W A T E R

CITY OF RIVERSIDE
CELEBRATING 100 YEARS
WATER DEPARTMENT 1913

INDEPENDENT AUDITORS' REPORT: WATER

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REPORT OF INDEPENDENT AUDITORS

To the Honorable City Council and Board of Public Utilities
City of Riverside
Riverside, California

We have audited the accompanying balance sheet of the City of Riverside, California, Water Utility (Water Utility), as of and for the year ended June 30, 2012, and the related statement of revenues, expenses and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Water Utility's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year partial comparative information has been derived from the financial statements of the Water Utility for the year ended June 30, 2011, and in our report dated October 14, 2011, we expressed unqualified opinion on those financial statements.

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 includes consideration of internal control over financial reporting as a basis for designing 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 over financial reporting. Accordingly, we express no such opinion. 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 present only the Water Utility and do not purport to, and do not, present fairly the financial position of the City of Riverside, as of June 30, 2012, and the changes in its financial position, or, where applicable, 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 the Water Utility as of June 30, 2012 and the results of its individual and combined operations and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Praxity

To the Honorable City Council and Board of Public Utilities
City of Riverside

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with the auditing standards generally accepted in the United States of America, which consisted of inquiries with management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The financial information included as supplementary information following the financial statements and notes to financial statements is provided for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements and we do not express an opinion on it.

Moss Adams LLP

Los Angeles, California
October 24, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS: WATER

As management of Riverside Public Utilities, a department of the City of Riverside (the City), we offer the readers this narrative overview and analysis of the 2011-12 financial report for the period ended June 30, 2012 and 2011 for Riverside's Water Utility (the Utility), an enterprise fund of the City. We encourage readers to consider the information presented here in conjunction with additional information furnished in our financial statements, which begin on page 71 of this report. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

FINANCIAL HIGHLIGHTS

Fiscal years 2012 and 2011 reflected strong operating results for the Water Utility, with retail sales exceeding the previous year's results, primarily from the effects of rate increases, expanded customer base, and an increase in consumption.

- Retail sales, net of reserve/recovery, were $59,620 and $55,186 for the years ended June 30, 2012 and 2011, respectively. The increase in sales was primarily due to a full year of rate increases under the SAFE W.A.T.E.R (Water Available to Everyone in Riverside) Plan required to support the Utility's Water Master, Water Supply and Asset Management Plans and a 4.4% increase in retail consumption.
- The assets of the Utility exceeded its liabilities (equity) at the close of fiscal years 2012 and 2011 by $313,939 and $301,733, respectively. Of this amount, $61,859 and $52,181, respectively, may be used to meet the Utility's ongoing obligations to creditors and customers.
- The Utility's total equity as of June 30, 2012 and 2011 increased by $12,206 and $23,739 from fiscal years ended June 30, 2011 and 2010, respectively, primarily due to positive operating results and an intra-entity property sale.
- As of June 30, 2012 and 2011, unrestricted equity represented 129% and 110% of annual operating expenses, respectively.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City of Riverside Water Utility financial statements. The Water Utility is a department of the City of Riverside, and its activities are recorded in a separate enterprise fund. These financial statements include only the activities for the City of Riverside Water Utility and provide comparative information for the last two fiscal years. Information on city-wide financial results is available in the City of Riverside's "Comprehensive Annual Financial Report."

The City of Riverside Water Utility's financial statements are comprised of two components: 1) financial statements, and 2) notes to the financial statements. In addition, this report also contains other supplementary information to provide the reader with additional information about the Water Utility, including key historical operating and other relevant data.

Included as part of the financial statements are three separate statements, which collectively provide an indication of the Water Utility's financial health.

The ***Balance Sheets*** present information on assets and liabilities, with the difference between the two reported as equity. Over time, increases or decreases in equity may serve as a useful indicator of whether the financial condition of the Utility is improving or deteriorating.

The ***Statements of Revenues, Expenses and Changes in Equity*** present information showing how the Utility's equity changed during the most recent two fiscal years. Results of operations are reported as underlying events occur, regardless of the timing of cash flows. Thus, revenues and expenses are reported in these statements for some items that will result in cash flows in future fiscal periods, e.g., accounts payable and accounts receivable. This is called the accrual basis of accounting and is described in more detail in the accompanying Notes to the Financial Statements.

The ***Statements of Cash Flows*** present the cash flow changes occurring during the last two fiscal years in highly liquid cash and cash equivalents, including certain restricted assets.

The ***Notes to the Financial Statements*** provide additional information that is essential to a full understanding of the data provided in the Water Utility's financial statements. The notes to the financial statements can be found on pages 77 to 89 of this report.

UTILITY FINANCIAL ANALYSIS

As noted earlier, equity (also called net assets) may serve over time as a useful indicator of the fund's financial position. In the case of Riverside's Water Utility, assets exceeded liabilities by $313,939 and $301,733 at the close of the fiscal years 2012 and 2011, respectively.

The following table summarizes the Utility's financial condition as of June 30:

CONDENSED STATEMENTS OF EQUITY (NET ASSETS)

	2012	2011	2010
Current and other assets	$ 141,346	$ 143,395	$ 148,966
Capital assets	409,675	392,264	372,792
Total assets	551,021	535,659	521,758
Long-term debt outstanding	204,526	209,112	219,414
Other liabilities	32,556	24,814	24,350
Total liabilities	237,082	233,926	243,764
Invested in capital assets, net of related debt	243,997	241,552	237,366
Restricted	8,083	8,000	8,599
Unrestricted	61,859	52,181	32,029
Total equity (net assets)	$ 313,939	$ 301,733	$ 277,994

ASSETS

Fiscal Year 2012 Total assets of $551,021 reflect an increase of $15,362 (2.9%), mainly due to the following:

- Current and other assets, comprised of restricted and unrestricted assets, reflect the use of $19,477 of bond proceeds for capital projects offset by a cash and cash equivalent increase of $7,123 primarily due to positive operating results and an increase of $6,838 in deferred debits on an interest rate swap fair valuation in accordance with Governmental Accounting Standards Board Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments* (GASB 53). See Notes 1 and 4 in the accompanying financial statements for additional information.
- Net capital assets (Utility plant net of depreciation), increased by $17,411 primarily due to an increase of $31,287 in completed transmission and distribution system assets related to pipeline replacement, system expansion and improvements, facilities rehabilitation and reservoir construction, offset by a decrease of $13,876 in construction in progress. Additional capital asset information can be found in the "Capital Assets and Debt Administration" section of the financial analysis.

Fiscal Year 2011 Total assets of $535,659 reflect an increase of $13,901 (2.7%), due to the use of $25,620 of bond proceeds for capital projects and a decrease of $6,580 in deferred debits on an interest rate swap fair valuation in accordance with GASB 53 offset by an increase in current and other assets of $27,434 primarily due to intra-entity property sale and positive operating results. Net capital assets (Utility plant) increased by $19,472 as a result of completed transmission and distribution system assets and an increase in construction in progress for pipeline replacement, system expansion and improvements, facilities rehabilitation and reservoir construction.

LIABILITIES

Fiscal Year 2012 The Utility's total liabilities were $237,082, an increase of $3,156 (1.3%), mainly due to the following:

- Other liabilities increased by $7,742 primarily due to $7,320 increase in derivative instruments related to interest rate swap fair valuation in accordance with GASB 53. See Note 4 in the accompanying financial statements for additional information.
- Long-term debt outstanding decreased by $4,586 primarily due to $4,545 in principal payments.

Fiscal Year 2011 The Utility's total liabilities were $233,926 a decrease of $9,838 (4.0%), primarily due to long-term debt outstanding decreased by $10,302 due to $4,660 in principal payments and $5,675 in unamortized deferred bond refunding costs.

EQUITY (NET ASSETS)

Fiscal Year 2012 The Utility's equity, which represents the difference between the Utility's resources and its obligations, totaled $313,939 an increase of $12,206 (4.0%) is comprised of the following:

- The largest portion of the Utility's equity is $243,997 (77.7% of total equity), and reflects its investment in capital assets, such as treatment, pumping, source of supply, transmission and distribution facilities, less any related outstanding debt used to acquire these assets. This portion increased by $2,445 (1.0%) primarily due to an increase in capital assets constructed or purchased during the fiscal year, net of the debt used to acquire these assets. Additional capital asset information can be found in the "Capital Assets and Debt Administration" section.
- The restricted portion totaled $8,083 (2.6% of total equity), an increase of $83 from prior fiscal year. Restricted equity is subject to internal and external restrictions on use and is reserved for items such as debt repayment and funds collected for the Conservation and Reclamation Programs.
- The unrestricted portion totaled $61,859 (19.7% of total equity), an increase of $9,678, primarily attributable to positive operating results.

Fiscal Year 2011 The Utility's equity increased by $23,739 (8.5%) to $301,773. The largest portion of the equity, $241,552 (80.0%), is represented by investment in capital assets, which increased by $4,186 (1.8%) primarily due to an increase in capital assets constructed or purchased during the fiscal year, net of the debt used to acquire these assets. The restricted portion decreased by $599 due to decreases in debt service reserves for principal and interest payments for new bond issues. The unrestricted portion increased by $20,152, primarily attributable to the intra-entity property sale and positive operating results.

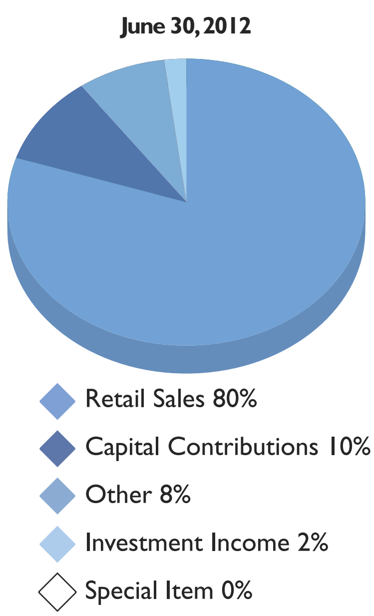
UTILITY FINANCIAL ANALYSIS (CONTINUED)

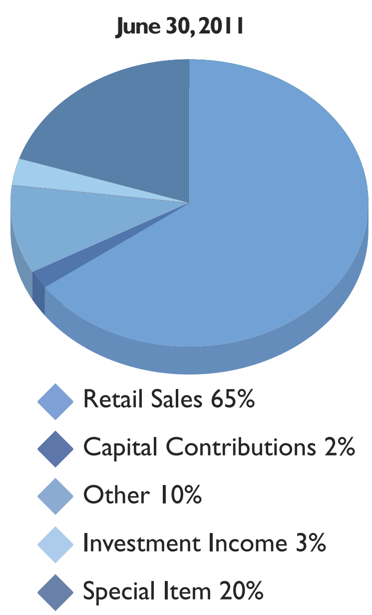
The Water Utility's overall increase in equity of $12,206 and $23,739 during fiscal years 2012 and 2011, respectively, was due to positive operating results that can be further explained in the following Condensed Statements of Changes in Equity:

CONDENSED STATEMENTS OF CHANGES IN EQUITY (NET ASSETS)

	2012	2011	2010
Revenues:			
Retail sales, net	$ 59,620	$ 55,186	$ 51,147
Other revenues	6,543	8,936	8,553
Investment income	1,428	2,635	1,815
Capital contributions	7,440	1,982	2,052
Total revenues	75,031	68,739	63,567
Expenses:			
Operations and maintenance	31,633	31,411	32,151
Purchased energy	4,600	4,558	4,362
Depreciation	11,824	11,386	10,660
Interest expenses and fiscal charges	8,510	8,912	7,886
Total expenses	56,567	56,267	55,059
Transfers to the City's general fund	(6,258)	(5,847)	(5,657)
Special item	-	17,114	-
Changes in equity	12,206	23,739	2,851
Equity, July 1	301,733	277,994	275,143
Equity, June 30	$ 313,939	$ 301,733	$ 277,994

REVENUES BY SOURCES





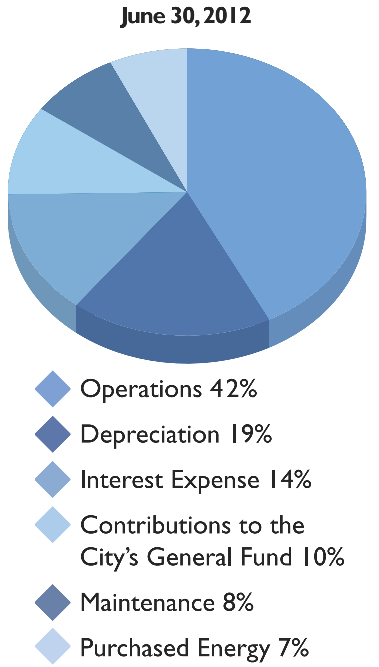
Fiscal Year 2012 Total revenues of $75,031 decreased by $10,822 (12.6%) from prior fiscal year, due to the following major changes:

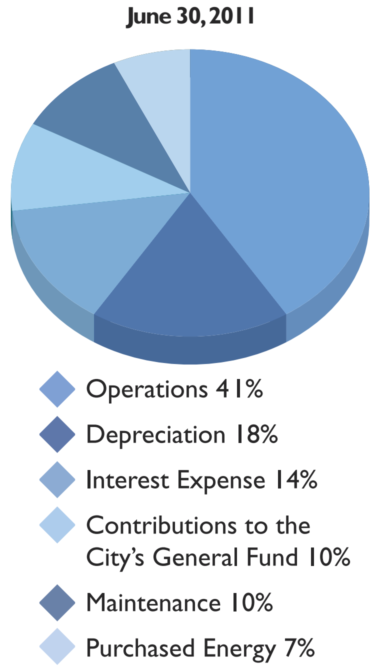
- Retail sales (residential, commercial, industrial, and others), net of reserve/recovery, totaled $59,620, an increase of $4,434 (8.0%) over the prior fiscal year. Retail sales continue to be the primary revenue source for the Water Utility, making up 80% of total revenues. The increase in sales was primarily due to a full year rate increase of 10% that became effective November 1, 2010 as part of the SAFE W.A.T.E.R. Plan, and a 4.4% increase in retail consumption.
- A prior year special item of $17,114 for an intra-entity property sale.
- Other revenues of $6,543 decreased by $2,393 (26.8%), primarily due to a decrease of $1,064 on gain on the sale of assets in the prior fiscal year and a decrease of $1,221 in other operating revenue.
- Investment income of $1,428 decreased by $1,207 (45.8%), due to a decrease in cash as a result of the use of bond proceeds for capital projects.
- Capital contributions of $7,440 increased by $5,458 (275.4%), primarily due to an increase in project activity related to Riverside County Transportation Commission (RCTC).

Fiscal Year 2011 Total revenues of $85,853, which included a special item, increased by $22,286 (35.1%) from prior fiscal year due to the following major changes:

- Net retail sales were $55,186, 65% of total revenues, reflecting an increase of $4,039 (7.9%) in net retail sales from the prior fiscal year primarily due to a 10.0% rate increase that became effective November 1, 2010 as part of the SAFE W.A.T.E.R. Plan, offset by a 3.0% decrease in retail consumption.
- A special item of $17,114 represented an intra-entity property sale.
- Investment income of $2,635 increased by $820 (45.2%), due to interest earned on the increase in cash as a result of the intra-entity property sale and a full year's interest on bond proceeds.

EXPENSES BY SOURCES





UTILITY FINANCIAL ANALYSIS (CONTINUED)

Fiscal Year 2012 Total expenses, excluding general fund transfer, were $56,567, an increase of $300 (0.5%) over the prior year's expenses.

Fiscal Year 2011 Total expenses were $56,267, reflecting an increase of $1,208 (2.2%), due to an increase in interest expense and fiscal charges due to the 2011 bond issuance and a full year of interest for the 2009 bond issuance and an increase in depreciation expense due to the completion of $20,622 of capital projects that were included as depreciable capital assets.

TRANSFERS

Pursuant to the City of Riverside Charter, the Water Utility may transfer up to 11.5 percent of prior year's gross operating revenues including adjustments to the City's general fund. The City uses these funds to help provide needed public services to the residents of the City, including police, fire, parks, libraries and other benefits.

Fiscal Year 2012 The Water Utility transferred the maximum allowable by the City Charter to the City's general fund, or $6,258, an increase of $411, primarily the result of a $4,039 increase in retail sales for fiscal year 2011.

Fiscal Year 2011 Transfers to the City's general fund of $5,847 increased by $190, primarily the result of increased retail sales of $1,556 for fiscal year 2010.

CAPITAL ASSETS AND DEBT ADMINISTRATION

CAPITAL ASSETS

The Water Utility's investment in capital assets includes investments in source of supply, pumping, treatment, transmission and distribution facilities, land, intangibles, and construction in progress, as well as general items such as office equipment, furniture, etc.

The following table summarizes the Utility's capital assets, net of depreciation as of June 30:

	2012	2011	2010
Source of supply	$ 33,888	$ 32,955	$ 33,215
Pumping	17,871	17,175	16,885
Treatment	36,355	34,998	35,739
Transmission and distribution	289,285	260,134	248,994
General	4,069	5,266	5,721
Land	10,996	10,861	10,809
Intangible	6,519	6,307	6,307
Construction in progress	10,692	24,568	15,122
Total	$ 409,675	$ 392,264	$ 372,792

Fiscal Year 2012 The Utility's investment in capital assets was $409,675, an increase of $17,411 (4.4%). The increase (net of accumulated depreciation) resulted mainly from the following significant capital projects:

• $15,653 for system expansion and improvements, facilities rehabilitation and reservoir construction.

• $6,050 for continued pipeline replacement programs.

• $5,987 for the Riverside County Transportation Commission project (RCTC).

Fiscal Year 2011 Investment in capital assets (net of accumulated depreciation) for the Utility increased by $19,472 (5.2%), for a total of $392,264. Major capital projects included $22,101 for system expansion and improvements including, facilities rehabilitation and reservoir construction, and $6,299 for continued pipeline replacement programs.

Additional information regarding capital assets can be found in Note 3 on Page 85 of this report.

DEBT ADMINISTRATION

The following table summarizes outstanding long-term debt (revenue bonds) as of June 30:

	2012	2011	2010
Revenue bonds	$ 213,320	$ 217,865	$ 222,525
Unamortized bond premium	4,341	4,797	4,987
Contracts payable	947	947	949
Less:			
Current portion	(4,845)	(4,695)	(4,810)
Unamortized deferred bond refunding costs	(9,237)	(9,802)	(4,127)
Unamortized capital appreciation	-	-	(110)
Total	$ 204,526	$ 209,112	$ 219,414

The Water Utility's bond indentures require the Utility to maintain a minimum debt service coverage ratio, as defined by the bond covenants, of 1.25. The Water Utility's debt service coverage ratio was 2.82, 3.49, and 2.08 at June 30, 2012, 2011, and 2010, respectively. The debt is backed by the revenues of the Utility (revenue bonds).

Fiscal Year 2012 Total long-term debt decreased by $4,586 (2.2%) to $204,526 primarily due to $4,545 of principal payments.

Fiscal Year 2011 Long-term debt of $209,112 decreased by $10,302 (4.7%) primarily due to $4,660 of principal payments and $5,675 in unamortized deferred bond refunding costs.

Additional information on the Water Utility's long-term debt can be found in Note 4 on pages 85 to 88 of this report.

CREDIT RATINGS

In April 2012, Standard & Poor's affirmed its "AAA" long-term credit rating on the Water Utility's outstanding debt and its"A-1+" on the short-term rating on the 2011A Variable Rate Water Refunding Revenue Bonds. The ratings reflect the Utility's "strong historical and projected debt service coverage and strong cash reserves; advantageous water supply position with low-cost groundwater sources providing nearly all of the city's water, thereby helping the Utility to maintain low rates to its customers; and local economic base that is enduring the economic downturn."

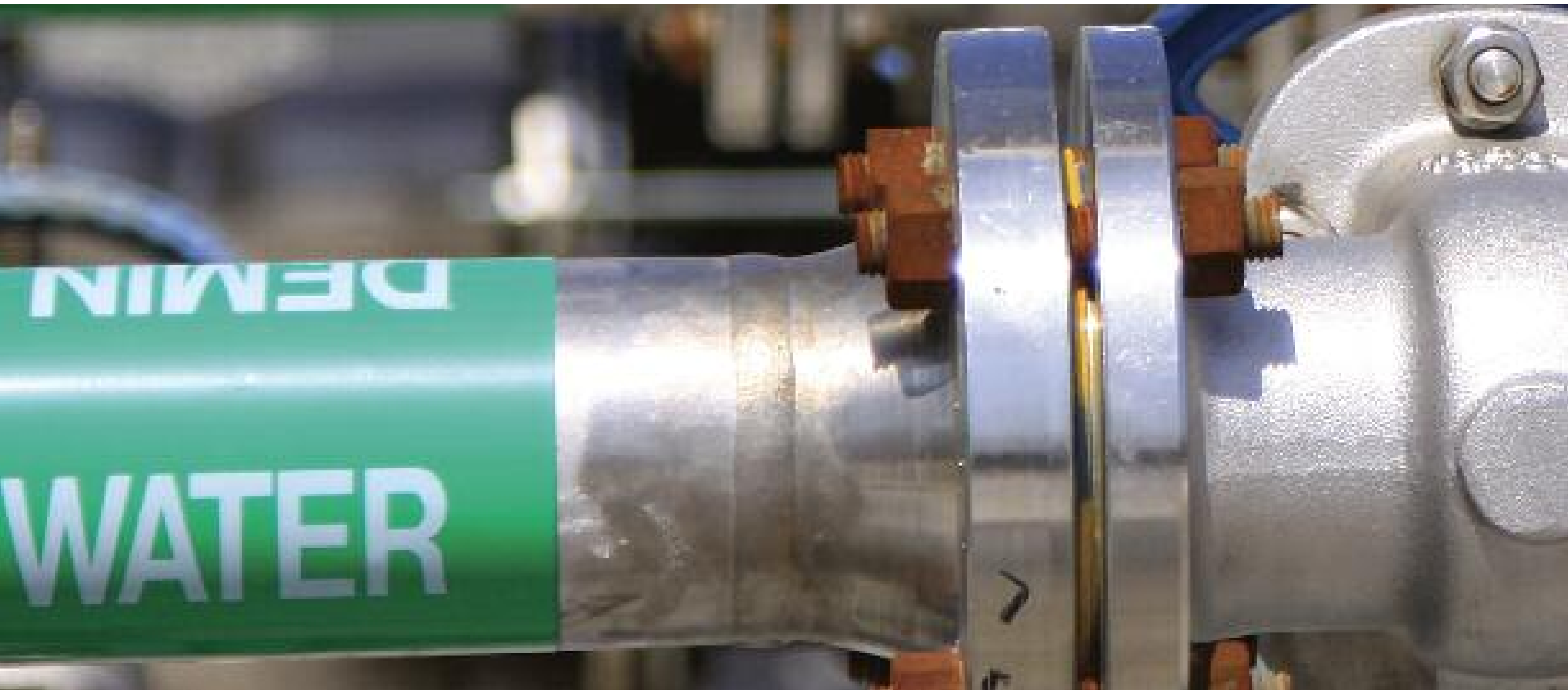
In April 2012, Moody's also affirmed its "Aa2" long-term rating on the 2011A Variable Rate Water Refunding Revenue Bonds. The ratings reflect the Utility's "consistent rate increases that have helped drive sound current and projected fiscal operations, strong levels of unrestricted cash reserves, water source independence which should insulate the Utility from the vulnerabilities of the State's water supply, and solid debt service coverage levels."

In May 2011, Fitch Ratings assigned an "AA+" long-term rating on the 2011A Variable Rate Water Refunding Revenue Bonds and affirmed the "AA+" rating on the Water Utility's outstanding debt. The ratings reflect the Utility's "healthy debt service coverage and liquidity levels, minimal reliance on connection fee revenues, rate flexibility is strong and competitive rates, capital plan that is designed to increase system reliability and water system that provides an essential service with a low cost of supplies."

REGULATORY AND LEGISLATIVE FACTORS

Utilities are faced with ongoing regulatory and legislative mandates enacted at the federal and state level that will have significant impact on the operations of the Utility.

The adoption of the Utility's SAFE W.A.T.E.R. Plan in March 2006, was to implement system improvements contained in the Water Master, Water Supply and Asset Management Plans. The SAFE W.A.T.E.R. Plan was initially funded by a fifty-two percent, five-year water rate increase, consisting of a twelve percent and four-ten percent increases effective November 1, 2006, 2007, 2008,



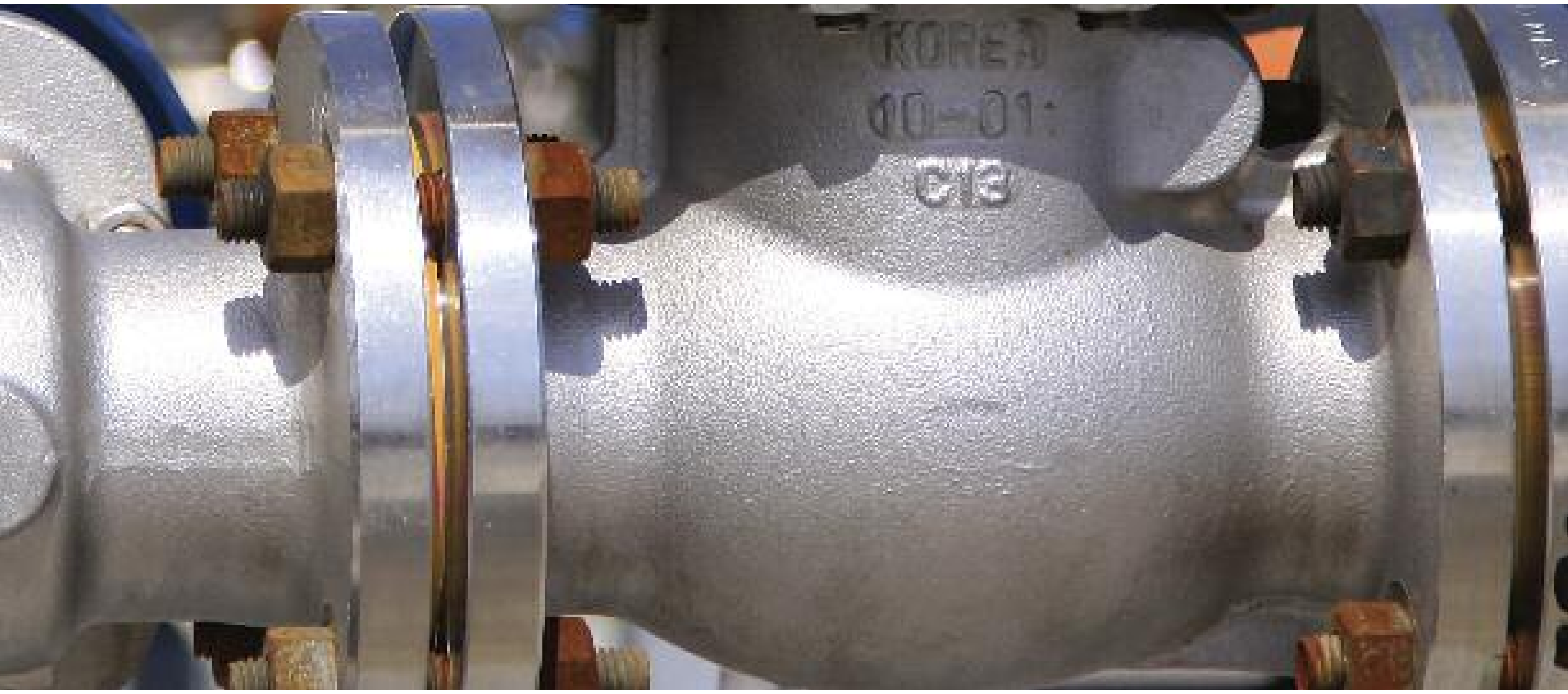
2009, and 2010, respectively. The Utility continues to make significant progress in replacing its aging infrastructure and since implementation of the rate increases, the Utility has invested approximately $162,000 in infrastructure improvements.

With the completion of the J.W. North Treatment Plant, the Utility is water independent and does not rely on state projects for water supply. However, under certain emergency conditions or a prolonged interruption of water supply, the challenges faced at the state level could impact the Utility. The state's primary water system, the Sacramento-San Joaquin River Delta, is in an ecological crisis that has led to historic restrictions on water deliveries from northern to southern California and threatens California's economy and endangered species. The levees that protect the Delta are at risk of failure and climate change will exacerbate the existing water management challenges.

In November 2009, the California legislature enacted a comprehensive set of laws aimed at improving the state's water supply reliability and restoring the Sacramento-San Joaquin River Delta ecosystem. The package included four policy bills and an $11.14 billion general obligation bond measure targeted for the November 2012 ballot. However, due to the economic downturn and state budget crisis, the general obligation bond measure has been postponed from the November 2012 ballot. One of the bills enacted, SB X7-7, requires a statewide 20% reduction in urban percapita water use by 2020. It also requires development of agricultural water management plans by December 31, 2012. The Utility has developed a comprehensive Water Efficiency Master Plan that outlines the steps necessary to comply with this requirement. For more information on the Utility's conservation efforts and available programs, visit BlueRiverside.com

In August 2011, the United States Fish and Wildlife Service (FWS) issued a draft rule designating portions of the Santa Ana River as critical habitat for the Southwestern Willow Flycatcher *(Empidonax traillii extimus)*, a federally threatened bird species. If approved, this could increase costs to planned water supply projects.

In December 2010, the FWS issued a final rule designating the Santa Ana River and the San Gabriel River as critical habitat for the Santa Ana Sucker *(Catostomus santaanae)*, a federally threatened fish species. This final rule expanded the existing designation of 8,305 acres to 9,331 acres of the Santa Ana River and the San Gabriel River as critical habitat for the Santa Ana Sucker. This expansion can potentially impact a number of water supply projects planned by the Utility. The Utility has joined with eleven other local cities and water agencies in filing a lawsuit against the federal government to overturn the rule. A hearing on plaintiffs' and defendant's motions for Summary Judgment was held in U.S. District Court in Santa Ana on September 20, 2012. A decision is expected by the end of calendar year 2012. Additionally, a recently formed collaborative between a number of the agencies involved in the lawsuit, the FWS, the California Department of Fish and Game, and the US Army Corps of Engineers is seeking



projects to improve habitat and serve as mitigation for planned projects within the Santa Ana River. The Utility will remain engaged and will continue to advocate at the state and federal level for sound environmental policy.

In September 2010 and July 2011, respectively, the U.S. Environmental Protection Agency (EPA) issued a first and second draft of the Scientific Human Health Assessment (toxicological review of Hexavalent Chromium, also known as Chrome-6). Water supply from underground aquifers in the Riverside and San Bernardino areas contain trace levels of naturally occurring Hexavalent Chromium, but at levels well exceeding the EPA standards. The EPA is developing new drinking water standards for Hexavalent Chromium and plan to release the third draft in 2013. In the interim period, the EPA is providing guidance to water systems on how they may monitor for Chromium 6, in addition to the monitoring they are required to perform for total chromium. Depending on the final drinking water standard adopted, there could be a significant impact to water supply costs. Management continues to monitor the progress of these rules and will advocate for standards that protect human health and are based on the best available science.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the City of Riverside Water Utility's finances. Questions concerning any information provided in this report or requests for additional financial information should be addressed to the Assistant General Manager Finance/Administration, Riverside Public Utilities, 3750 University Avenue, 3rd floor, Riverside, CA 92501. Additional financial information can also be obtained by visiting RiversidePublicUtilities.com.

FINANCIAL STATEMENTS: WATER

BALANCE SHEETS

ASSETS	June 30, 2012	June 30, 2011
	(in thousands)	
UTILITY PLANT:		
Utility plant, net of depreciation (Note 3)	$ 409,675	$ 392,264
RESTRICTED ASSETS:		
Cash and cash equivalents (Note 2)	5,764	5,684
Cash and investments at fiscal agent (Note 2)	41,810	61,287
Total restricted non-current assets	47,574	66,971
OTHER NON-CURRENT ASSETS:		
Deferred pension costs	5,327	5,480
Deferred bond issuance costs	1,882	1,957
Deferred debits (Note 4)	6,838	-
Total other non-current assets	14,047	7,437
Total non-current assets	471,296	466,672
CURRENT ASSETS:		
Unrestricted assets:		
Cash and cash equivalents (Note 2)	63,927	56,804
Accounts receivable, less allowance for doubtful accounts 2012 $111; 2011 $261	12,105	9,385
Accrued interest receivable	280	435
Advances to City	976	-
Prepaid expenses	23	2
Total unrestricted current assets	77,311	66,626
Restricted assets:		
Conservation and Reclamation - Cash and cash equivalents (Note 2)	2,294	2,245
Conservation and Reclamation Programs receivable	120	116
Total restricted current assets	2,414	2,361
Total current assets	79,725	68,987
Total assets	$ 551,021	$ 535,659

See accompanying notes to the financial statements

BALANCE SHEETS

EQUITY AND LIABILITIES	June 30, 2012	June 30, 2011
	(in thousands)	
EQUITY:		
Invested in capital assets, net of related debt	$ 243,997	$ 241,552
Restricted for:		
Debt service (Note 5)	5,764	5,684
Conservation and Reclamation Programs	2,319	2,316
Unrestricted	61,859	52,181
Total equity	313,939	301,733
LONG-TERM OBLIGATIONS, LESS CURRENT PORTION (NOTE 4)	204,526	209,112
OTHER NON-CURRENT LIABILITIES:		
Advance from City - Pension obligation (Notes 1 and 4)	5,164	5,327
Postemployment benefits payable (Notes 1 and 4)	1,644	1,222
Derivative instrument (Note 4)	12,768	5,448
Deferred charges on derivative instrument (Note 4)	-	482
Total other non-current liabilities	19,576	12,479
CURRENT LIABILITIES PAYABLE FROM RESTRICTED ASSETS:		
Accrued interest payable	1,858	1,891
Conservation and Reclamation Programs payable	95	45
Current portion of long-term obligations (Note 4)	4,695	4,545
Total current liabilities payable from restricted assets	6,648	6,481
CURRENT LIABILITIES:		
Accounts payable and other accruals	5,458	5,026
Current portion of long-term obligations (Note 4)	150	150
Customer deposits	724	678
Total current liabilities	6,332	5,854
Total liabilities	237,082	233,926
COMMITMENTS AND CONTINGENCIES (NOTES 6 AND 7)	-	-
Total equity and liabilities	$ 551,021	$ 535,659

See accompanying notes to the financial statements

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN EQUITY

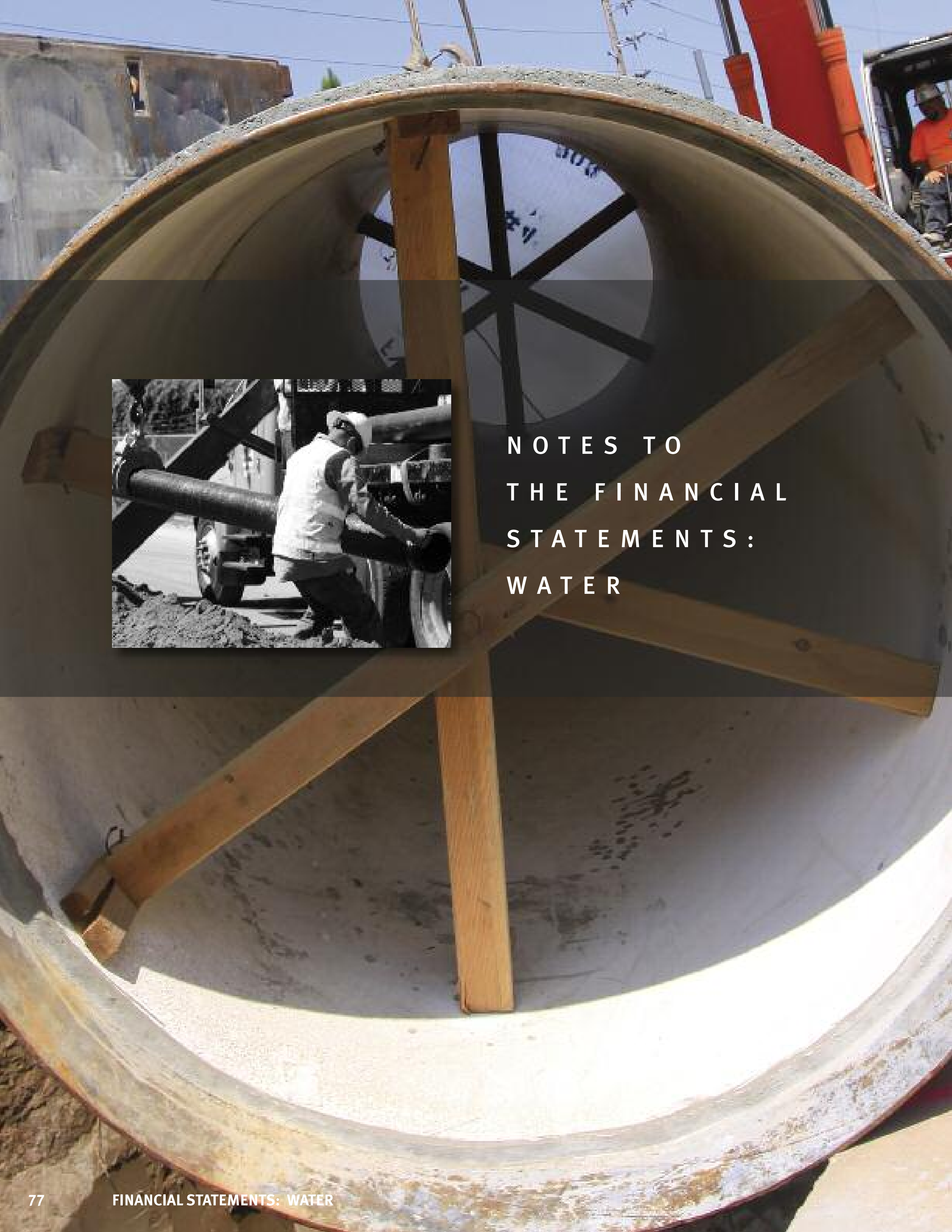
	For the Fiscal Years Ended June 30, 2012 (in thousands)	2011
OPERATING REVENUES:		
Residential sales	$ 38,552	$ 35,721
Commercial sales	19,353	17,863
Other sales	1,863	1,725
Wholesale sales	2,599	2,745
Conservation and Reclamation Programs	928	898
Other operating revenue	1,911	3,132
Total operating revenues before (reserve)/recovery	65,206	62,084
Reserve for uncollectible, net of bad debt recovery	(148)	(123)
Total operating revenues, net of (reserve)/recovery	65,058	61,961
OPERATING EXPENSES:		
Operations	25,668	24,791
Maintenance	5,040	5,872
Purchased energy	4,600	4,558
Conservation and Reclamation Programs	925	748
Depreciation	11,824	11,386
Total operating expenses	48,057	47,355
Operating income	17,001	14,606
NON-OPERATING REVENUES (EXPENSES):		
Investment income	1,428	2,635
Interest expense and fiscal charges	(8,510)	(8,912)
Gain on sale of capital assets	187	1,251
Other	918	910
Total non-operating revenues (expenses)	(5,977)	(4,116)
Income before contributions and transfers	11,024	10,490
Capital contributions	7,440	1,982
Transfers out - contributions to the City's general fund	(6,258)	(5,847)
Total capital contributions and transfers out	1,182	(3,865)
Income before special item	12,206	6,625
SPECIAL ITEM:		
Intra-entity property sale	-	17,114
Increase in equity	12,206	23,739
EQUITY, BEGINNING OF YEAR	301,733	277,994
EQUITY, END OF YEAR	$ 313,939	$ 301,733

See accompanying notes to the financial statements

STATEMENTS OF CASH FLOWS

	For the Fiscal Years Ended June 30, 2012 (in thousands)	2011
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from customers and users	$ 64,610	$ 60,023
Cash paid to suppliers and employees	(35,345)	(34,101)
Other receipts	918	910
Net cash provided by operating activities	30,183	26,832
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES:		
Transfers out - contributions to the City's general fund	(6,258)	(5,847)
Intra-entity property acquisition	(976)	-
Payment on Advance from City - pension obligation	(163)	(139)
Net cash used by non-capital financing activities	(7,397)	(5,986)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Purchase of utility plant	(27,794)	(29,754)
Proceeds from the sale of utility plant	208	18,379
Principal paid on long-term obligations	(4,545)	(4,660)
Interest paid on long-term obligations	(9,273)	(9,268)
Bond issuance costs	-	(402)
Capital contributions	4,810	3,706
Net cash used by capital and related financing activities	(36,594)	(21,999)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from investment securities	149	6,998
Income from investments	1,583	2,385
Net cash provided by investing activities	1,732	9,383
Net (decrease) increase in cash and cash equivalents	(12,076)	8,230
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR **(including $68,532 and $87,736 at June 30, 2011 and June 30, 2010, respectively, reported in restricted accounts)**	125,336	117,106
CASH AND CASH EQUIVALENTS, END OF YEAR **(including $49,333 and $68,532 at June 30, 2012 and June 30, 2011, respectively, reported in restricted accounts)**	$ 113,260	$ 125,336
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	$ 17,001	$ 14,606
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	11,824	11,386
Amortization of deferred charges-pension costs	153	125
Decrease in allowance for uncollectible accounts	(150)	(57)
Increase in accounts receivable	(491)	(2,067)
(Increase) decrease in prepaid expenses	(21)	3
Increase in accounts payable and other accruals	432	1,496
Increase in postemployment benefits payable	422	341
Increase in Conservation & Reclamation Programs	49	26
Increase in customer deposits	46	63
Other receipts	918	910
Net cash provided by operating activities	$ 30,183	$ 26,832
SCHEDULE OF NON-CASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:		
Capital contributions - capital assets	548	626
Principal balance of revenue bonds refunded	-	59,000

See accompanying notes to the financial statements



NOTES TO THE FINANCIAL STATEMENTS: WATER

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Water Utility exists under, and by virtue of, the City of Riverside (the City) Charter enacted in 1883. The Water Utility is responsible for the production, transmission and distribution of water for sale in the City, except for certain areas served by another water utility. The accompanying financial statements present only the financial position and the results of operations of the Water Utility (the Utility), which is an enterprise fund of the City, and are not intended to present fairly the financial position and results of operations of the City in conformity with generally accepted accounting principles. However, certain disclosures are for the City as a whole, since such information is generally not available for the Utility on a separate fund basis. All amounts, unless otherwise indicated, are expressed in thousands of dollars.

BASIS OF ACCOUNTING

The Water Utility uses the accrual basis of accounting as required for enterprise funds with accounting principles generally accepted in the United States of America as applicable to governments. The accounting records of the Utility are also in conformity with the Uniform System of Accounts prescribed by the California Public Utilities Commission. The Utility is not subject to the regulations of the California Public Utilities Commission. The Utility is not required to and does not elect to implement the pronouncements of the Financial Accounting Standards Board issued after November 1989.

USE OF ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts of revenues and expenses during a reporting period. Actual results could differ from those estimates.

REVENUE RECOGNITION

The Water Utility customers are billed monthly. Unbilled water service charges including the Conservation and Reclamation Programs, are recorded at year-end and are included in accounts receivable. Unbilled accounts receivable totaled $3,475 at June 30, 2012, and $3,355 at June 30, 2011.

An allowance for doubtful accounts is maintained for utility and miscellaneous accounts receivable. The balance in this account is adjusted at fiscal year-end to approximate the amount anticipated to be uncollectible.

UTILITY PLANT AND DEPRECIATION

The Water Utility defines capital assets as assets with an initial, individual cost of more than five thousand dollars and an estimated useful life in excess of one year. Utility plant assets are valued at historical costs or estimated historical cost, if actual historical cost is not available. Costs include labor; materials; interest during construction; allocated indirect charges such as engineering, supervision, construction and transportation equipment; retirement plan contributions and other fringe benefits. Contributed plant assets are valued at estimated fair value on the date contributed. The cost of relatively minor replacements is included in maintenance expense. Intangible assets that cost more than one hundred thousand dollars with useful lives of at least three years are capitalized and are recorded at cost.

Depreciation is recorded over the estimated useful lives of the related assets using the straight-line method. The estimated useful lives are as follows:

Supply, pumping and treatment plant	15-60 years
Transmission and distribution plant	25-50 years
General plant and equipment	5-50 years
Intangibles	5 years

RESTRICTED ASSETS

Proceeds of revenue bonds yet to be used for capital projects, as well as certain resources set aside for debt service, are classified as restricted assets on the Balance Sheets because their use is limited by applicable bond covenants.

In June 2004, the Water Utility began collecting a surcharge for Conservation and Reclamation Programs. This surcharge was approved by the City Council and was phased in over a three-year period with a 0.5%, 1.0% and 1.5% surcharge effective June 1, 2004, 2005 and 2006, respectively, to be in effect for services rendered on or after June 1, 2004 through May 31, 2014. The programs and services offered include conservation, education, and water use efficiency programs; programs to encourage the use of reclaimed water; research, development and demonstration programs to advance science and technology with respect to water conservation and reclamation; and water service provided to low-income customers. The activity associated with the surcharge is reflected in the accompanying financial statements on the Balance Sheets, Statements of Revenues, Expenses and Changes in Equity, and Statements of Cash Flows.

CASH AND INVESTMENTS

In accordance with Water Utility policy, the Utility's cash and investments, except for cash and investments with fiscal agents, are invested in a pool managed by the Treasurer of the City. The Utility does not own specific, identifiable investments of the pool. The pooled interest earned is allocated monthly based on the month end cash balances.

The Utility values its cash and investments in accordance with provisions of Governmental Accounting Standards Board Statement No. 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools* (GASB 31), which requires governmental entities, including governmental external investment pools, to report certain investments, at fair value in the Statements of Net Assets/Balance Sheets and recognize the corresponding change in the fair value of investments in the year in which the change occurred. Fair value is determined using published market prices.

Cash accounts of all funds are pooled for investment purposes to enhance safety and liquidity while maximizing interest earnings. Investments are stated at fair value.

City-wide information concerning cash and investments for the year ended June 30, 2012, including authorized investments, custodial credit risk, credit and interest rate risk for debt securities and concentration of investments, carrying amount and market value of deposits and investments may be found in the notes to the City's "Comprehensive Annual Financial Report."

CASH AND INVESTMENTS AT FISCAL AGENTS

Cash and investments maintained by fiscal agents are considered restricted by the Water Utility and are pledged as collateral for payment of principal and interest on outstanding bonds, or for use on construction of capital assets.

DERIVATIVES

On July 1, 2009, the Water Utility adopted GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments* (GASB 53). This Statement requires the Utility to report its derivative instruments at fair value. Changes in fair value for effective hedges are to be reported as deferrals on the Balance Sheets. Changes in fair value of derivative instruments not meeting the criteria for an effective hedge, or that are associated with investments are to be reported in the investment section of the Statements of Revenues, Expenses and Changes in Equity.

The Utility has determined that its interest rate swaps associated with variable rate obligations are derivative instruments under GASB 53. See Note 4 Long-Term Obligations for further discussion related to the Utility's interest rate swaps.

BOND PREMIUM/DISCOUNTS, ISSUANCE COSTS, GAINS AND LOSSES ON REFUNDING

Bond premium/discounts, issuance costs and gains and losses on refunding (including gains and losses related to interest rate swap transactions) are deferred and amortized over the term of the bonds using the effective interest method. Bond premium/discounts, and gains and losses on refunding are presented as a reduction of the face amount of bonds payable, whereas issuance costs are recorded as other assets.

CUSTOMER DEPOSITS

The City holds customer deposits as security for the payment of utility bills and plan check fee deposits for future water connection. The Water Utility's portion of these deposits as of June 30, 2012 and 2011 was $724 and $678, respectively (including $77 and $115, respectively, held on behalf of La Sierra Water Company pending dissolution and distribution of remaining cash asset to shareholders, of which the Utility is the largest owner).

COMPENSATED ABSENCES

The accompanying financial statements include accruals for salaries, fringe benefits and compensated absences due to employees at June 30, 2012 and 2011. The Water Utility including the Conservation and Reclamation Programs, treats compensated absences due to employees as an expense and a current liability and is included in accounts payable and other accruals in the accompanying Balance Sheets. The amount accrued for compensated absences was $1,428 at June 30, 2012, and $1,429 at June 30, 2011.

Employees receive 10 to 25 vacation days per year based upon length of service. A maximum of two years vacation accrual may be accumulated and unused vacation is paid in cash upon separation.

Employees primarily receive one day of sick leave for each month of employment with unlimited accumulation. Upon retirement or death, certain employees or their estates receive a percentage of unused sick leave paid in a lump sum based on longevity.

INSURANCE PROGRAMS

The Water Utility participates in a self-insurance program for workers' compensation and general liability coverage that is administered by the City. The Utility pays an amount to the City based on actuarial estimates of the amounts needed to fund prior and current year claims and incidents that have been incurred but not reported. The City maintains property insurance on most City property holdings, including the Utility plant with a limit of $1 billion.

City-wide information concerning risks, insurance policy limits and deductibles and designation of general fund balance for risks for the year ended June 30, 2012, may be found in the notes to the City's "Comprehensive Annual Financial Report."

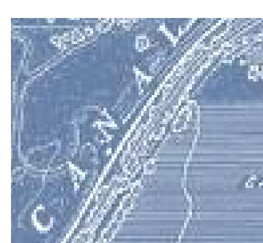
Although the ultimate amount of losses incurred through June 30, 2012 is dependent upon future developments, management believes that amounts paid to the City are sufficient to cover such losses. Premiums paid to the City by the Water Utility including the Conservation and Reclamation Programs, were $662 and $620 for the years ended June 30, 2012 and 2011, respectively. Any losses above the City's reserves would be covered through increased rates charged to the Utility in future years.

EMPLOYEE RETIREMENT PLAN

The City contributes to the California Public Employees Retirement System (PERS), a public employee retirement system that services more than 3,000 public agency employers within the State of California and acts as a common investment and administrative agency for those participating public entities.

All permanent full-time and selected part-time employees are eligible for participation in PERS. Benefits vest after five years of service and are determined by a formula that considers the employee's age, years of service and salary. Employees may retire at age 55 and receive 2.7 percent of their highest annual salary for each year of service completed. For new employees hired after December 9, 2011, all bargaining units including management, SEIU, and IBEW, agreed to change the calculation from utilizing the highest year of salary to the average of the highest three years of salary. PERS also provides death and disability benefits. These benefit provisions and all other requirements are established by state statute and City ordinance.

Employee contributions are 8.0 percent of their annual covered salary. The Utility pays both the employee and employer contributions except for new employees hired after October 19, 2011, who pay their own 8.0 percent contribution. The Water Utility is required to contribute the remaining amounts necessary to fund the benefits for its employees using the actuarial basis recommended by the PERS actuaries and actuarial consultants and adopted by the PERS Board of Administration. The total Water Utility's contribution to PERS



including the Conservation and Reclamation Programs as of June 30, 2012 and 2011 was $3,095 and $2,603, respectively. The employer portion of PERS funding as of June 30, 2012 and 2011 was 18.44 percent and 14.51 percent, respectively, of annual covered payroll.

City-wide information concerning elements of the unfunded actuarial accrued liabilities, contributions to PERS for the fiscal year ended June 30, 2012, and recent trend information may be found in the notes to the City's "Comprehensive Annual Financial Report" for the fiscal year ended June 30, 2012.

PENSION OBLIGATION BONDS

In 2005, the City issued Pension Obligation Bonds in the amount of $60,000, of which the Water Utility's share is $5,890. The deferred charge relating to the net pension asset will be amortized over 19 years in accordance with the method used by PERS for calculating actuarial gains and losses. The Bond proceeds were deposited with PERS to fund the unfunded actuarial accrued liability for non-safety employees. The balance in deferred pension costs as of June 30, 2012 and 2011 was $5,327 and $5,480, respectively. For more discussion relating to the City's issue, see the notes to the City's "Comprehensive Annual Financial Report" for the fiscal year ended June 30, 2012.

OTHER POSTEMPLOYMENT BENEFITS

The City contributes to two single-employer defined benefit healthcare plans: Stipend Plan (SP) and the Implied Subsidy Plan (ISP). The plans provide other postemployment health care benefits (OPEB) for eligible retirees and beneficiaries.

The Stipend Plan is available to eligible retirees and beneficiaries pursuant to their collective bargaining agreements. The Water Utility currently contributes to a bargaining unit through the Service Employee's International Union General Trust (SEIUG). Benefit provisions for the Stipend Plan for eligible retirees and beneficiaries are established and amended through the various memoranda of understanding (MOU). The MOU's are agreements established between the City and the respective employee associations. The City does not issue separate stand-alone financial reports for the plans, instead financial information for the trust funds can be obtained by contacting the individual association.

The Utility also provides benefits to retirees in the form of an implicit rate subsidy (Implied Subsidy). Under an implied rate subsidy, retirees and current employees are insured together as a group, thus creating a lower rate for retirees than if they were insured separately. Although the retirees are solely responsible for the cost of their health insurance benefits through this plan, the retirees are receiving the benefit of a lower rate.

The contribution requirements of the Utility for the Stipend Plan are established and may be amended through the MOU between the City and the unions. The Utility's contribution is financed on a "pay-as-you-go-basis" and the current contribution is unfunded. The contribution requirements of the Utility's Implied Subsidy Plan are established by the City Council. The Utility is not required by law or contractual agreement to provide funding other than the pay-as-you-go amount necessary to provide current benefits to eligible retirees and beneficiaries.

The Utility's annual OPEB cost (expense) for each plan is calculated based on annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* (GASB 45). The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) (UAAL) over a period not to exceed thirty years. The Water Utility's OPEB liability including the Conservation and Reclamation Programs as of June 30, 2012 and 2011 was $1,656 and $1,228, respectively.

City-wide information concerning the description of the plans, funding policy and annual OPEB cost, funding status and funding progress, and actuarial methods and assumptions for the year ended June 30, 2012 can be found in the notes to the City's "Comprehensive Annual Financial Report" for the fiscal year ended June 30, 2012.

EQUITY

The Water Utility's equity consists of its net assets (assets less liabilities) which are classified into the following three components:

Invested in capital assets, net of related debt – this component consists of capital assets (net of accumulated depreciation) and unamortized debt expenses reduced by the outstanding balance of any bonds or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

Restricted – this component consists of net assets on which constraints are placed as to their use. Constraints include those imposed by creditors (such as through debt covenants), contributors, or laws or regulation of other governments or constraints imposed by law through constitutional provisions or through enabling legislation.

Unrestricted – this component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

CONTRIBUTIONS TO THE CITY'S GENERAL FUND

Pursuant to the City of Riverside Charter, the Water Utility may transfer up to 11.5 percent of prior year's gross operating revenues including adjustments to the City's general fund. In fiscal years ended June 30, 2012 and 2011, $6,258 and $5,847, respectively was transferred representing 11.5 percent.

CASH AND CASH EQUIVALENTS

For the Statements of Cash Flows, cash and cash equivalents include all unrestricted and restricted highly liquid investments with original purchase maturities of three months or less, and all bond construction proceeds available for capital projects. Pooled cash and investments in the City's Treasury represent monies in a cash management pool. Such accounts are similar in nature to demand deposits, and are classified as cash equivalents for the purpose of presentation in the Statements of Cash Flows.

BUDGETS AND BUDGETARY ACCOUNTING

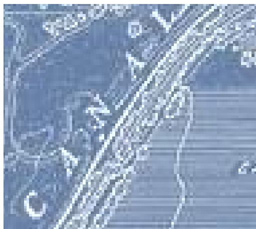
The Water Utility presents, and the City Council adopts, an annual budget. The proposed budget includes estimated expenses and forecasted revenues. The City Council adopts the Utility's budget in June each year via resolution.

RECLASSIFICATIONS

Certain reclassifications have been made to prior year's financial statements to conform with the current year's presentation.

PRIOR YEAR DATA

Selected information regarding the prior year has been included in the accompanying financial statements. This information has been included for comparison purposes only and does not represent a complete presentation in accordance with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Water Utility's prior year financial statements, from which this selected financial data was derived.



NOTE 2. CASH AND INVESTMENTS

Cash and investments at June 30, 2012 and 2011, consist of the following (in thousands):

	June 30, 2012	June 30, 2011
	Fair Value	
Equity interest in City Treasurer's investment pool	$ 71,985	$ 64,733
Cash and investments at fiscal agent	41,287	60,764
	113,272	125,497
Certificate of Deposit with financial institutions at fiscal agent[3]	523	523
Total cash and investments	$ 113,795	$ 126,020

The amounts above are reflected in the accompanying financial statements as:

	June 30, 2012	June 30, 2011
Unrestricted cash and cash equivalents	$ 63,927	$ 56,804
Restricted cash and cash equivalents	8,058	7,929
Restricted cash and investments at fiscal agent	41,810	61,287
Total cash and investments	$ 113,795	$ 126,020

Cash and investments distribution by maturities as of year end are as follows:

		Remaining Maturity (In Months)		
Investment Type	**Total**	**12 Months or less**	**13 to 24 Months**	**25 to 60 Months**
Held by fiscal agent				
Money market funds	$ 12	$ 12	$ -	$ -
Investment contracts [1]	41,275	41,275	-	-
City Treasurer's investment pool [2]				
Money market funds	12,334	12,334	-	-
Federal agency securities	32,019	3,895	7,371	20,753
Corp medium term notes	9,877	1,672	3,429	4,776
State investment pool	16,454	16,454	-	-
Negotiable Certificate of Deposit	1,301	41	814	446
Total [3]	$ 113,272	$ 75,683	$ 11,614	$ 25,975

Presented below is the actual rating as of year end for each investment type:

		Rating as of Year End			
Investment Type	**Total**	**AAA**	**AA**	**A**	**Unrated**
Held by fiscal agent					
Money market funds	$ 12	$ 12	$ -	$ -	$ -
Investment contracts [1]	41,275	-	-	-	41,275
City Treasurer's investment pool [2]					
Money market funds	12,334	300	7,141	4,893	-
Federal agency securities	32,019	32,019	-	-	-
Corp medium term notes	9,877	-	8,107	1,770	-
State investment pool	16,454	-	-	-	16,454
Negotiable Certificate of Deposit	1,301	-	-	-	1,301
Total [3]	$ 113,272	$ 32,331	$ 15,248	$ 6,663	$ 59,030

1 Amounts related to bond construction proceeds are invested in specific maturities but are available for construction of capital assets as funding is needed.

2 Additional information on investment types and credit risk may be found in the City's "Comprehensive Annual Financial Report."

3 $523 in Certificates of Deposits is not considered an investment under GASB Statement No. 40, *Deposit and Investment Risk Disclosures,* and is excluded above from the Investment Type presentation above.

NOTE 3. UTILITY PLANT

The following is a summary of changes in utility plant during the fiscal years ended June 30, 2012 and 2011 (in thousands):

	Balance As of 6/30/10	Additions	Retirements /Transfers	Balance As of 6/30/11	Additions	Retirements /Transfers	Balance As of 6/30/12
Source of supply	$ 45,465	$ 987	$ -	$ 46,452	$ 1,852	$ -	$ 48,304
Pumping	24,673	891	-	25,564	1,305	-	26,869
Treatment	41,165	35	-	41,200	2,497	-	43,697
Transmission and distribution	356,201	18,669	(906)	373,964	37,089	(2,392)	408,661
General	14,080	792	(507)	14,365	38	(362)	14,041
Intangible	137	-	-	137	216	-	353
Depreciable utility plant	481,721	21,374	(1,413)	501,682	42,997	(2,754)	541,925
Less accumulated depreciation							
Source of supply	(12,250)	(1,247)	-	(13,497)	(919)	-	(14,416)
Pumping	(7,788)	(601)	-	(8,389)	(609)	-	(8,998)
Treatment	(5,426)	(776)	-	(6,202)	(1,140)	-	(7,342)
Transmission and distribution	(107,207)	(7,529)	906	(113,830)	(7,938)	2,392	(119,376)
General	(8,359)	(1,232)	492	(9,099)	(1,214)	341	(9,972)
Intangible	(137)	-	-	(137)	(4)	-	(141)
Accumulated depreciation	(141,167)	(11,385)	1,398	(151,154)	(11,824)	2,733	(160,245)
Net depreciable utility plant	340,554	9,989	(15)	350,528	31,173	(21)	381,680
Land	10,809	95	(43)	10,861	135	-	10,996
Intangible	6,307	-	-	6,307	-	-	6,307
Construction in progress	15,122	30,068	(20,622)	24,568	29,368	(43,244)	10,692
Nondepreciable utility plant	32,238	30,163	(20,665)	41,736	29,503	(43,244)	27,995
Total utility plant	$ 372,792	$ 40,152	$ (20,680)	$ 392,264	$ 60,676	$ (43,265)	$ 409,675

NOTE 4. LONG-TERM OBLIGATIONS

The following is a summary of changes in long-term obligations during the fiscal years ended June 30, 2012 and 2011 (in thousands):

	Balance As of 6/30/2010	Additions	Reductions	Balance As of 6/30/2011	Additions	Reductions	Balance As of 6/30/2012	Due Within One Year
Revenue bonds	$ 223,275	$ 50,010	$ (60,425)	$ 212,860	$ -	$ (4,436)	$ 208,424	$ 4,695
Advance from City - pension obligation	5,466	-	(139)	5,327	-	(163)	5,164	
Postemployment benefits payable	881	341	-	1,222	422	-	1,644	
Water stock acquisition rights	949	-	(2)	947	-	-	947	150
Total long-term obligations	$ 230,571	$ 50,351	$ (60,566)	$ 220,356	$ 422	$ (4,599)	$ 216,179	$ 4,845

Long-term debt consists of the following (in thousands):

CONTRACTS PAYABLE	June 30, 2012	June 30, 2011
Water Stock Acquisitions: Payable on demand to various water companies	$ 947	$ 947
Total contracts payable	947	947
REVENUE BONDS PAYABLE		
$20,000 2001 Water Revenue Bonds: serial bonds due in annual installments from $490 to $510 through October 1, 2013, interest from 4.3 percent to 4.4 percent (partially advance refunded in 2005 and 2009 with final maturity in 2013)	1,000	1,470
$58,235 2008 Water Revenue Series B Bonds: fixed rate bonds due in annual installments from $1,210 to $7,505 from October 1, 2016 through October 1, 2038, interest from 4.0 percent to 5.0 percent	58,235	58,235
$31,895 2009 Water Refunding/Revenue Series A Bonds: fixed rate bonds due in annual installments from $2,270 to $4,335 through October 1, 2020, interest from 3.0 percent to 5.0 percent	28,095	31,370
$67,790 2009 Water Revenue Series B Bonds: fixed rate, federally taxable, Build America Bonds due in annual installments from $2,475 to $4,985 from October 1, 2021 through October 1, 2039, interest from 3.3 percent to 4.1 percent	67,790	67,790
$59,000 2011 Water Revenue/Refunding Series A Bonds: variable rate bonds due in annual installments from $600 to $3,950 through October 1, 2035. Interest rate is subject to weekly repricing (net interest rate, including swaps, at June 27, 2012 was 3.2 percent)	58,200	59,000
Total water revenue bonds payable	213,320	217,865
Total water revenue bonds and contracts payable	214,267	218,812
Unamortized deferred bond refunding costs	(9,237)	(9,802)
Unamortized bond premium	4,341	4,797
Total water revenue bonds and contracts payable, net of deferred bond refunding costs and bond premium	209,371	213,807
Less current portion	(4,845)	(4,695)
Total long-term water revenue bonds and contracts payable	$ 204,526	$ 209,112

Revenue Bonds annual debt service requirements, including contracts payable, to maturity, as of June 30, 2012, are as follows (in thousands):

	2013	2014	2015	2016	2017	2018-22	2023-27	2028-32	2033-37	2038-40	Total
Principal	$ 4,845	$ 5,020	$ 5,165	$ 5,410	$ 5,330	$ 29,512	$ 35,270	$ 42,730	$ 51,960	$ 29,025	$ 214,267
Interest	8,678	8,487	8,276	8,046	7,814	35,597	29,439	21,747	12,229	1,647	141,960
Total	$ 13,523	$ 13,507	$ 13,441	$ 13,456	$ 13,144	$ 65,109	$ 64,709	$ 64,477	$ 64,189	$ 30,672	$ 356,227

The Water Utility's bond indentures require the Utility to maintain a minimum debt service coverage ratio, as defined by the bond covenants of 1.25. The Water Utility's debt service coverage ratio was 2.82 and 3.49 at June 30, 2012 and 2011, respectively. The debt (revenue bonds) is backed by the revenues of the Utility.

NOTE 4. LONG-TERM OBLIGATIONS (CONTINUED)

PRIOR YEAR DEFEASANCE OF DEBT

In prior years, the Water Utility defeased certain Revenue Bonds by placing the proceeds of the new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Utility's financial statements. At fiscal year ended June 30, 2012, no bonds outstanding were considered defeased.

2011 WATER REFUNDING/REVENUE BONDS

In May 2008, the Water Utility refinanced $60,300 of Auction Rate Securities (ARS) with Variable Rate Demand Notes (VRDNs). The VRDNs require credit enhancements (e.g. insurance or a bank letter of credit) to ensure debt service payments to bondholders are made should the Utility fail to make payment. Bank of America/Merrill Lynch (BAML) provided the Letter of Credit (LOC) at attractive rates. The LOC with BAML expired in May 2011. Renewing the existing LOC with BAML would result in higher rates due to a limited number of highly-rated banks offering this service. To mitigate various risk exposure and to provide an overall lower cost of financing, the Utility restructured the 2008 VRDN by refunding the 2008 VRDN with the 2011 VRDN.

On May 26, 2011, $59,000 of Water Refunding/Revenue Series A Bonds were sold with an all-in true interest cost of 3.33% to refund $59,000 of previously outstanding 2008 Water Refunding/Revenue Bonds. The refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $434. The difference is being charged to operations using the proportional method. Principal payments are due on October 1, 2011 until the maturity date of October 1, 2035 ranging from $600 to $3,950.

INTEREST RATE SWAPS ON REVENUE BONDS

The Water Utility has one cash flow hedging derivative instrument, which is a pay-fixed swap. The swap was employed as a hedge against debt that was refunded in 2008 and 2011. At the time of the refunding, hedge accounting ceased to be applied. The balance of the deferral account for the swap is included in the net carrying amount of the new bonds. The swap was also employed as a hedge against the new debt. Hedge accounting was applied to that portion of the hedging relationship, which was determined to be effective.

A summary of the derivative activity for the year ended June 30, 2012 is as follows:

	Notional Amount	Fair Value as of 6/30/2012	Change in Fair Value for Fiscal Year
2011 Water Refunding/Revenue Bonds Series A	$ 59,000	$ (12,768)	$ (7,320)

Objective: In order to lower borrowing costs as compared to fixed-rate bonds, the Utility entered into an interest rate swap agreement in connection with its $59,000 2011 Water Refunding/Revenue Series A Bonds.

Terms: Per the existing swap agreement, the Utility pays the counterparty a fixed payment as noted above and receives a variable payment computed as 62.68% of the London Interbank Offering Rate ("LIBOR") one month index plus 12 basis points. The swap has a notional amount equal to the principal amount stated above. The notional value of the swap and principal amount of the associated debt decline by $600 to $3,950 until the debt is completely retired in fiscal year 2036.

The bonds and the related swap agreement for the 2011 Water Refunding/Revenue Series A Bonds mature on October 1, 2035. As of June 30, 2012, rates were as follows:

Interest rate swap:	Terms	Rates
Fixed payment to counterparty	Fixed	3.20000%
Variable payment from counterparty	62.68 LIBOR + 12bps	(0.26684%)
Net interest rate swap payments		2.93316%
Variable-rate bond coupon payments		0.21969%
Synthetic interest on bonds		3.15285%

Fair value: As of June 30, 2012, in connection with the swap agreement, the transactions had a total negative fair value of ($12,768). Because the coupons on the Utility's variable-rate bonds adjust to changing interest rates, the bonds do not have a corresponding fair value decrease. The fair value was developed by a pricing service using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement of the swap.

Credit risk: As of June 30, 2012, the Utility was not exposed to credit risk because the swap had a negative fair value. The swap counterparty, J.P. Morgan Chase & Co. was rated A by Standard & Poor's. To mitigate the potential for credit risk, the swap agreement requires the fair value of the swap to be collateralized by the counterparty with U.S. Government securities if the counterparty's rating decreases to negotiated trigger points. Collateral would be posted with a third-party custodian. At June 30, 2012, there is no requirement for collateral posting for the outstanding swap.

Basis risk: As noted above, the swap exposes the Utility to basis risk should the relationship between LIBOR and the variable rates converge, changing the synthetic rate on the bonds. If a change occurs that results in the rates moving to convergence, the expected cost savings may not be realized.

Termination risk: The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. The Schedule to the Master Agreement includes an "additional termination event." That is, a swap may be terminated by the Utility if the counterparty's credit quality falls below "BBB-" as issued by Standards & Poor's. The Utility or the counterparty may terminate a swap if the other party fails to perform under the terms of the contract. If a swap is terminated, the variable-rate bond would no longer carry a synthetic interest rate. Also, if at the time of termination a swap has a negative fair value, the Utility would be liable to the counterparty for a payment equal to the swap's fair value.

Swap payments and associated debt: As of June 30, 2012, the debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same for their term, are summarized as follows. As rates vary, variable-rate bond interest payments and net swap payments will vary.

	Variable-Rate Bonds			
Fiscal Year Ending June 30,	**Principal**	**Interest**	**Interest Rate Swaps, Net**	**Total**
2013	$ 825	$ 126	$ 1,683	$ 2,634
2014	850	124	1,658	2,632
2015	875	122	1,632	2,629
2016	925	120	1,605	2,650
2017	600	119	1,588	2,307
2018-2022	10,550	531	7,087	18,168
2023-2027	14,025	388	5,185	19,598
2028-2032	15,700	225	3,007	18,932
2033-2036	13,850	51	680	14,581
Total	$ 58,200	$ 1,806	$ 24,125	$ 84,131

NOTE 5. RESTRICTED EQUITY

Pursuant to applicable bond indentures, a reserve for debt service has been established by restricting assets and reserving a portion of equity. Bond indentures for the Utility's water revenue and refunding bonds require debt service reserves that equate to the maximum annual debt service required in future years and bond service reserves of three months interest and nine months principal due in the next fiscal year. Variable rate revenue and refunding bonds require 110% of the monthly accrued interest to be included in the reserve. Active water revenue bonds requiring reserves is issue 2001. Certain revenue/refunding bond issues are covered by a Surety Bond (2008B) and certain issues have no debt service reserve requirements (2009A & B and 2011A).

NOTE 6. LITIGATION

The Water Utility is a defendant in various lawsuits arising in the normal course of business. Present lawsuits and other claims against the Utility are incidental to the ordinary course of operations of the Utility and are largely covered by the City's self-insurance program. In the opinion of management and the City Attorney, such claims and litigation will not have a materially adverse effect upon the financial position or results of operations of the Utility.

The Utility is a plaintiff in a lawsuit against several entities that either owned or leased a property site in the City of Colton and City of Rialto that is contaminated by perchlorate. The lawsuit was filed March 31, 2009, and no trial date has been set.

NOTE 7. CONSTRUCTION COMMITMENTS

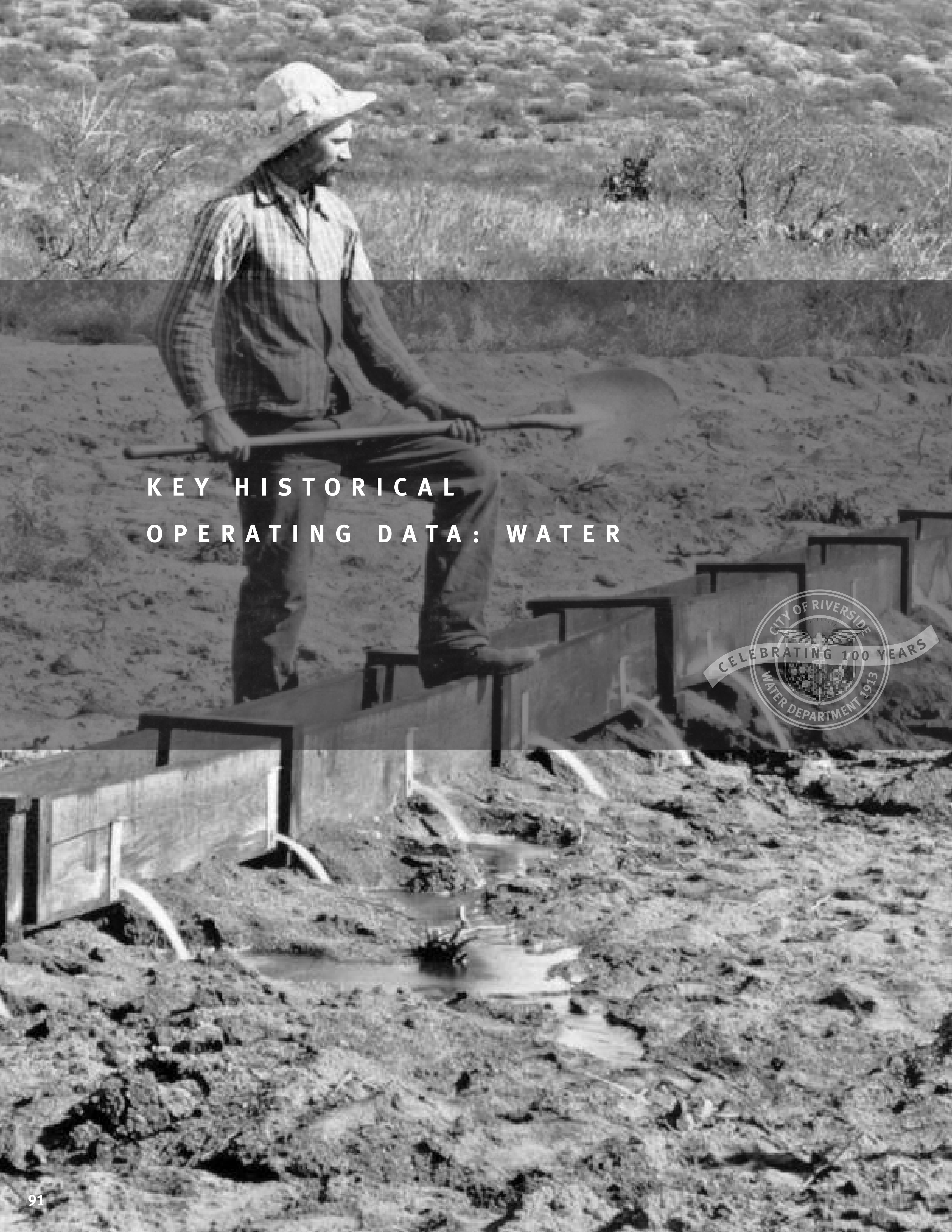
As of June 30, 2012, the Water Utility had major commitments (encumbrances) of approximately $8,550 with respect to unfinished capital projects of which $4,678 is expected to be funded by bonds and $3,872 to be funded by other sources.

NOTE 8. SPECIAL ITEM

On January 4, 2011 and March 1, 2011, City Council approved the sale of the 56-acre AB Brown Sports Complex and a certain property (Reid Park land and a 64 acre portion of the former Riverside Golf Course) from the Water Utility to the Electric Utility. The properties were sold for a fair market value of $11,600 (AB Brown Sports Complex) and $5,558 ($720 Reid Park and $4,838 Riverside Golf Course), respectively. The original and carrying value of the properties was $17 and $27, respectively. The balance between the sales price and carrying value of $11,583 and $5,531, respectively, was recorded as a special item in fiscal year ended June 30, 2011.

RiversidePublicUtilities.com

KEY HISTORICAL OPERATING DATA: WATER



KEY HISTORICAL OPERATING DATA

WATER SUPPLY (ACRE FEET)

	2011/12	2010/11	2009/10	2008/09	2007/08
Pumping	69,564	66,492	69,676	76,830	80,974
Purchases	0	0	0	0	1,643
Total:	69,564	66,492	69,676	76,830	82,617
Percentage pumped	100.00%	100.00%	100.00%	100.00%	98.0%
System peak day (gallons)	88,370,000	90,556,000	98,017,000	105,780,000	111,300,000

WATER USE

	2011/12	2010/11	2009/10	2008/09	2007/08
Number of meters as of year end					
Residential	58,506	58,460	58,372	58,152	57,694
Commercial/Industrial	5,504	5,482	5,451	5,519	5,446
Other	357	407	408	391	354
Total:	64,367	64,349	64,231	64,062	63,494
*CCF sales					
Residential	16,288,918	15,698,321	16,321,425	17,898,798	18,483,522
Commercial/Industrial	9,703,162	9,219,913	9,344,085	10,342,284	10,510,953
Other	893,971	826,165	871,396	983,553	970,239
Subtotal:	26,886,051	25,744,399	26,536,906	29,224,635	29,964,714
Wholesale	176,091	158,040	150,365	496,601	618,552
Total:	27,062,142	25,902,439	26,687,271	29,721,236	30,583,266

*(CCF equals 100 cubic feet)

WATER FACTS

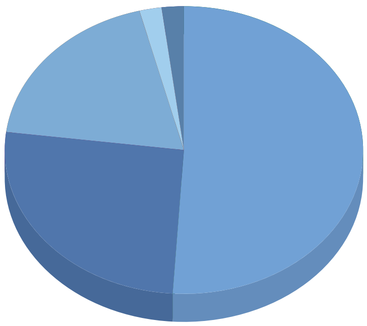
	2011/12	2010/11	2009/10	2008/09	2007/08
Average annual CCF per residential customer	278	269	280	308	320
Average price ($/CCF) per residential customer	$2.37	$2.28	$2.05	$1.81	$1.63
Debt service coverage ratio (DSC)[2]	2.82	3.49	2.08	2.25	3.88
Employees[1]	181	180	178	167	167

[1] Approved positions

[2] For FY 09/10 and thereafter, interest expense used to calculate DSC is net of federal subsidy on Build America Bonds.

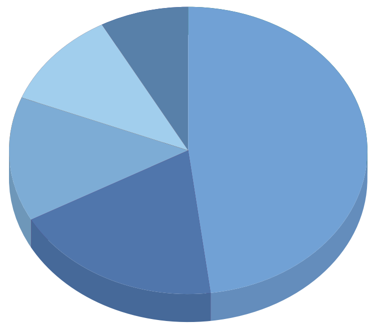
2011/2012 WATER REVENUE AND RESOURCES

Source of Revenue



- Residential Sales 51¢
- Commercial Sales 26¢
- Other Revenues 19¢
- Investment Income 2¢
- Other Sales 2¢

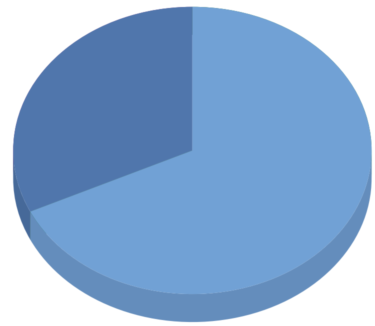
Distribution of Revenue



- Operations and Maintenance 48¢
- Debt Service 19¢
- Additional Reserves 14¢
- Additions and Replacements to the System 11¢
- Transfers to the City's General Fund* 8¢

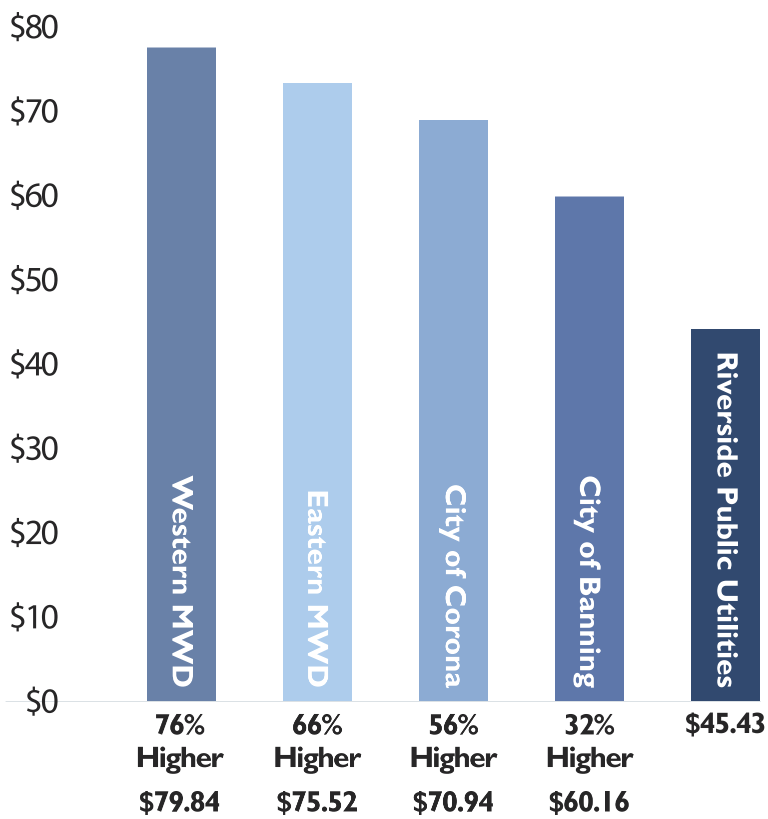
** Based on transfer of 11.5% of fiscal year 2010/2011 operating revenues (excludes wholesale sales and Conservation and Reclamation revenue)*

Water Resources



- San Bernardino Basin Wells 68%
- Riverside Basin Wells 32%
- Purchased Water 0%

RESIDENTIAL WATER RATE COMPARISON – 23 CCF PER MONTH (AS OF JUNE 30, 2012)

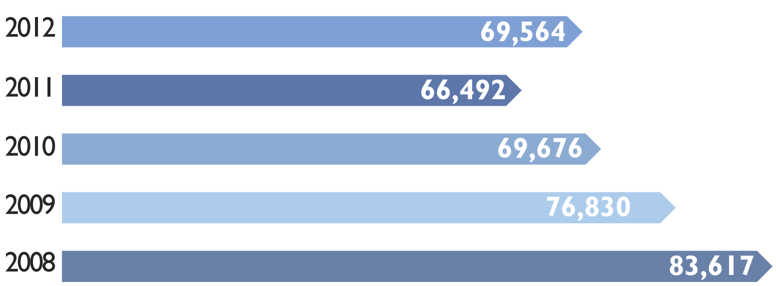


GENERAL FUND TRANSFER (IN MILLIONS)

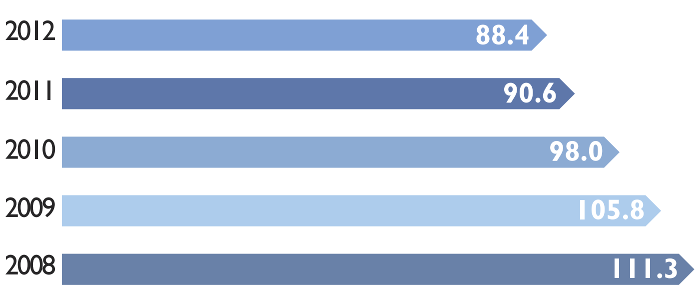
NUMBER OF METERS AT YEAR END

TOTAL OPERATING REVENUE (IN MILLIONS)

PRODUCTION (IN ACRE FEET)



PEAK DAY DEMAND (IN MILLION GALLONS)



WATER FACTS AND SYSTEM DATA

Established	1913
Service Area Population	308,452
Service Area Size (square miles)	74.40
System Data:	
Smallest pipeline	2.0”
Largest pipeline	72.0”
Miles of pipeline	1,000
Number of domestic wells	53
Number of active reservoirs	16
Total reservoir capacity (gallons)	108,500,000
Number of treatment plants	6
Number of treatment vessels	84
Miles of canal	14
Number of fire hydrants	7,682
Daily average production (gallons)	60,014,625
2011-2012 Peak day (gallons)	88,370,000
07/07/11, 101 degrees	
Historical peak (gallons)	118,782,000
08/09/05, 99 degrees	

Bond Ratings

Fitch Ratings	AA+
Moody’s	Aa2
Standard & Poor’s	AAA