518,722
Current portion of sewer revenue bonds payable	4,550,000
Current portion of wastewater loans payable	4,950,734
Deferred revenue	3,796,457
Total current liabilities	<u>22,818,402</u>

Noncurrent liabilities:

Construction contract retentions payable	4,851,976
Landfill closure and postclosure care costs payable	15,635,842
Sewer revenue bonds payable, less current portion	55,525,000
Wastewater loans payable, less current portion	79,281,579
Deferred interest expense and bond discount	(4,520,723)
Total noncurrent liabilities	<u>150,773,674</u>

Total liabilities	<u>173,592,076</u>
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Net Assets

Invested in capital assets, net of related debt	448,396,131
Restricted for:	
Debt service	467,956
Capital projects	45
Wastewater management	3,511,265
Unrestricted	<u>12,891,549</u>
Total net assets	<u>\$ 465,266,946</u>

See accompanying notes to financial statements

Pima County  
 Department of Wastewater Management  
 Statement of Revenues, Expenses, and  
 Changes in Fund Net Assets - Enterprise Fund  
 Year Ended June 30, 2005

Operating revenues:	
Sewer utility service	\$ 50,393,306
Solid waste fees	4,670,430
Engineering review and inspection fees	70,754
Permits and fines	101,160
Other income	<u>1,878,176</u>
Total operating revenues	<u>57,113,826</u>
Operating expenses:	
Employee compensation	26,921,317
Operating supplies	4,713,748
Utilities	3,817,640
Sludge and refuse disposal	2,456,122
Repairs and maintenance	3,602,682
General and administrative	7,385,059
Consultants and professional services	3,539,422
Depreciation	<u>18,108,096</u>
Total operating expenses	<u>70,544,086</u>
Operating loss	<u>(13,430,260)</u>
Nonoperating revenues (expenses):	
Intergovernmental revenue	635,019
Interest income	576,148
Sewer connection revenue	36,906,421
State-shared tax revenue	1,162,869
Loss on disposal of equipment	(564,641)
Interest expense	(4,212,690)
Amortization of deferred charges	<u>(97,087)</u>
Total nonoperating revenues (expenses)	<u>34,406,039</u>
Income before capital contributions and transfers	20,975,779
Capital contributions	20,722,136
Transfers out	(52,742)
Increase in net assets	41,645,173
Net assets—July 1, 2004 (as restated)	<u>423,621,773</u>
Net assets—June 30, 2005	<u><u>\$ 465,266,946</u></u>

See accompanying notes to financial statements

Pima County  
Department of Wastewater Management  
Statement of Cash Flows - Enterprise Fund  
Year Ended June 30, 2005

Cash flows from operating activities:	
Receipts from customers	\$ 53,577,988
Miscellaneous receipts	1,492,385
Payments to suppliers for goods and services	(15,961,262)
Payments to other Pima County Funds for goods and services	(9,120,689)
Payments to employees	<u>(26,594,797)</u>
Net cash provided by operating activities	<u>3,393,625</u>
Cash flows from noncapital financing activities:	
Intergovernmental receipts	635,019
State-shared tax receipts	1,162,869
Repayment of interfund borrowings	16,304
Cash transfers to other Pima County Funds	<u>(52,742)</u>
Net cash provided by noncapital financing activities	<u>1,761,450</u>
Cash flows from capital and related financing activities:	
Sewer connection receipts from customers	35,688,645
Federal contract receipts	188,409
Purchase and construction of capital assets	(10,873,269)
Principal payments on revenue bonds and loans	(4,705,000)
Interest payments on revenue bonds and loans	<u>(2,276,249)</u>
Net cash provided by capital and related financing activities	<u>18,022,536</u>
Cash flows from investing activities:	
Interest received on investments	<u>501,469</u>
Net cash provided by investing activities	<u>501,469</u>
Net increase in cash and cash equivalents	23,679,080
Cash and cash equivalents, July 1, 2004	<u>15,403,133</u>
Cash and cash equivalents, June 30, 2005	<u>\$ 39,082,213</u>

(Continued)

See accompanying notes to financial statements

Pima County  
 Department of Wastewater Management  
 Statement of Cash Flows - Enterprise Fund  
 Year Ended June 30, 2005  
 (Continued)

Reconciliation of operating loss to net cash provided by operating activities:

Operating loss	\$(13,430,260)
Adjustments to reconcile operating loss to net cash provided by operating activities:	
Depreciation	18,108,096
Landfill closure and postclosure care costs	(385,791)
Changes in assets and liabilities:	
Decrease (increase) in assets:	
Accounts receivable	(1,566,034)
Due from other governments	(91,628)
Inventory of materials and supplies	(118,435)
Prepaid expenses	65,376
Increase (decrease) in liabilities:	
Accounts payable	485,387
Due to other governments	12,648
Accrued payroll and employee benefits	326,520
Due to other Pima County funds	(12,254)
Net cash provided by operating activities	\$ 3,393,625

Noncash investing, capital, and noncapital financing activities:

During the year ended June 30, 2005, developers conveyed capital assets with an estimated fair value of \$21,820,307 to the Department. This transaction was recorded as a capital contribution.

During the year ended June 30, 2005, the Pima County Board of Supervisors approved Connection Fee Flow-Through Sewer Credit Agreements totaling \$1,098,171. This transaction was recorded as an increase to deferred revenue and a decrease in capital contributions.

During the year ended June 30, 2005, the Department retired assets with a net book value of \$564,641.

During the year ended June 30, 2005, the Department adjusted the Corrective Action Costs decreasing the landfill liability and increasing miscellaneous revenue by \$385,791.

During the year ended June 30, 2005, the Department transferred \$196,786 of fully-depreciated capital assets to Pima County.

See accompanying notes to financial statements

Pima County  
Department of Wastewater Management  
Notes to Financial Statements  
June 30, 2005

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

The accounting policies of the Department of Wastewater Management conform to generally accepted accounting principles applicable to governmental units adopted by the Governmental Accounting Standards Board (GASB).

A summary of the Department's more significant accounting policies follows.

**A. Reporting Entity**

The Department is accounted for as an enterprise fund of Pima County, Arizona, and is responsible for managing and operating all liquid and solid waste programs in Pima County. The Department's management is directed by an administrator appointed by the Pima County Board of Supervisors. However, ultimate financial accountability for the Department remains with Pima County.

**B. Fund Accounting**

The Department's accounts are maintained in accordance with the principles of fund accounting to ensure that limitations and restrictions on the Department's available resources are observed. The principles of fund accounting require that resources be classified for accounting and reporting purposes into funds in accordance with the activities or objectives specified for those resources. A fund is considered a separate accounting entity, and its operations are accounted for in a separate set of self-balancing accounts that comprise its assets, liabilities, net assets, revenues, and expenses.

The Department's financial transactions are recorded and reported as an enterprise fund because its operations are financed and operated in a manner similar to private business enterprises, in which the intent of the Board of Supervisors is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

**C. Basis of Accounting**

Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied, and determines when revenues and expenses are recognized in the accounts and reported in the financial statements. The Department's financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. Revenues are recognized when earned, and expenses are recognized at the time liabilities are incurred, regardless of when the related cash flows take place. When both restricted and unrestricted net assets are available to finance departmental expenses, restricted resources are used before unrestricted resources. Interfund transactions that would be treated as revenues or

Pima County  
Department of Wastewater Management  
Notes to Financial Statements  
June 30, 2005

expenses if they involved parties external to Pima County are recorded in the appropriate revenue or expense accounts. Intrafund transactions within the Department are eliminated for the consolidated financial statement presentation.

The Department follows those Financial Accounting Standards Board Statements and Interpretations issued on or before November 30, 1989; Accounting Principles Board Opinions; and Accounting Research bulletins, unless those pronouncements conflict with GASB pronouncements. The Department has chosen the option not to follow FASB Statements and Interpretations issued after November 30, 1989.

#### **D. Basis of Presentation**

The financial statements include a statement of net assets; a statement of revenues, expenses, and changes in fund net assets; and a statement of cash flows.

A statement of net assets provides information about the assets, liabilities, and net assets of the Department at the end of the year. Assets and liabilities are classified as either current or noncurrent. Net assets are classified according to external restrictions or availability of assets to satisfy the Department's obligations. Invested in capital assets net of related debt represents the value of capital assets, net of accumulated depreciation, less any outstanding debt incurred to acquire or construct the assets. Restricted net assets represent grants, contracts, and other resources that have been externally restricted for specific purposes. Unrestricted net assets include all other net assets, including those that have been designated by management to be used for other than general operating purposes.

A statement of revenues, expenses, and changes in fund net assets provides information about the Department's financial activities during the year. Revenues and expenses are classified as either operating or nonoperating, and all changes in net assets are reported, including capital contributions and transfers. Operating revenues and expenses generally result from providing waste services. Accordingly, operating revenues, such as sewer utility service and solid waste fees, result from transactions associated with the Department's principal activities. Other revenues, such as sewer connection revenues and interest income, are not generated from operations and are considered to be nonoperating revenues. Operating expenses include the costs of providing sewer services, administrative expenses, and depreciation on capital assets. Other expenses, such as interest expense on debt, are considered to be nonoperating expenses.

A statement of cash flows provides information about the Department's sources and uses of cash and cash equivalents during the year. Increases and decreases in cash and cash equivalents are classified as either, operating, noncapital financing, capital financing, or investing.

Pima County  
Department of Wastewater Management  
Notes to Financial Statements  
June 30, 2005

**E. Cash and Cash Equivalents**

For purposes of the statement of cash flows, cash and cash equivalents consist of cash on hand, cash and investments held by the Pima County Treasurer, investments with the State Treasurer, and deposits held in escrow accounts from both restricted and unrestricted sources. Unrestricted cash and cash equivalents consist of cash on hand, cash and investments held by the Pima County Treasurer in an investment pool, and investments with the State Treasurer. Restricted cash and cash equivalents consist of cash and investments held by the Pima County Treasurer in an investment pool, and deposits held in escrow accounts. All investments are stated at fair value.

**F. Deferred Charges**

Deferred charges (primarily bond and loan issuance costs) are being amortized over the life of the related debt using the straight-line method.

**G. Capital Assets**

Capital assets are reported at actual cost. Donated assets are reported at estimated fair value at the time received. The Department capitalizes all land and buildings regardless of cost and all other capital assets costing \$5,000 or more. Costs for internally constructed capital assets include material, direct labor, engineering, interest, and allocated portions of other indirect costs related to the construction projects. Depreciation of such assets is charged as an expense against operations. These assets are depreciated over their estimated useful lives using the straight-line method. The estimated useful lives are as follows:

Treatment facilities and equipment	4 to 50 years
Conveyance systems	50 years
Solid waste transfer stations	50 years

**H. Compensated Absences**

Compensated absences consist of annual leave and a calculated amount of sick leave earned by employees based on services already rendered. Employees may accumulate up to 240 hours of annual leave, but must forfeit any annual leave hours in excess of the maximum that are unused at the end of the payroll period in which the employee's anniversary date falls. Upon termination, all unused and unforfeited annual leave benefits are paid to employees. Accordingly, annual leave benefits are accrued as a liability in the financial statements.

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Department of Wastewater Management  
Notes to Financial Statements  
June 30, 2005

Generally, sick leave benefits provide for ordinary sick pay and are cumulative, but do not vest with employees and therefore, are not accrued in the financial statements, except for the actual amount used during the thirty day period subsequent to fiscal year end. However, for employees who retire with 20 years or more of continuous service or who have a combined total of age and years of service equal to 80 points, and who retire from service into the Arizona State Retirement System, sick leave benefits do vest and, therefore, are accrued.

### **I. Construction Contract Retentions**

The Department has numerous construction projects in process. The Department retains a percentage of each progress payment until the project's successful completion. In some instances, contract retentions are deposited in escrow accounts so contractors may earn interest during the construction period.

### **J. Deferred Interest Expense**

For advance refundings resulting in defeasance of debt, the difference between the reacquisition price and net carrying amount of the old debt is deferred and amortized as a component of interest expense over the life of the refunded debt or the refunding debt, whichever is shorter. This deferred amount is reported as a deduction from the new debt liability on the statement of net assets.

### **K. Revenues**

Sewer utility billings are based on the content and volume of wastewater discharged and a minimum service charge. Solid waste fees are based on landfill location, weight of disposed material, and material type.

Land developers contribute capital and aid in the construction of certain portions of the conveyance systems. Contributions are recorded as an increase in net assets at their estimated fair value. In those instances when a developer makes enhancements that exceed the requirements for the conveyance systems, the Department establishes reduced fees and credits that can be used to offset future fees charged to developers for each new connection to the conveyance systems. These credits are recorded as deferred sewer connection revenue and recognized as income when connection permits are issued.

Sewer connection fees are assessed to land developers based on the type and number of fixtures attached to the conveyance systems. Fees are established at a level to provide for the recovery of the Department's operating expenses that are not recovered by the sewer utility service fees. Accordingly, fees collected are classified as nonoperating revenues.

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 Department of Wastewater Management  
 Notes to Financial Statements  
 June 30, 2005

**Note 2 - Net Asset Beginning Balance Restated**

The beginning net asset balance was restated to correct misclassifications in reporting construction in progress in prior years.

Net assets, June 30, 2004, as previously reported	\$ 433,533,482
Correction of error	<u>(9,911,709)</u>
Net assets, July 1, 2004, as restated	<u>\$ 423,621,773</u>

**Note 3 - Cash and Cash Equivalents**

Cash and cash equivalents consisted of the following amounts:

Current assets:	
Cash on hand	\$ 3,900
Cash and investments held by the Pima County Treasurer	<u>30,787,023</u>
Total current cash and cash equivalents	<u>30,790,923</u>
Restricted assets:	
Cash and investments held by the Pima County Treasurer	7,446,866
Deposits held in escrow accounts	<u>844,424</u>
Total restricted cash and cash equivalents	<u>8,291,290</u>
Total cash and cash equivalents	<u>\$39,082,213</u>

The Department's cash and investments in the Pima County Treasurer's investment pool represent a portion of the County Treasurer's investment pool portfolio. There is no oversight provided for the County Treasurer's investment pool, and the pool's structure does not provide for shares. The Department's portion in the pool is not identified with specific investments and is not subject to custodial credit risk.

Of the deposits held in escrow accounts by financial institutions, \$100,000 was covered by federal depository insurance and \$744,424 was uninsured and uncollateralized at June 30, 2005.

**Credit Risk** – Credit risk is the risk that an issuer or counterparty to an investment will not fulfill its obligations. The Department does not have a formal investment policy with respect to credit risk. The Pima County Treasurer's investment pool is unrated.

**Interest Rate Risk** – Interest rate risk is the risk that changes in interest rates will adversely affect an investment's fair value. The Department does not have a formal investment policy with respect to interest rate risk. The Pima County Treasurer's investment pool had a weighted average maturity of 80 days at June 30, 2005.

Pima County  
Department of Wastewater Management  
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**Legal Provisions** – Arizona Revised Statutes authorize counties to invest public monies in the State Treasurer's investment pool: obligations issued or guaranteed by the United States or any of the senior debt of its agencies, sponsored agencies, corporations, sponsored corporations, or instrumentalities; specified state and local government bonds; interest earning investments such as savings accounts, certificates of deposit, and repurchase agreements in eligible depositories; and specified commercial paper, bonds, debentures, and notes issued by corporations organized and doing business in the United States. In addition, the County Treasurer may invest trust funds in fixed income securities of corporations doing business in the United States or District of Columbia.

Credit risk - Statutes have the following requirements for credit risk:

1. Commercial paper must be rated P1 by Moody's investors' service or A1 or better by Standard and Poor's rating service.
2. Corporate bonds, debentures, and notes must be rated A or better by Moody's investors' service or Standard and Poor's rating service.
3. Fixed income securities must carry one of the two highest ratings by Moody's investors' service and Standard and Poor's rating service. If only one of the above-mentioned services rates the security, it must carry the highest rating of that service.

Custodial credit risk - Statutes require collateral for demand deposits, certificates of deposit, and repurchase agreements at 101 percent of all deposits not covered by federal depository insurance.

Concentration of credit risk - Statutes do not include any requirements for concentration of credit risk.

Interest rate risk - Statutes require that public monies invested in securities and deposits have a maximum maturity of 5 years and that public operating fund monies invested in securities and deposits have a maximum maturity of 3 years. Investments in repurchase agreements must have a maximum maturity of 180 days.

Foreign currency risk - Statutes do not allow foreign investments.

Pima County  
 Department of Wastewater Management  
 Notes to Financial Statements  
 June 30, 2005

**Note 4 - Capital Asset Activity**

Capital asset activity for the year ended June 30, 2005, is presented in the following schedule:

	<u>Balance July 1, 2004 (as restated)</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance June 30, 2005</u>
Capital assets not being depreciated:				
Land and other improvements	\$ 12,396,649	\$ 1,200		\$ 12,397,849
Construction in progress	<u>142,508,935</u>	<u>7,668,286</u>	<u>\$86,852,414</u>	<u>63,324,807</u>
Total capital assets not being depreciated	<u>154,905,584</u>	<u>7,669,486</u>	<u>86,852,414</u>	<u>75,722,656</u>
Capital assets being depreciated:				
Transfer stations	2,168,380			2,168,380
Conveyance systems	423,337,256	51,817,472	6,587	475,148,141
Treatment facilities	222,839,363	56,914,979	1,699,876	278,054,466
Equipment	<u>18,721,413</u>	<u>596,979</u>	<u>908,469</u>	<u>18,409,923</u>
Total capital assets being depreciated	<u>667,066,412</u>	<u>109,329,430</u>	<u>2,614,932</u>	<u>773,780,910</u>
Less accumulated depreciation for:				
Transfer stations	625,890	46,939		672,829
Conveyance systems	143,719,835	9,285,645	2,195	153,003,285
Treatment facilities	90,558,245	7,539,215	1,149,956	96,947,504
Equipment	<u>11,206,855</u>	<u>1,236,297</u>	<u>898,138</u>	<u>11,545,014</u>
Total accumulated depreciation	<u>246,110,825</u>	<u>18,108,096</u>	<u>2,050,289</u>	<u>262,168,632</u>
Total capital assets being depreciated, net	<u>420,955,587</u>	<u>91,221,334</u>	<u>564,643</u>	<u>511,612,278</u>
Capital assets, net	<u>\$ 575,861,171</u>	<u>\$98,890,820</u>	<u>\$87,417,057</u>	<u>\$ 587,334,934</u>

Pima County  
Department of Wastewater Management  
Notes to Financial Statements  
June 30, 2005

**Note 5 - Long-Term Liabilities**

The following schedule details the Department's long-term liability and obligation activity for the year ended June 30, 2005:

	Balance <u>July 1, 2004</u>	<u>Increases</u>	<u>Decreases</u>	Balance <u>June 30, 2005</u>	Due Within <u>1 year</u>
Sewer revenue bonds	\$ 64,780,000		\$4,705,000	\$ 60,075,000	\$4,550,000
Less unamortized deferred amounts	<u>4,715,916</u>		<u>450,220</u>	<u>4,265,696</u>	<u>                    </u>
Total sewer revenue bonds payable	<u>60,064,084</u>			<u>55,809,304</u>	<u>4,550,000</u>
Wastewater loans payable	84,232,313			84,232,313	4,950,734
Less unamortized deferred amounts	<u>291,459</u>		<u>36,432</u>	<u>255,027</u>	<u>                    </u>
Total wastewater loans payable	<u>83,940,854</u>			<u>83,977,286</u>	<u>4,950,734</u>
Landfill closure and postclosure care costs	16,021,633		385,791	15,635,842	
Construction contract retentions payable	<u>5,782,697</u>	<u>286,277</u>	<u>1,216,998</u>	<u>4,851,976</u>	<u>                    </u>
Total long-term liabilities	<u>\$165,809,268</u>	<u>\$ 286,277</u>	<u>\$5,821,137</u>	<u>\$160,274,408</u>	<u>\$9,500,734</u>

**Sewer Revenue Bonds Payable**—The Department has issued several series of sewer revenue bonds (Series 1993, Series 1998, Refunding 2001, and Refunding 2004) to provide funds for the defeasance of prior sewer revenue bonds, the construction of a utility plant, and the construction of improvements to the sewer system. The bonds are callable at various prices depending on the date of call. Interest on the bonds is payable semiannually. Of the total amount originally authorized, \$5,894,000 from the May 20, 1997, bond election, and \$150,000,000 from the May 18, 2004, bond election remain unissued.

**Wastewater Loans Payable**—The Department has entered into four loan agreements with the Water Infrastructure Financing Authority of Arizona (1996, 1997, 2000, and 2004 loans payable) to provide funds for the defeasance of prior sewer revenue bonds and the construction and improvement of wastewater treatment facilities. Interest is payable semiannually and is calculated based on the principal amount of the loan outstanding.

At June 30, 2005, the Department has drawn down only \$17,452,651 of the \$18,015,000 authorized loan amount for the 2004 Water Infrastructure Financing Authority of Arizona loan. Payments of principal, which are subject to change, are based on the total amounts drawn.

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 Notes to Financial Statements  
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As of December 1, 2004, the Water Infrastructure Financing Authority of Arizona has been authorized to process loan payments via EFT debit. Since the debit payment this year was processed effective July 1, 2005, the principal loan amount outstanding at June 30, 2005 remained unchanged.

**Debt Covenants**—All revenue bonds were issued and the loan agreements were executed with a first lien on the first pledge of the Department's net revenues and have restrictive covenants, primarily related to minimum utility rates and limitations on future bond issues. The bond covenants also require the Department to either maintain a surety bond guaranteeing the payment of annual debt service or to maintain in the Bond Reserve Account monies equal to the average annual debt service payment. At June 30, 2005, the Department had a surety bond to meet the requirements of the debt covenants. The Department is also authorized to issue additional parity bonds if certain conditions are met, primarily that net revenues for the fiscal year immediately preceding issuance of the parity bonds exceed 120 percent of the maximum annual debt service requirements immediately after such issuance.

Bonds and loans outstanding at June 30, 2005, were as follows:

Description	Interest Rates	Maturity Dates	Outstanding Principal
Series 1998	4.0-5.5%	2006 - 15	19,660,000
Refunding 2001	4.0-5.4%	2006 - 15	16,070,000
Refunding 2004	2.25-5.5%	2006 - 15	<u>24,345,000</u>
Total sewer revenue bonds payable			<u>\$60,075,000</u>
1996 loan payable	3.19%	2005 - 12	10,615,745
1997 loan payable	2.95%	2005 - 11	4,221,855
2000 loan payable	2.20%	2005 - 16	51,942,062
2004 loan payable	1.81%	2005 - 24	<u>17,452,651</u>
Total wastewater loans payable			<u>\$84,232,313</u>

Revenue bond debt service and loan payment requirements to maturity, are as follows:

	<u>Revenue Bond Debt Service</u>		<u>Loan Payment Requirements</u>	
	Principal	Interest	Principal	Interest
Year ending June 30,				
2006	\$ 4,550,000	\$ 2,759,658	\$ 4,950,734	\$ 2,946,630
2007	5,570,000	2,573,045	5,502,957	2,754,834
2008	5,800,000	2,339,501	5,640,514	2,551,745
2009	6,025,000	2,098,076	5,871,286	2,343,340
2010	5,280,000	1,816,076	6,230,119	2,124,110
2011-2015	32,850,000	5,040,190	34,259,533	6,774,271
2016-2020			16,236,605	1,770,474
2021-2025			<u>5,540,565</u>	<u>434,405</u>
Total	<u>\$60,075,000</u>	<u>\$16,626,546</u>	<u>\$ 84,232,313</u>	<u>\$21,699,809</u>

Pima County  
Department of Wastewater Management  
Notes to Financial Statements  
June 30, 2005

**Landfill Closure and Postclosure Care Costs**—State and federal laws and regulations require the Department to place a final cover on its solid waste landfill sites when these sites stop accepting waste and to perform certain maintenance and monitoring functions at the sites for 30 years after closure. Although closure and postclosure care costs will not be paid until near or after the date that the landfill stops accepting waste, the Department reports a portion of these closure and postclosure care costs in each operating period even though actual payouts will not occur until the landfill is closed.

The amount recognized each year is based on landfill capacity used at the end of each fiscal year. The Sahuarita and Tangerine Landfill capacities were increased from 5,130,192 and 5,530,000 cubic yards at June 30, 2004 to 5,233,952 and 5,737,761 cubic yards at June 30, 2005, respectively. Concurrently, the estimated years of closure were adjusted to 2022 and 2008 from 2019 and 2006, respectively. The Ajo Landfill capacity was decreased from 1,150,620 cubic yards at June 30, 2004 to 1,147,620 cubic yards at June 30, 2005. During the fiscal year, the Ajo Landfill reached 100% capacity and was closed. Life extending facility development options are presently being considered for the Ajo Landfill, including vertical and/or horizontal expansion. The \$15,635,842 reported as landfill closure and postclosure care liability at June 30, 2005, represents the cumulative amount reported to date based on the use of 100, 41, and 89 percent of the estimated capacity of the Ajo, Sahuarita, and Tangerine landfills, respectively and the elimination of \$1,250,000 in prior year Corrective Action Costs. The Department will recognize the remaining estimated cost of closure and postclosure care of \$5,076,879 as the remaining estimated capacity of each landfill is filled. These amounts are based on what it would cost to perform all closure and postclosure care in fiscal year 2005. The Department expects to close the Sahuarita, and Tangerine, landfills in the years 2022 and 2008, respectively, and actual costs may be higher due to inflation, changes in technology, or changes in regulations.

According to state and federal laws and regulations, the County must comply with the local government financial test requirements that assure that the County can meet the costs of landfill closure, postclosure, and corrective action when needed. The County is in compliance with these requirements.

El Camino del Cerro Landfill stopped accepting waste during 1978 and is not subject to the state and federal regulations referred to above. However, the Arizona Department of Environmental Quality (ADEQ) has filed a complaint pursuant to other state and federal laws alleging that hazardous substances have been released at the landfill. The County has entered into settlement negotiations with the ADEQ to resolve the cleanup litigation. The County has also voluntarily incurred cleanup expenses for a soil vapor extraction system, a series of drainage improvements, a re-grade of the landfill cap, and groundwater remediation. No liability has been recognized in the financial statements because the outcome of the litigation is uncertain and the amount of the loss cannot be reasonably estimated.

**Construction Contract Retentions Payable**—State laws and regulations require the Department to withhold a portion of progress payments made on construction contracts until the successful completion of the construction project.

Pima County  
Department of Wastewater Management  
Notes to Financial Statements  
June 30, 2005

**Note 6 - Due To Other Pima County Funds**

Due to other Pima County funds represents payables for goods or services. At June 30, 2005, the payables included \$5,498 due to the General Fund, \$9,983 due to the Transportation Fund, \$7,759 due to the Environmental Quality Fund, \$12,003 due to the Self Insurance Fund, and \$72,346 due to the Capital Projects Fund.

**Note 7 - Related Party Transactions**

**Administrative and Fiscal Services**—The Department incurred expenses from Pima County for a variety of administrative and fiscal services, including \$1,762,237 for the allocation of overhead; \$1,235,902 for self-insurance premiums; \$2,491,446 for interdepartmental supplies and services charges; \$1,760,874 for motor pool charges; \$422,981 for professional charges; \$874,029 for repair and maintenance charges; \$39,633 for printing charges; and \$286,686 for miscellaneous other charges.

**Public Works Center**—The Department occupies a portion of the Public Works Center and pays rent based on a pro rata share of the building expenses incurred by the Pima County Facilities Management department. The Department's rent totaled \$234,678 for the year ended June 30, 2005.

**Note 8 - Significant Commitments**

Commitments under construction contracts at June 30, 2005 totaled \$20,019,531.

**Note 9 - Risk Management**

The Department is a participant in Pima County's self-insurance program. The County's self-insurance program covers the Department for risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. In the opinion of the Department's management, any unfavorable outcomes from these types of risks would be covered by that self-insurance program. Accordingly, the Department has no risk of loss beyond adjustments to future years' premium payments to Pima County's self-insurance program. All estimated losses for unsettled claims and actions of Pima County are determined on an actuarial basis and are included in the *Pima County Comprehensive Annual Financial Report*.

Risks of loss arising from contractual breaches are not covered by the County's self-insurance program or commercial insurance. The Department's management does not believe that these types of losses would be material to the financial statements; therefore, no accrual of losses has been reported in the financial statements. At June 30, 2005, there were no material lawsuits related to contractual breaches.

Pima County  
 Department of Wastewater Management  
 Notes to Financial Statements  
 June 30, 2005

**Note 10 - Intergovernmental Agreement**

The City of Tucson, Metropolitan Domestic Water Improvement District (MDWID), Town of Marana Water, and Oro Valley Water provide sewer utility billing and collection services, certain computer services, accounting information, and statistical data to the Department. During the year ended June 30, 2005, the Department paid fees totaling \$1,453,630, \$110,141, \$6,012, and \$106,241, respectively, for such services. As part of its agreement, the City of Tucson invests cash collected from utility customers and held for remittance to the Department. Interest earnings on such investments are remitted to the Department. The MDWID, Town of Marana Water and Oro Valley Water submit cash receipts to the Department regularly. However, cash collections are not invested, and therefore, MDWID, Town of Marana Water, and Oro Valley Water do not remit interest to the Department.

**Note 11 - Segment Information**

Liquid Waste, a division of the Department, is reported within the Department's enterprise fund. Liquid Waste operates the sewer system that provides wastewater collection, treatment, and disposal throughout Pima County. All revenues generated by the ownership, use, and operation of Pima County's sewer system are pledged in support of sewer system debt. In addition, debt covenants require sewer system revenues, expenses, gains, losses, assets, and liabilities to be accounted for separately. As a result, condensed financial information for the Liquid Waste Division is presented below:

**Condensed Statement of Net Assets**

Assets:	
Current assets	\$ 37,616,475
Due from other Pima County funds	58,776
Restricted assets	8,291,335
Capital assets, net of accumulated depreciation	576,000,827
Other noncurrent assets	<u>847,787</u>
Total assets	<u>622,815,200</u>
Liabilities:	
Current liabilities	22,151,526
Due to other Pima County funds	102,740
Noncurrent liabilities	<u>135,137,832</u>
Total liabilities	<u>157,392,098</u>
Net Assets:	
Invested in capital assets, net of related debt	437,062,024
Restricted	3,979,266
Unrestricted	<u>24,381,812</u>
Total net assets	<u>\$465,423,102</u>

Pima County  
 Department of Wastewater Management  
 Notes to Financial Statements  
 June 30, 2005

**Condensed Statement of Revenues, Expenses,  
 and Changes in Fund Net Assets**

Operating revenues (expenses):	
Sewer utility service	\$ 50,393,306
Other operating revenues	1,468,503
Depreciation expense	(17,655,120)
Other operating expenses	<u>(47,036,884)</u>
Operating loss	(12,830,195)
Nonoperating revenues (expenses):	
Sewer connection revenue	36,906,421
Other nonoperating revenues	1,133,149
Interest expense	(4,212,690)
Loss on disposal of equipment	(564,641)
Other nonoperating expenses	(97,087)
Capital contributions	<u>20,722,136</u>
Increase in net assets	41,057,093
Net assets, July 1, 2004 (as restated)	<u>424,366,009</u>
Net assets, June 30, 2005	<u>\$465,423,102</u>

**Condensed Statement of Cash Flows**

Net cash provided by (used for):	
Operating activities	\$ 4,001,143
Noncapital financing activities	688,747
Capital and related financing activities	18,242,009
Investing activities	<u>429,287</u>
Increase in cash and cash equivalents	23,361,186
Cash and cash equivalents, July 1, 2004	<u>11,639,148</u>
Cash and cash equivalents, June 30, 2005	<u>\$ 35,000,334</u>

Pima County  
Department of Wastewater Management  
Notes to Financial Statements  
June 30, 2005

## Note 12 - Retirement Plan

**Plan Description**—The Department contributes to a cost-sharing multiple-employer defined benefit pension plan administered by the Arizona State Retirement System (ASRS) that covers general employees of the Department. Benefits are established by state statute and generally provide retirement, death, long-term disability, survivor, and health insurance premium benefits. The ASRS is governed by the Arizona State Retirement System Board according to the provisions of Arizona Revised Statutes Title 38, Chapter 5, Article 2.

The ASRS issues a comprehensive annual financial report that includes financial statements and required supplementary information. The most recent report may be obtained by writing the Arizona State Retirement System, 3300 North Central Avenue, P.O. Box 33910, Phoenix, Arizona 85067-3910, by calling (602) 240-2000 or on-line at <http://www.ASRS.state.az.us/web/Aboutus.do>.

**Funding Policy**—The Arizona State Legislature establishes and may amend active plan members' and the Department's contribution rates. For the year ended June 30, 2005, active plan members and the Department were each required by statute to contribute at the actuarially determined rate of 5.7 percent (5.2 percent retirement and 0.5 percent long-term disability) of the members' annual covered payroll. The Department's contributions to the ASRS for the years ended June 30, 2005, 2004, and 2003, were \$1,172,625, \$1,219,545, and \$495,645, respectively, which were equal to the required contributions for the year.

## Note 13 -Subsequent Event

On September 1, 2005, at the request of Pima County, the Water Infrastructure Authority of Arizona (WIFA) amended the 2004 WIFA loan agreement with Pima County, increasing available funding from \$18,015,219 to \$19,967,331. There was no change to the interest rate or terms of repayment of the original loan.

## Supplementary Schedules

Pima County  
Department of Wastewater Management  
Combining Statement of Net Assets  
June 30, 2005

Assets

	<u>Liquid Waste</u>	<u>Solid Waste</u>	<u>Total</u>
Current assets:			
Cash and cash equivalents	\$ 26,709,044	\$ 4,081,879	\$ 30,790,923
Interest receivable	78,006	8,957	86,963
Accounts receivable, net	7,747,191	329,819	8,077,010
Due from other Pima County funds	58,776		58,776
Intrafund due from (due to)	(14,194)	14,194	-
Due from other governments	257,051	273,107	530,158
Inventory of materials and supplies	2,814,893		2,814,893
Prepaid expenses	24,484	1,759	26,243
Total current assets	<u>37,675,251</u>	<u>4,709,715</u>	<u>42,384,966</u>
Noncurrent assets:			
Restricted assets:			
Cash and cash equivalents:			
Restricted for construction	2,629,898		2,629,898
Restricted for debt service	1,305,703		1,305,703
Restricted for operation and maintenance	3,511,265		3,511,265
Held in escrow as construction contract retentions	844,424		844,424
Interest receivable	45		45
Total restricted assets	<u>8,291,335</u>		<u>8,291,335</u>
Capital assets, net of accumulated depreciation where applicable:			
Land and other improvements	4,557,210	7,840,639	12,397,849
Solid waste transfer stations, net		1,495,551	1,495,551
Conveyance systems, net	322,144,855		322,144,855
Treatment facilities, net	181,106,962		181,106,962
Equipment, net	4,866,993	1,997,917	6,864,910
Construction in progress	63,324,807		63,324,807
Total capital assets, net	<u>576,000,827</u>	<u>11,334,107</u>	<u>587,334,934</u>
Deferred financing costs	847,787		847,787
Total noncurrent assets	<u>585,139,949</u>	<u>11,334,107</u>	<u>596,474,056</u>
Total assets	<u>\$ 622,815,200</u>	<u>\$ 16,043,822</u>	<u>\$ 638,859,022</u>

(Continued)

Pima County  
 Department of Wastewater Management  
 Combining Statement of Net Assets  
 June 30, 2005  
 (Continued)

Liabilities

	Liquid Waste	Solid Waste	Total
Current liabilities:			
Accounts payable	\$ 3,866,095	\$ 291,231	\$ 4,157,326
Accrued payroll and employee benefits	3,468,086	256,840	3,724,926
Due to other Pima County funds	102,740	4,849	107,589
Due to other governments	1,432	11,216	12,648
Interest payable	1,518,722		1,518,722
Current portion of sewer revenue bonds payable	4,550,000		4,550,000
Current portion of wastewater loans payable	4,950,734		4,950,734
Deferred revenue	3,796,457		3,796,457
Total current liabilities	22,254,266	564,136	22,818,402
Noncurrent liabilities:			
Construction contract retentions payable	4,851,976		4,851,976
Landfill closure and postclosure care costs payable		15,635,842	15,635,842
Sewer revenue bonds payable, less current portion	55,525,000		55,525,000
Wastewater loans payable, less current portion	79,281,579		79,281,579
Deferred interest expense and bond discount	(4,520,723)		(4,520,723)
Total noncurrent liabilities	135,137,832	15,635,842	150,773,674
Total liabilities	157,392,098	16,199,978	173,592,076
Net Assets			
Invested in capital assets, net of related debt	437,062,024	11,334,107	448,396,131
Restricted for:			
Debt service	467,956		467,956
Capital projects	45		45
Wastewater management	3,511,265		3,511,265
Unrestricted	24,381,812	(11,490,263)	12,891,549
Total net assets	\$ 465,423,102	\$ (156,156)	\$ 465,266,946

Pima County  
Department of Wastewater Management  
Combining Statement of Revenues, Expenses,  
and Changes in Fund Net Assets  
Year Ended June 30, 2005

	<u>Liquid Waste</u>	<u>Solid Waste</u>	<u>Total</u>
Operating revenues:			
Sewer utility service	\$ 50,393,306		\$ 50,393,306
Solid waste fees		\$ 4,670,430	4,670,430
Engineering review and inspection fees	70,754		70,754
Permits and fines	101,160		101,160
Other income	1,296,589	581,587	1,878,176
Total operating revenues	<u>51,861,809</u>	<u>5,252,017</u>	<u>57,113,826</u>
Operating expenses:			
Employee compensation	24,730,566	2,190,751	26,921,317
Operating supplies	4,712,606	1,142	4,713,748
Utilities	3,772,346	45,294	3,817,640
Sludge and refuse disposal	1,519,857	936,265	2,456,122
Repairs and maintenance	2,750,888	851,794	3,602,682
General and administrative	6,438,499	946,560	7,385,059
Consultants and professional services	3,112,122	427,300	3,539,422
Depreciation	17,655,120	452,976	18,108,096
Total operating expenses	<u>64,692,004</u>	<u>5,852,082</u>	<u>70,544,086</u>
Operating loss	<u>(12,830,195)</u>	<u>(600,065)</u>	<u>(13,430,260)</u>
Nonoperating revenues (expenses):			
Intergovernmental revenue	635,019		635,019
Interest income	498,130	78,018	576,148
Sewer connection revenue	36,906,421		36,906,421
State-shared tax revenue		1,162,869	1,162,869
Loss on disposal of equipment	(564,641)		(564,641)
Interest expense	(4,212,690)		(4,212,690)
Amortization of deferred charges	(97,087)		(97,087)
Total nonoperating revenues (expenses)	<u>33,165,152</u>	<u>1,240,887</u>	<u>34,406,039</u>
Income before capital contributions and transfers	<u>20,334,957</u>	<u>640,822</u>	<u>20,975,779</u>
Capital contributions	20,722,136		20,722,136
Transfers out		(52,742)	(52,742)
Increase in net assets	41,057,093	588,080	41,645,173
Net assets—July 1, 2004 (as restated)	<u>424,366,009</u>	<u>(744,236)</u>	<u>423,621,773</u>
Net assets—June 30, 2005	<u>\$465,423,102</u>	<u>\$ (156,156)</u>	<u>\$ 465,266,946</u>

Pima County  
Department of Wastewater Management  
Combining Statement of Cash Flows  
Year Ended June 30, 2005

	Liquid Waste	Solid Waste	Total
Cash flows from operating activities:			
Receipts from customers	\$ 48,933,657	\$ 4,644,331	\$ 53,577,988
Miscellaneous receipts	1,296,589	195,796	1,492,385
Payments to suppliers for goods and services	(15,663,636)	(297,626)	(15,961,262)
Payments to other Pima County Funds for goods and services	(6,146,612)	(2,974,077)	(9,120,689)
Payments to employees	(24,418,855)	(2,175,942)	(26,594,797)
Net cash provided by (used for) operating activities	4,001,143	(607,518)	3,393,625
Cash flows from noncapital financing activities:			
Intrafund borrowings	37,424	(37,424)	
Intergovernmental receipts	635,019		635,019
State-shared tax receipts		1,162,869	1,162,869
Repayment of interfund borrowings	16,304		16,304
Cash transfers to other Pima County Funds		(52,742)	(52,742)
Net cash provided by noncapital financing activities	688,747	1,072,703	1,761,450
Cash flows from capital and related financing activities:			
Sewer connection receipts from customers	35,688,645		35,688,645
Federal contract receipts	188,409		188,409
Purchase and construction of capital assets	(10,653,796)	(219,473)	(10,873,269)
Principal payments on revenue bonds and loans	(4,705,000)		(4,705,000)
Interest payments on revenue bonds and loans	(2,276,249)		(2,276,249)
Net cash provided by (used for) capital and related financing activities	18,242,009	(219,473)	18,022,536
Cash flows from investing activities:			
Interest received on investments	429,287	72,182	501,469
Net cash provided by investing activities	429,287	72,182	501,469
Net increase in cash and cash equivalents	23,361,186	317,894	23,679,080
Cash and cash equivalents, July 1, 2004	11,639,148	3,763,985	15,403,133
Cash and cash equivalents, June 30, 2005	\$ 35,000,334	\$ 4,081,879	\$ 39,082,213

(Continued)

Pima County  
Department of Wastewater Management  
Combining Statement of Cash Flows  
Year Ended June 30, 2005  
(Continued)

	Liquid Waste	Solid Waste	Total
Reconciliation of operating loss to net cash provided by operating activities:			
Operating loss	\$(12,830,195)	\$ (600,065)	\$ (13,430,260)
Adjustments to reconcile operating loss to net cash provided by operating activities:			
Depreciation	17,655,120	452,976	18,108,096
Landfill closure and postclosure care costs		(385,791)	(385,791)
Changes in assets and liabilities:			
Decrease (increase) in assets:			
Accounts receivable	(1,563,042)	(2,992)	(1,566,034)
Due from other governments	(68,521)	(23,107)	(91,628)
Inventory of materials and supplies	(118,435)		(118,435)
Prepaid expenses	60,268	5,108	65,376
Increase (decrease) in liabilities:			
Accounts payable	552,805	(67,418)	485,387
Due to other governments	1,432	11,216	12,648
Accrued payroll and employee benefits	311,711	14,809	326,520
Due to other Pima County funds		(12,254)	(12,254)
Net cash provided by (used for) operating activities	\$ 4,001,143	\$ (607,518)	\$ 3,393,625

Noncash investing, capital, and noncapital financing activities:

During the year ended June 30, 2005, developers conveyed capital assets with an estimated fair value of \$21,820,307 to the Department. This transaction was recorded as a capital contribution.

During the year ended June 30, 2005, the Pima County Board of Supervisors approved Connection Fee Flow-Through Sewer Credit Agreements totaling \$1,098,171. This transaction was recorded as an increase to deferred revenue and a decrease in capital contributions.

During the year ended June 30, 2005, the Department retired assets with a net book value of \$564,641.

During the year ended June 30, 2005, the Department adjusted the Corrective Action Costs decreasing the landfill liability and increasing miscellaneous revenue by \$385,791.

During the year ended June 30, 2005, the Department transferred \$196,786 of fully-depreciated capital assets to Pima County.

