

SUNSET BEACH SANITARY DISTRICT
BASIC FINANCIAL STATEMENTS
WITH REPORT ON AUDIT BY INDEPENDENT
CERTIFIED PUBLIC ACCOUNTANTS
JUNE 30, 2016

SUNSET BEACH SANITARY DISTRICT

TABLE OF CONTENTS

June 30, 2016

	<u>Page Number</u>
Independent Auditors' Report	1 - 2
Basic Financial Statements:	
Governmental Fund Balance Sheet and Statement of Net Position	3
Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balance and Statement of Activities	4
Statement of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual - General Fund	5
Notes to Basic Financial Statements	6 - 19

INDEPENDENT AUDITORS' REPORT

Board of Directors
Sunset Beach Sanitary District
Sunset Beach, California

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activity and general fund of the Sunset Beach Sanitary District (the District) as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express opinions 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 from material misstatement.

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

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

Opinions

In our opinions, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activity and general fund of the District as of June 30, 2016, and the respective changes in financial position and the budgetary comparison for the general fund for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Required Supplementary Information

Management has omitted the Management's Discussion and Analysis information that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing 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. Our opinions on the basic financial statements are not affected by this missing information.

White Nelson Dick Evans LLP

Irvine, California
November 9, 2017

BASIC FINANCIAL STATEMENTS

SUNSET BEACH SANITARY DISTRICT
GOVERNMENTAL FUND BALANCE SHEET
AND STATEMENT OF NET POSITION

June 30, 2016

	General Fund	Adjustments	Statement of Net Position
ASSETS			
CURRENT ASSETS:			
Cash and investments	\$ 1,036,904	\$ -	\$ 1,036,904
Property taxes receivable, net	20,024	-	20,024
Interest receivable	316	-	316
Prepaid items	24,786	-	24,786
TOTAL CURRENT ASSETS	1,082,030	-	1,082,030
CAPITAL ASSETS:			
Sewer transmission and treatment capacity rights	-	1,754,389	1,754,389
Construction in progress	-	80,573	80,573
Property, plant and equipment, net of \$1,018,309 accumulated depreciation	-	1,786,494	1,786,494
TOTAL CAPITAL ASSETS	-	3,621,456	3,621,456
TOTAL ASSETS	\$ 1,082,030	\$ 3,621,456	4,703,486
LIABILITIES AND FUND BALANCE/NET POSITION			
CURRENT LIABILITIES:			
Accounts payable	\$ 300,342	\$ -	300,342
Wages payable	8,997	-	8,997
Due to other governmental agencies	608	-	608
TOTAL CURRENT LIABILITIES	309,947	-	309,947
TOTAL LIABILITIES	309,947	-	309,947
FUND BALANCE/NET POSITION:			
Fund balance:			
Nonspendable:			
Prepaid items	24,786	(24,786)	
Assigned:			
Capital improvements	50,000	(50,000)	
Unassigned	697,297	(697,297)	
TOTAL FUND BALANCE	772,083	(772,083)	
Net position:			
Net investment in capital assets		3,621,456	3,621,456
Unrestricted		772,083	772,083
TOTAL NET POSITION		4,393,539	\$ 4,393,539
TOTAL LIABILITIES AND FUND BALANCE	\$ 1,082,030	\$ 3,621,456	

See accompanying notes to basic financial statements.

SUNSET BEACH SANITARY DISTRICT

GOVERNMENTAL FUND STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCE
AND STATEMENT OF ACTIVITIES

For the year ended June 30, 2016

	General Fund	Adjustments	Statement of Activities
EXPENDITURES / PROGRAM EXPENSES:			
Sanitation services:			
Salaries and employee benefits	\$ 130,187	\$ -	\$ 130,187
Equipment and facilities, maintenance and repair	229,682	(123,383)	106,299
Memberships	6,735	-	6,735
Office expense	1,675	-	1,675
Professional and specialized services	53,972	(4,311)	49,661
Publication of legal notice	300	-	300
Refuse disposal	239,804	-	239,804
Rents and leases	12,089	-	12,089
Engineering and construction	125,567	(111,142)	14,425
Principal paid on liability due to City of Huntington Beach	80,000	(80,000)	-
Telephone	2,893	-	2,893
Transportation and travel	6,941	-	6,941
Utilities	280,709	-	280,709
Depreciation	-	183,867	183,867
TOTAL EXPENDITURES / PROGRAM EXPENSES	1,170,554	(134,969)	1,035,585
PROGRAM REVENUES:			
Sanitation services	438,396	-	438,396
NET PROGRAM ACTIVITY	(732,158)	134,969	(597,189)
GENERAL REVENUES:			
Property taxes	658,282	-	658,282
Penalties and costs	103	-	103
Interest earned	5,424	-	5,424
Other	1,738	-	1,738
TOTAL GENERAL REVENUES	665,547	-	665,547
CHANGE IN FUND BALANCE / NET POSITION	(66,611)	134,969	68,358
FUND BALANCE, AS RESTATED - JULY 1, 2015	838,694		
FUND BALANCE - JUNE 30, 2016	\$ 772,083		
CHANGE IN NET POSITION		\$ 134,969	68,358
NET POSITION, AS RESTATED - JULY 1, 2015			4,325,181
NET POSITION - JUNE 30, 2016			\$ 4,393,539

See accompanying notes to basic financial statements.

SUNSET BEACH SANITARY DISTRICT

STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCE - BUDGET AND ACTUAL -
GENERAL FUND

For the year ended June 30, 2016

	Budgeted Amounts		Actual	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES:				
Sanitation services	\$ 455,000	\$ 455,000	\$ 438,396	\$ (16,604)
Property taxes	569,350	569,350	658,282	88,932
Penalties and costs	-	-	103	103
Interest earned	2,500	2,500	5,424	2,924
Other	-	-	1,738	1,738
TOTAL REVENUES	<u>1,026,850</u>	<u>1,026,850</u>	<u>1,103,943</u>	<u>77,093</u>
EXPENDITURES:				
Salaries and employee benefits	127,115	127,115	130,187	(3,072)
Equipment and facilities, maintenance and repair	282,000	282,000	229,682	52,318
Insurance	8,050	8,050	-	8,050
Miscellaneous	7,300	7,300	6,735	565
Office expense	500	500	1,675	(1,175)
Professional and specialized services	49,600	49,600	53,972	(4,372)
Publication of legal notice	1,000	1,000	300	700
Refuse disposal	262,375	262,375	239,804	22,571
Rents and leases	12,125	12,125	12,089	36
Telephone	3,260	3,260	2,893	367
Transportation and travel	6,350	6,350	6,941	(591)
Utilities	242,735	242,735	280,709	(37,974)
Capital outlay - engineering and construction	360,000	360,000	125,567	234,433
Principal paid on liability due to City of Huntington Beach	80,000	80,000	80,000	-
TOTAL EXPENDITURES	<u>1,442,410</u>	<u>1,442,410</u>	<u>1,170,554</u>	<u>271,856</u>
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	(415,560)	(415,560)	(66,611)	348,949
FUND BALANCE, AS RESTATED - JULY 1, 2015	<u>838,694</u>	<u>838,694</u>	<u>838,694</u>	<u>-</u>
FUND BALANCE - JUNE 30, 2016	<u><u>\$ 423,134</u></u>	<u><u>\$ 423,134</u></u>	<u><u>\$ 772,083</u></u>	<u><u>\$ 348,949</u></u>

See accompanying notes to basic financial statements.

NOTES TO BASIC FINANCIAL STATEMENTS

SUNSET BEACH SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

A. Description of Reporting Entity:

The Sunset Beach Sanitary District (the District) was organized in 1930 to operate a sewer system serving the residents of Sunset Beach, within the City of Huntington Beach, Surfside Colony within the City of Seal Beach, and certain lots within the City of Huntington Beach. At June 30, 2016, the District served 242 commercial units, 1,000 residential sewer units, and 1,029 trash units.

B. Financial Statement Presentation:

Local government entities are required to report information on a government-wide basis and on a fund basis (with emphasis placed on major funds of the entity). The government-wide financial statements (i.e., statement of net position and the statement of activities) report information on all of the activities of the primary government and its component units. The governmental fund financial statements (i.e., balance sheet and the statement of revenues, expenditures and changes in fund balance) report information on individual funds of the government. A fund is considered to be a separate accounting entity with a self-balancing set of accounts.

Since the District is engaged in a single governmental activity and it has no component units, the government-wide and governmental fund financial statements have been combined with a reconciliation of the individual line items in a separate column entitled "Adjustments" on the financial statements, which accounts for the differences in measurement focus and basis of accounting of these financial statements as described in Notes 1C and 1D. The amounts reported in the "Adjustments" column pertain to the balances and activity of the District's long-term assets and liabilities. The government-wide financial statements are reported in the "Statement of Net Position" and "Statement of Activities" columns. The governmental fund financial statements are reported in the "General Fund" column.

C. Measurement Focus:

Measurement focus is a term used to describe "which" transactions are recorded within the various financial statements. Basis of accounting refers to "when" transactions are recorded regardless of the measurement focus applied.

On the government-wide statement of net position and the statement of activities, activities are presented using the economic resources measurement focus. Under the economic resources measurement focus, all (both current and long term) economic resources and obligations of the government are reported.

SUNSET BEACH SANITARY DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

C. Measurement Focus (Continued):

In the governmental fund financial statements, all funds are accounted for on the current financial resources measurement focus. This means that only current assets and current liabilities are generally included on their balance sheets. Their reported fund balances (net current assets) are considered a measure of “available spendable resources.” Governmental fund operating statements present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets. Accordingly, they are said to present a summary of sources and uses of available spendable resources during a period.

Because of their spending measurement focus, expenditure recognition for governmental fund types excludes amounts represented by noncurrent liabilities. Since they do not affect net current assets, such long-term amounts are not recognized as governmental fund type expenditures or fund liabilities. Amounts expended to acquire capital assets are recorded as expenditures in the year that the resources were expended, rather than as fund assets. The proceeds of long-term debt are recorded as other financing sources rather than as a fund liability. Amounts paid to reduce long-term indebtedness are reported as fund expenditures.

D. Basis of Accounting:

In the government-wide statement of net position and statement of activities, the governmental activities are presented using the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or the economic asset is used, regardless of the timing of related cash flows. Revenues, expenses, gains, losses, assets, and liabilities resulting from exchange and exchange-like transactions are recognized when the exchange takes place.

In the governmental fund financial statements, funds are presented using the modified-accrual basis of accounting. Revenues are recognized when they become measurable and available as net current assets. Measurable means that the amounts can be estimated or otherwise determined. Available means that the amounts were collected during the reporting period or soon enough thereafter to be available to finance the expenditures accrued for the reporting period. Revenue recognition is subject to the measurable and availability criteria for the governmental funds in the fund financial statements. The District considers fees for sanitation services, property taxes, and investment income to be available if collected within 60 days of the end of the current fiscal period.

SUNSET BEACH SANITARY DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

D. Basis of Accounting (Continued):

Fees for sanitation services, property taxes, and investment income associated with the current fiscal period are all considered to be susceptible to accrual and have been recognized as revenues of the current fiscal period to the extent normally collected within the availability period. Other revenue items are considered to be measurable and available when cash is received by the government.

E. New Accounting Pronouncements:

GASB Current Year Standards:

In fiscal year 2015-2016, the District implemented Governmental Accounting Standards Board (GASB) Statement No. 72, *Fair Value Measurement and Application*. GASB Statement No. 72 requires the District to use valuation techniques which are appropriate under the circumstances and are either a market approach, a cost approach or income approach. GASB Statement No. 72 establishes a hierarchy of inputs used to measure fair value consisting of three levels. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs are inputs, other than quoted prices included within Level 1, which are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability. GASB Statement No. 72 also contains note disclosure requirements regarding the hierarchy of valuation inputs and valuation techniques that are used for the fair value measurements. There was no material impact on the District's financial statements as a result of the implementation of GASB Statement No. 72.

GASB Statement No. 73 - *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68 and Amendments to Certain Provisions of GASB Statements 67 and 68*, was required to be implemented in the current fiscal year, except for those provisions that address employer and governmental nonemployer contributing entities for pensions that are not within the scope of GASB Statement No. 68, and is effective for periods beginning after June 15, 2016, and did not impact the District.

GASB Statement No. 76 - *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, was required to be implemented in the current fiscal year and did not impact the District.

GASB Statement No. 79 - *Certain External Investment Pools and Pool Participants*, was required to be implemented in the current fiscal year, except for certain provisions on portfolio quality, custodial credit risk, and shadow pricing, which are effective for periods beginning after December 15, 2015, and did not impact the District.

SUNSET BEACH SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. New Accounting Pronouncements (Continued):

GASB Current Year Standards (Continued):

GASB Statement No. 82, *Pension Issues an Amendment of GASB Statements No. 67, No. 68, and No. 73*, changed the measurement of covered payroll reported in required supplementary information and did not impact the District.

GASB Pending Accounting Standards:

GASB has issued the following statements, which may impact the District's financial reporting requirements in the future.

- GASB 73 - *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68 and Amendments to Certain Provisions of GASB Statements 67 and 68*, the provisions that address employer and governmental nonemployer contributing entities for pensions that are not within the scope of GASB 68, effective for periods beginning after June 15, 2016.
- GASB 74 - *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, effective for periods beginning after June 15, 2016.
- GASB 75 - *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, effective for periods beginning after June 15, 2017.
- GASB 77 - *Tax Abatement Disclosure*, effective for periods beginning after December 15, 2015.
- GASB 78 - *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*, effective for periods beginning after December 15, 2015.
- GASB 79 - *Certain External Investment Pools and Pool Participants*, contain certain provisions on portfolio quality, custodial credit risk, and shadow pricing, effective for periods beginning after December 15, 2015.
- GASB 80 - *Blending Requirements for Certain Component Units*, effective for periods beginning after June 15, 2016.
- GASB 81 - *Irrevocable Split-Interest Agreements*, effective for periods beginning after December 15, 2016.

SUNSET BEACH SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. New Accounting Pronouncements (Continued):

GASB Pending Accounting Standards (Continued):

- GASB 82 - *Pension Issues*, effective for periods beginning after June 15, 2016, except for certain provisions on selection of assumptions, which are effective in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017.
- GASB 83 - *Certain Asset Retirement Obligations*, effective for periods beginning after June 15, 2018.
- GASB 84 - *Fiduciary Activities*, effective for periods beginning after December 15, 2018.
- GASB 85 - *Omnibus 2017*, effective for periods beginning after June 15, 2017.
- GASB 86 - *Certain Debt Extinguishment Issues*, effective for periods beginning after June 15, 2017.
- GASB 87 - *Leases*, effective for periods beginning after December 15, 2019.

F. Investments:

Investments are reported at the fair value, which represents the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

G. Capital Assets:

The capital assets of the District are comprised of capacity rights purchased by the District in sewage treatment and transmission facilities owned by others, as well as fixed assets owned by the District. Capacity rights are carried at cost with no provision for amortization.

Other capital assets owned by the District, which includes sewer improvements, pump stations and equipment, are carried at cost, net of accumulated depreciation. Capital assets are depreciated using the straight-line method and lives used for depreciation are:

Sewer improvements and pump stations	10 - 30 years
Equipment	7 - 10 years

SUNSET BEACH SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

G. Capital Assets (Continued):

The District's policy is to capitalize assets purchased with an economic useful life of more than one year and a cost of more than \$1,000.

H. Sanitation Services Revenue:

Sanitation services revenue results from residential and business refuse disposal secured assessments which are collected from the District population by additions to the annual property tax statements.

I. Property Taxes:

Property taxes attach as an enforceable lien on property as of January 1. Taxes are levied on July 1 and are payable in two installments on November 1 and February 1 and become delinquent December 11 and April 11. The County of Orange bills and collects the property taxes and remits them to the District in installments during the year. District property tax revenues are recognized when levied to the extent that they result in current receivables.

J. Lease:

The District accounts for its leased storage space under the operating method of accounting, thus, lease payments are expensed as incurred.

K. Net Position:

In the statement of net position, net position is classified in the following categories:

Net Investment in Capital Assets - This category groups all capital assets, including infrastructure, into one component of net position. Accumulated depreciation on these assets and related long-term debt used to acquire the assets reduces this category.

Unrestricted Net Position - This category represents the net position of the District that is not restricted for any project or other purpose.

SUNSET BEACH SANITARY DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

K. Net Position (Continued):

Net Position Flow Assumption:

Sometimes the District will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted - net position and unrestricted - net position in the government-wide financial statements, a flow assumption must be made about the order in which the resources are considered to be applied.

It is the District's practice to consider restricted - net position to have been depleted before unrestricted - net position is applied.

L. Fund Balance:

The fund balance reported in the governmental fund balance sheet is classified in the following categories:

Nonspendable Fund Balance - this includes amounts that cannot be spent because they are either not spendable in form or legally or contractually required to be maintained intact.

Assigned Fund Balance - This classification includes amounts that are intended to be used by the government for specific purposes but do not meet the criteria to be classified as restricted or committed. Intent is expressed by the Board of Directors to assign amounts to be used for specific purposes.

Unassigned Fund Balance - This classification includes the residual balance for the government's general fund and includes all spendable amounts not contained in other classifications.

When an expenditure is incurred for purposes for which both restricted and unrestricted fund balances are available, the District's policy is to apply restricted fund balance first.

When an expenditure is incurred for purposes for which committed, assigned, or unassigned fund balances are available, the District's policy is to apply committed fund balance first, then assigned fund balance, and finally unassigned fund balance.

SUNSET BEACH SANITARY DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

M. Budget:

The Board of Directors adopts an annual budget which begins on July 1. Annual appropriations are approved by the Board of Directors prior to the beginning of each year. All appropriations lapse at year-end. The Board of Directors has the legal authority to amend the budget at any time during the fiscal year. The level of budgetary control (that is, the level at which expenditures cannot legally exceed the appropriated amount) is established at the expenditure line item level.

N. Estimates:

The preparation of basic financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities/and disclosures of contingent assets and liabilities at the date of the basic financial statements, as well as the reported amounts of revenues and expenditures/expenses during the reporting period. Accordingly, actual results could differ from those estimates.

2. CASH AND INVESTMENTS:

Cash and Investments:

Cash and investments of \$1,036,904 consists of \$63,560 in federally-insured demand accounts, \$569,955 invested in California Local Agency Investment Fund (LAIF), and \$403,389 maintained by the County of Orange (County), and pooled with other County cash and investments. Interest income is allocated to the District on a quarterly basis by the County and LAIF.

Investments Authorized by the California Government Code:

The table below identifies the investment types that are authorized by the District's investment policy. The table also identifies certain provisions of the California Government Code that address interest rate risk, credit risk, and concentration of credit risk.

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Maximum Percentage of Portfolio</u>	<u>Maximum Investment in One Issuer</u>
Local Agency Investment Fund (LAIF)	N/A	None	None
Orange County Pooled Investment Fund	N/A	None	None
N/A - Not Applicable			

SUNSET BEACH SANITARY DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

2. CASH AND INVESTMENTS (CONTINUED):

Disclosures Relating to Interest Rate Risk:

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the District manages its exposure to interest rate risk is by investing in the Orange County Pooled Investment Fund and LAIF. Funds invested in the Orange County Pooled Investment Fund and LAIF are highly liquid as deposits and withdrawals can be made at any time without penalty.

Disclosures Relating to Credit Risk:

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The District's investments in the Orange County Pooled Investment Fund and LAIF are not rated.

The District has no limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code.

Custodial Credit Risk:

Custodial credit risk for *deposits* is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for *investments* is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) the District will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code and the District's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure District deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits. Any deposits in excess of depository insurance limits at the end of the year are collateralized by securities held at the depository financial institution's trust department.

SUNSET BEACH SANITARY DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

2. CASH AND INVESTMENTS (CONTINUED):

Investment in Orange County Pooled Investment Fund:

The District is a voluntary participant in the Orange County Pooled Investment Fund (OCPIF) that is a pooled investment fund program governed by the Orange County Board of Supervisors, and is administered by the Orange County Treasurer and Tax Collector. Investments in OCPIF are highly liquid as deposits and withdrawal can be made at any time without penalty. The District's fair value of its share in the pool is the same value of the pool shares. Information on OCPIF's use of derivative securities in its investment portfolio, OCPIF's, and the District's exposure to credit, market, or legal risk is not available.

Investment in Local Agency Investment Fund:

The District is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. The fair value of the District's investment in this pool is reported in the accompanying financial statements at amounts based upon the District's pro rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis.

Fair Value Measurements:

The District categorizes its fair value measurement within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the relative inputs used to measure the fair value of the investments. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

The three levels of the fair value hierarchy are described as follows:

Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the District has the ability to access.

Level 2: Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

SUNSET BEACH SANITARY DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

2. CASH AND INVESTMENTS (CONTINUED):

Fair Value Measurements (Continued):

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement. Unobservable inputs reflect the District's own assumptions about the inputs market participants would use in pricing the asset or liability (including assumptions about risk). Unobservable inputs are developed based on the best information available in the circumstances and may include the District's own data.

The asset's or liability's level within the hierarchy is based on the lowest level of input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The determination of what constitutes observable requires judgment by the District's management. District management considers observable data to be that market data which is readily available, regularly distributed or updated, reliable, and verifiable, not proprietary, and provided by multiple independent sources that are actively involved in the relevant market.

The categorization of an investment or liability within the hierarchy is based upon the relative observability of the inputs to its fair value measurement and does not necessarily correspond to District management's perceived risk of that investment or liability.

The District's investment consists of OCPIF and LAIF, which are investments not subject to the fair value hierarchy disclosure.

3. SEWER TRANSMISSION AND TREATMENT CAPACITY RIGHTS:

The District purchased capacity rights in facilities for transmission and treatment of District wastewater and sewage from the City of Huntington Beach on December 23, 1970, at a cost of \$158,812, on July 29, 1986, at a cost of \$327,500, on July 17, 2006, at a cost of \$800,000, and on June 11, 2015, at a cost of \$468,077. The City of Huntington Beach has contracted with County Sanitation District No. 11 of Orange County to provide treatment and disposal facilities for the processing of wastewater and sewage from the District's area.

The District owns certain transmission lines and pumps which are in use but are fully depreciated since they were acquired prior to 1940. No cost or book values for these assets are shown in the accompanying financial statements.

SUNSET BEACH SANITARY DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

4. CAPITAL ASSETS:

Capital asset activity for the year ended June 30, 2016 was as follows:

	Balance at June 30, 2015	Additions	Deletions	Balance at June 30, 2016
Capital assets, not being depreciated:				
Capacity rights	\$ 1,754,389	\$ -	\$ -	\$ 1,754,389
Construction in progress	<u>19,481</u>	<u>61,092</u>	<u>-</u>	<u>80,573</u>
Total capital assets, not being depreciated	<u>1,773,870</u>	<u>61,092</u>	<u>-</u>	<u>1,834,962</u>
Capital assets, being depreciated:				
Sewer improvements and pump stations	2,398,143	116,873	-	2,515,016
Equipment	<u>228,916</u>	<u>60,871</u>	<u>-</u>	<u>289,787</u>
Total capital assets being depreciated	2,627,059	177,744	-	2,804,803
Less accumulated depreciation	<u>(834,442)</u>	<u>(183,867)</u>	<u>-</u>	<u>(1,018,309)</u>
Total capital assets being depreciated, net	<u>1,792,617</u>	<u>(6,123)</u>	<u>-</u>	<u>1,786,494</u>
Capital assets, net	<u>\$ 3,566,487</u>	<u>\$ 54,969</u>	<u>\$ -</u>	<u>\$ 3,621,456</u>

5. DUE TO THE CITY OF HUNTINGTON BEACH:

The District entered into an amendment on July 17, 2006, (Amendment No. 1) to supplement an agreement dated April 2, 2001, entitled "Agreement for the Conveyance of Wastewater" between the City of Huntington Beach (the City) and Sunset Beach Sanitary District whereby the District was afforded a capacity right in the City's existing and expanded wastewater facilities. The City has entered into a contract "Existing Work" for the construction of certain pump stations and sewer lines at a depth and location which will substantially reduce capital, operation, and maintenance costs, that the District would otherwise incur provided it remains connected to the City's sewerage system. Under the agreement, \$800,000 is the District's fair share of the "Existing Work" to design, administer, and construct the "Existing Work." The District will pay the City an annual payment of \$80,000 (without interest) for ten consecutive years commencing February 1, 2007, and each successive payment will be made on the anniversary of that date. During the year ended June 30, 2016, the District made the final principal payment of \$80,000.

SUNSET BEACH SANITARY DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

6. MINIMUM LEASE PAYMENTS:

The District leases a storage facility under a three-year, noncancelable operating lease agreement. The lease requires monthly payments of \$926 through May 31, 2016 and \$972 thereafter through May 31, 2018. Total rental expenditures for the period ended June 30, 2016, is \$11,296. The following is a schedule by fiscal year of future minimum rental payments required under the operating lease agreements:

<u>Year Ending</u> <u>June 30,</u>	<u>Amount</u>
2017	\$ 11,664
2018	<u>10,692</u>
	<u>\$ 22,356</u>

7. JOINT POWERS AUTHORITY:

The District is a member of the Special District Risk Management Authority (Authority).

A. Description of Special District Risk Management Authority:

The Authority is an intergovernmental risk sharing joint powers authority, created under provisions of California Government Code Sections 6500 et seq. The purpose of the Authority is to arrange and administer programs of insurance for the pooling of self-insured losses and to purchase excess insurance coverage.

B. Self-Insurance Programs of the Authority:

At June 30, 2016, the District participated in the self-insurance programs of the Authority as follows:

Property Loss: Insured up to replacement cost for scheduled property. \$1,000,000,000 per occurrence, subject to a \$1,000 deductible.

Boiler and Machinery Coverage: Insured up to replacement cost for scheduled property. \$100,000,000 per occurrence, subject to a \$1,000 deductible.

General and Auto Liability: Insured up to \$5,000,000 per occurrence, subject to a \$500 deductible for general liability claims and \$1,000 deductible for auto liability claims.

SUNSET BEACH SANITARY DISTRICT

NOTES TO BASIC FINANCIAL STATEMENTS
(CONTINUED)

June 30, 2016

7. JOINT POWERS AUTHORITY (CONTINUED):

B. Self-Insurance Programs of the Authority (Continued):

Public Officials' and Employees' Errors and Omissions, and Employment Practices Liability: Insured up to \$5,000,000 per wrongful act with an annual member aggregate. The District is responsible for 50% of the amount in excess of \$10,000 and less than \$50,000. However, if certain criteria is met, this obligation will be waived.

General and Auto Liability, Public Officials' and Employees' Errors and Omissions, and Employment Practices Liability have a combined single limit of \$5,000,000 per occurrence.

Public Officials' Personal Liability: Insured up to \$500,000 per occurrence with an annual aggregate per Board Member, subject to a \$500 deductible.

Employee Dishonesty Coverage: Insured up to \$1,000,000 per occurrence. Includes public employee dishonesty, forgery, or alteration and theft, and disappearance and destruction coverages.

Workers' Compensation Coverage and Employer's Liability Coverage: Insured up to California statutory limits for all work related injuries/illnesses covered by California law and up to \$5,000,000 for employer's liability coverage subject to terms, conditions and exclusions as provided in the Memorandum of Coverage.

During the past three years, the above programs have had no settlements that exceed insurance coverage and there have been no significant reductions in insurance coverage.

8. RESTATEMENT OF FUND BALANCE/NET POSITION:

The District reduced fund balance and net position by \$24,580 as of July 1, 2015 for an adjustment of prior year salary and utility expenses recorded in the current year.

9. SUBSEQUENT EVENTS:

In preparing these financial statements, the District has evaluated events and transactions for potential recognition or disclosure through November 9, 2017, the date the financial statements were available to be issued.