



# El Toro Water District

"A District of Distinction"

Serving the Public - Respecting the Environment

**Board of Directors**

Ted F. Martin  
M. Scott Goldman  
William H. Kahn  
Jerard B. Werner  
Jose F. Vergara

**General Manager**

Robert R. Hill

November 26, 2014

Wendy Giltner  
County of Orange, Auditor-Controller  
12 Civic Center Plaza  
P.O. Box 567  
Santa Ana, CA 92702-0567

Dear Ms. Giltner:

Enclosed please find a copy of El Toro Water District's Audit Report for the fiscal year ended June 30, 2014 as required by Government Code Section 26909. The Report was prepared by Charles Z. Fedak & Company, Certified Public Accountants.

If you have any questions concerning this information, feel free to contact me.

Sincerely,

EL TORO WATER DISTRICT

Michael P. Grandy  
Chief Financial Officer

Enclosure

cc: Audit

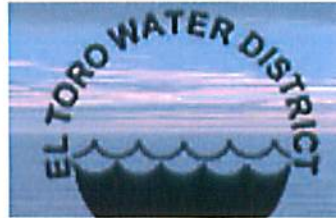


**El Toro Water District**

**Annual Financial Report**

**For the Fiscal Year Ended June 30, 2014**

AUDITOR-CONTROLLER  
DEC. 12, 2014



**El Toro Water District  
Board of Directors as of June 30, 2014**

<u>Name</u>	<u>Title</u>	<u>Elected/ Appointed</u>	<u>Current Term</u>
Ted F. Martin	President	Elected	2012 - 2016
M. Scott Goldman	Vice President	Elected	2012 - 2016
Jerard B. Werner	Treasurer	Elected	2010 - 2014
William H. Kahn	Director	Elected	2010 - 2014
Jose Vergara	Director	Elected	2012 - 2016

**El Toro Water District  
Robert R. Hill, General Manager  
24251 Los Alisos Blvd.  
Lake Forest, California 92630  
(949) 837-0660 – [www.etwd.com](http://www.etwd.com)**

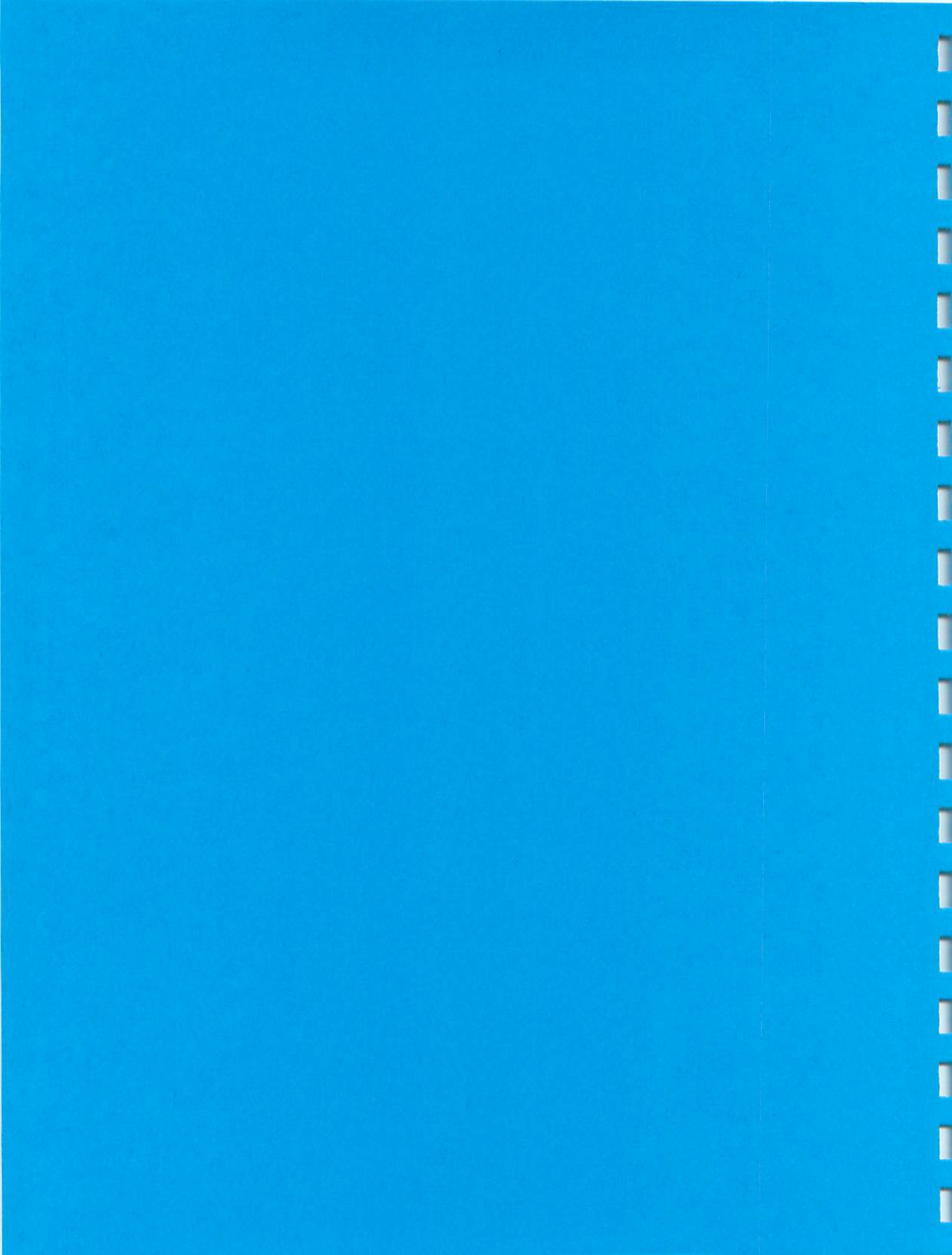
**El Toro Water District**  
**Annual Financial Report**  
**For the Fiscal Year Ended June 30, 2014**

**El Toro Water District  
Annual Financial Report  
For the Fiscal Year Ended June 30, 2014**

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## **Financial Section**





Charles Z. Fedak, CPA, MBA  
Paul J. Kaymark, CPA  
Christopher J. Brown, CPA

# Charles Z. Fedak & Company

Certified Public Accountants  
An Accountancy Corporation

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## Independent Auditor's Report

Board of Directors  
El Toro Water District  
Lake Forest, California

### Report on the Financial Statements

We have audited the accompanying financial statements of the El Toro Water District (District) as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents. The comparative financial information as of June 30, 2013, was audited by other auditors whose report dated November 6, 2013, expressed an unqualified opinion on those basic financial statements.

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

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

### *Auditor's Responsibility*

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's 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 auditor considers internal control relevant to the entity'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 entity'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.

### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the District, as of June 30, 2014, and the respective changes in financial position, and, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.



## Independent Auditor's Report, continued

### *Other Matters*

#### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 6 and the required supplementary information on page 26 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 auditing standards generally accepted in the United States of America, which consisted of inquiries of 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.

#### *Other Reporting Required by Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 10, 2014, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance. This report can be found on pages 27 and 28.



**Charles Z. Fedak and Company, CPAs – An Accountancy Corporation**  
Cypress, California  
October 10, 2014

**El Toro Water District**  
**Management's Discussion and Analysis**  
**For the Fiscal Year Ended June 30, 2014**

The following Management's Discussion and Analysis (MD&A) of activities and financial performance of the El Toro Water District (District) provides an introduction to the financial statements of the District for the fiscal year ended June 30, 2014. We encourage readers to consider the information presented here in conjunction with the basic financial statements and related notes, which follow this section.

**Financial Highlights**

- The District's net position increased 1.8%, or \$1,215,067 to \$69,597,452, in fiscal year 2014, as a result of operations.
- In 2014, the District's operating revenues increased 2.6%, or \$596,115, primarily due to a \$233,131 increase in water consumption sales and \$355,995 increase in sewer services.
- In 2014, the District's operating expenses increased 8.6%, or \$1,733,911, primarily due to increases in source of supply of \$1,030,504 and transmission and distribution costs of \$332,181.

**Required Financial Statements**

This annual report consists of a series of financial statements. The Statement of Net Position, Statement of Revenues, Expenses and Changes in Net Position and Statement of Cash Flows provide information about the activities and performance of the District using accounting methods similar to those used by private sector companies.

The Statement of Net Position includes all of the District's investments in resources (assets) and the obligations to creditors (liabilities). It also provides the basis for computing a rate of return, evaluating the capital structure of the District and assessing the liquidity and financial flexibility of the District. All of the current year's revenue and expenses are accounted for in the Statement of Revenues, Expenses and Changes in Net Position. This statement measures the success of the District's operations over the past year and can be used to determine if the District has successfully recovered all of its costs through its rates and other charges. This statement can also be used to evaluate profitability and credit worthiness. The final required financial statement is the Statement of Cash Flows, which provides information about the District's cash receipts and cash payments during the reporting period. The Statement of Cash Flows reports cash receipts, cash payments and net changes in cash resulting from operations, investing, non-capital financing, and capital and related financing activities and provides answers to such questions as where did cash come from, what was cash used for, and what was the change in cash balance during the reporting period.

**Financial Analysis of the District**

One of the most important questions asked about the District's finances is, "Is the District better off or worse off as a result of this year's activities?" The Statement of Net Position and the Statement of Revenues, Expenses and Changes in Net Position report information about the District in a way that helps answer this question.

These statements include all assets and liabilities using the *accrual basis of accounting*, which is similar to the accounting method used by most private sector companies. All of the current year's revenues and expenses are taken into account regardless of when the cash is received or paid.

These two statements report the District's *net position* and changes in them. One can think of the District's net position – the difference between assets and liabilities – as one way to measure the District's financial health, or *financial position*. Over time, *increases or decreases* in the District's net position are one indicator of whether its *financial health* is improving or deteriorating. However, one will need to consider other non-financial factors such as changes in economic conditions, population growth, zoning and new or changed government legislation, such as changes in Federal and State water quality standards.

**El Toro Water District**  
**Management's Discussion and Analysis**  
**For the Fiscal Year Ended June 30, 2014**

**Notes to the Basic Financial Statements**

The notes provide additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the basic financial statements can be found on pages 11 through 25.

**Statements of Net Position**

**Condensed Statements of Net Position**

	<u>2014</u>	<u>2013</u>	<u>Change</u>
<b>Assets:</b>			
Current assets	\$ 22,973,175	22,837,894	135,281
Non-current assets	-	204,546	(204,546)
Capital assets, net	<u>81,171,562</u>	<u>60,520,579</u>	<u>20,650,983</u>
<b>Total assets</b>	<u><u>104,144,737</u></u>	<u><u>83,563,019</u></u>	<u><u>20,581,718</u></u>
<b>Liabilities:</b>			
Current liabilities	6,879,027	5,829,684	1,049,343
Non-current liabilities	<u>27,668,259</u>	<u>9,350,950</u>	<u>18,317,309</u>
<b>Total liabilities</b>	<u><u>34,547,285</u></u>	<u><u>15,180,634</u></u>	<u><u>19,366,651</u></u>
<b>Net Position:</b>			
Net investment in capital assets	57,218,606	53,386,647	3,831,959
Restricted for debt service	2,856,335	3,427,601	(571,266)
Unrestricted	<u>9,522,511</u>	<u>11,568,137</u>	<u>(2,045,626)</u>
<b>Total net position</b>	<u><u>69,597,452</u></u>	<u><u>68,382,385</u></u>	<u><u>1,215,067</u></u>
<b>Total liabilities and net position</b>	<u><u>\$ 104,144,737</u></u>	<u><u>83,563,019</u></u>	<u><u>20,581,718</u></u>

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. In the case of the District, assets of the District exceeded liabilities by \$69,597,452 as of June 30, 2014.

By far the largest portion of the District's net position (82% as of June 30, 2014) reflects the District's investment in capital assets (net of accumulated depreciation) less any related debt used to acquire those assets that is still outstanding. The District uses these capital assets to provide services to customers within the District's service area; consequently, these assets are not available for future spending.

At the end of fiscal year 2014, the District showed a balance in its restricted net position of \$2,856,335, which is restricted for debt service repayments.

At the end of fiscal year 2014, the District showed a positive balance in its unrestricted net position of \$9,522,511, which may be utilized in future years. (See note 9 for further details)

**El Toro Water District**  
**Management's Discussion and Analysis**  
**For the Fiscal Year Ended June 30, 2014**

**Statements of Revenues, Expenses and Changes in Net Position**

**Condensed Statements of Revenues, Expenses and Changes in Net Position**

	<u>2014</u>	<u>2013</u>	<u>Change</u>
<b>Revenue:</b>			
Operating revenue	\$ 23,188,691	22,592,576	596,115
Non-operating revenue	1,048,295	1,342,285	(293,990)
Total revenue	<u>24,236,986</u>	<u>23,934,861</u>	<u>302,125</u>
<b>Expense:</b>			
Operating expense	21,703,124	19,969,213	1,733,911
Depreciation expense	2,781,397	2,816,753	(35,356)
Non-operating expense	185,655	1,899,303	(1,713,648)
Total expense	<u>24,670,176</u>	<u>24,685,269</u>	<u>(15,093)</u>
Net loss before capital contributions	(433,190)	(750,408)	317,218
<b>Capital contributions:</b>	<u>1,648,257</u>	<u>3,092,146</u>	<u>(1,443,889)</u>
Change in net position	1,215,067	2,341,738	(1,126,671)
Net position, beginning of year	<u>68,382,385</u>	<u>66,040,647</u>	<u>2,341,738</u>
Net position, end of year	<u>\$ 69,597,452</u>	<u>68,382,385</u>	<u>1,215,067</u>

The statement of revenues, expenses and changes of net position shows how the District's net position changed during the fiscal year. In the case of the District, the District's change in net position increased by \$1,215,067 for the fiscal year ended June 30, 2014.

A closer examination of the sources of changes in net position reveals that:

In 2014, the District's operating revenues increased 2.6%, or \$596,115, primarily due to a \$233,131 increase in water consumption sales and \$355,995 increase in sewer services.

In 2014, the District's operating expenses increased 8.7%, or \$1,733,911, primarily due to increases in source of supply of \$1,030,504 and increase in transmission and distribution costs of \$332,181.

**Capital Asset Administration**

Changes in capital asset amounts for 2014 were as follows:

	<u>Balance 2013</u>	<u>Additions</u>	<u>Transfers/ Deletions</u>	<u>Balance 2014</u>
<b>Capital assets:</b>				
Non-depreciable assets	\$ 21,974,133	22,990,259	(5,499,383)	39,465,009
Depreciable assets	92,576,662	5,941,504	-	98,518,166
Accumulated depreciation	<u>(54,030,216)</u>	<u>(2,781,397)</u>	<u>-</u>	<u>(56,811,613)</u>
Total capital assets, net	<u>\$ 60,520,579</u>	<u>26,150,366</u>	<u>(5,499,383)</u>	<u>81,171,562</u>

At the end of fiscal year 2014, the District's investment in capital assets amounted to \$81,171,562 (net of accumulated depreciation). This investment in capital assets includes land, transmission and distribution systems, buildings, equipment, vehicles and construction-in-process, etc. (See note 4 for further information)

**El Toro Water District**  
**Management's Discussion and Analysis**  
**For the Fiscal Year Ended June 30, 2014**

**Debt Administration**

Changes in long-term debt amounts for 2014 were as follows:

	<u>Balance 2013</u>	<u>Additions</u>	<u>Principal Payments</u>	<u>Balance 2014</u>
Long-term debt:				
Loans payable	\$ 7,133,932	18,118,947	(1,299,923)	23,952,956
Total long-term debt	\$ <u>7,133,932</u>	<u>18,118,947</u>	<u>(1,299,923)</u>	<u>23,952,956</u>

**Conditions Affecting Current Financial Position**

Management is unaware of any conditions which could have a significant impact on the District's current financial position, net position or operating results based on past, present and future events. (See note 6 for further information)

**Requests for Information**

This financial report is designed to provide the District's funding sources, customers, stakeholders and other interested parties with an overview of the District's financial operations and financial condition. Should the reader have questions regarding the information included in this report or wish to request additional financial information, please contact Michael P. Grandy, Assistant General Manager/CFO at El Toro Water District 24251 Los Alisos Boulevard, Lake Forest, California.

# Basic Financial Statements

**El Toro Water District**  
**Statements of Net Position**  
**June 30, 2014**  
**With comparative amounts for June 30, 2013**

<i>Assets</i>	<b>2014</b>	<b>2013</b>
<b>Current assets:</b>		
Cash and cash equivalents (note 2)	\$ 9,543,932	5,255,781
Investments (note 2)	7,011,860	8,026,812
Restricted – cash and cash equivalents (note 2)	2,856,335	3,427,601
Accrued interest receivable	26,073	33,514
Accounts receivable – water sales and sewer services	2,144,469	2,224,826
Property taxes receivable	8,955	18,222
Accounts receivable – grants	655,915	3,062,505
Accounts receivable – other	29,561	26,880
Note receivable – AMP – current portion (note 3)	-	58,535
Materials and supplies inventory	597,528	600,195
Prepaid expenses and other deposits	98,547	103,023
Total current assets	<u>22,973,175</u>	<u>22,837,894</u>
<b>Non-current assets:</b>		
Note receivable – AMP – long-term portion (note 3)	-	204,546
Capital assets – not being depreciated (note 4)	39,465,009	21,974,133
Capital assets, net – being depreciated (note 4)	41,706,553	38,546,446
Total non-current assets	<u>81,171,562</u>	<u>60,725,125</u>
<b>Total assets</b>	<u>\$ 104,144,737</u>	<u>83,563,019</u>
<b><i>Liabilities and Net Position</i></b>		
<b>Current liabilities:</b>		
Accounts payable and accrued expenses	\$ 5,498,974	4,021,283
Accrued wages and related payables	117,711	95,037
Customer deposits and unearned revenue	55,416	30,995
Accrued interest payable	169,574	71,020
Long-term liabilities – due within one year:		
Compensated absences (note 5)	339,505	305,246
Loans payable (note 6)	697,847	1,306,103
Total current liabilities	<u>6,879,027</u>	<u>5,829,684</u>
<b>Non-current liabilities:</b>		
Compensated absences (note 5)	1,018,514	915,738
Other post-employment benefits payable (note 8)	3,394,636	2,607,383
Loans payable (note 6)	23,255,109	5,827,829
Total non-current liabilities	<u>27,668,259</u>	<u>9,350,950</u>
<b>Total liabilities</b>	<u>34,547,285</u>	<u>15,180,634</u>
<b>Net position: (note 9)</b>		
Net investment in capital assets	57,218,606	53,386,647
Restricted for debt service	2,856,335	3,427,601
Unrestricted	9,522,511	11,568,137
Total net position	<u>69,597,452</u>	<u>68,382,385</u>
<b>Total liabilities and net position</b>	<u>\$ 104,144,737</u>	<u>83,563,019</u>

See accompanying notes to the basic financial statements

**El Toro Water District**  
**Statements of Revenues, Expenses and Changes in Net Position**  
**For the Fiscal Year Ended June 30, 2014**  
**With comparative amounts for the fiscal year ended June 30, 2013**

	<b>2014</b>	<b>2013</b>
<b>Operating revenues:</b>		
Water consumption sales	\$ 10,687,396	9,897,084
Water service charges	3,979,752	3,803,734
Sewer service charges	8,077,870	7,721,875
Standby charges	10,623	984,847
Reimbursement from others	124,353	117,364
Other charges for services	308,697	67,672
<b>Total operating revenues</b>	<b>23,188,691</b>	<b>22,592,576</b>
<b>Operating expenses:</b>		
Source of supply	9,584,718	8,554,214
Pumping	1,293,752	1,232,213
Water treatment	2,953,328	2,831,190
Transmission and distribution	4,492,432	4,160,251
Customer service	465,163	438,053
General and administrative	2,913,731	2,753,292
<b>Total operating expenses</b>	<b>21,703,124</b>	<b>19,969,213</b>
Operating income before depreciation	1,485,567	2,623,363
Depreciation expense – capital recovery	(2,781,397)	(2,816,753)
<b>Operating loss</b>	<b>(1,295,830)</b>	<b>(193,390)</b>
<b>Non-operating revenue(expense):</b>		
Property taxes-ad valorem	774,568	753,865
Rental revenue	165,282	184,548
Investment earnings	51,881	124,439
Interest expense	(185,655)	(327,684)
Other non-operating revenue	56,564	279,433
El Toro Recycled Water System Expansion project agreement	-	(1,571,619)
<b>Total non-operating, net</b>	<b>862,640</b>	<b>(557,018)</b>
<b>Net loss before capital contributions</b>	<b>(433,190)</b>	<b>(750,408)</b>
<b>Capital contributions:</b>		
Capital facility fees	85,847	29,641
Capital grants	1,562,410	3,062,505
<b>Total capital contributions</b>	<b>1,648,257</b>	<b>3,092,146</b>
<b>Change in net position</b>	<b>1,215,067</b>	<b>2,341,738</b>
<b>Net position, beginning of year</b>	<b>68,382,385</b>	<b>66,040,647</b>
<b>Net position, end of year</b>	<b>\$ 69,597,452</b>	<b>68,382,385</b>

See accompanying notes to the basic financial statements



**El Toro Water District**  
**Statements of Cash Flows**  
**For the Fiscal Year Ended June 30, 2014**  
**With comparative amounts for the fiscal year ended June 30, 2013**

	<u>2014</u>	<u>2013</u>
<b>Cash flows from operating activities:</b>		
Cash receipts from customers for water sales and services	\$ 23,488,213	23,463,502
Cash paid to employees for salaries and wages	(4,097,678)	(4,058,095)
Cash paid to vendors and suppliers for materials and services	<u>(15,149,230)</u>	<u>(15,514,653)</u>
Net cash provided by operating activities	<u>4,241,305</u>	<u>3,890,754</u>
<b>Cash flows from non-capital financing activities:</b>		
Proceeds from property taxes-ad valorem	<u>783,835</u>	<u>813,340</u>
Net cash provided by non-capital financing activities	<u>783,835</u>	<u>813,340</u>
<b>Cash flows from capital and related financing activities:</b>		
Acquisition and construction of capital assets	(23,432,380)	(8,667,495)
Capital contributions	4,054,847	29,641
Principal payments on long-term debt	(1,299,923)	(2,588,722)
Proceeds received from long-term debt	18,118,947	260,001
Interest paid	<u>(87,101)</u>	<u>(366,784)</u>
Net cash used in capital and related financing activities	<u>(2,645,610)</u>	<u>(11,333,359)</u>
<b>Cash flows from investing activities:</b>		
Principal received on note receivable – AMP	263,081	1,304,261
Sale(purchase) of investments, net	1,014,952	(971,580)
Investment earnings	<u>59,322</u>	<u>132,457</u>
Net cash provided by investing activities	<u>1,337,355</u>	<u>465,138</u>
<b>Net increase(decrease) in cash and cash equivalents</b>	<b>3,716,885</b>	<b>(6,164,127)</b>
<b>Cash and cash equivalents, beginning of year</b>	<u>8,683,382</u>	<u>14,847,509</u>
<b>Cash and cash equivalents, end of year</b>	<u>\$ 12,400,267</u>	<u>8,683,382</u>
<b>Reconciliation of cash and cash equivalents to statement of financial position:</b>		
Cash and cash equivalents	\$ 9,543,932	5,255,781
Restricted – cash and cash equivalents	<u>2,856,335</u>	<u>3,427,601</u>
<b>Total cash and cash equivalents</b>	<u>\$ 12,400,267</u>	<u>8,683,382</u>

Continued on next page

See accompanying notes to the basic financial statements

**El Toro Water District**  
**Statements of Cash Flows, continued**  
**For the Fiscal Year Ended June 30, 2014**  
**With comparative amounts for the fiscal year ended June 30, 2013**

	<b>2014</b>	<b>2013</b>
<b>Reconciliation of operating loss to net cash provided by operating activities:</b>		
<b>Operating loss</b>	\$ (1,295,830)	(193,390)
<b>Adjustments to reconcile operating loss to net cash provided by operating activities:</b>		
Depreciation expense – capital recovery	2,781,397	2,816,753
Rental revenue	165,282	184,548
Other non-operating revenue	56,564	279,433
El Toro Recycled Water System Expansion project agreement	-	(1,571,619)
<b>Changes in assets and liabilities:</b>		
<b>(Increase)decrease in assets:</b>		
Accounts receivable – water sales and sewer services, net	80,357	385,150
Accounts receivable – other	(2,681)	21,795
Materials and supplies inventory	2,667	(17,845)
Prepaid expenses and other deposits	4,476	(2,494)
<b>Increase(decrease) in liabilities:</b>		
Accounts payable and accrued expenses	1,477,691	1,472,373
Accrued wages and related payables	22,674	3,127
Customer deposits and unearned revenue	24,421	(5,855)
Compensated absences	137,034	(27,788)
Other post-employment benefits payable	787,253	546,566
Total adjustments	5,537,135	4,084,144
Net cash provided by operating activities	\$ 4,241,305	3,890,754

See accompanying notes to the basic financial statements

**El Toro Water District  
Notes to the Financial Statements  
For the Fiscal Year Ended June 30, 2014**

**(1) Reporting Entity and Summary of Significant Accounting Policies**

**A. Organization and Operations of the Reporting Entity**

El Toro Water District (District) was organized in September 1960, under provisions of the County Water District Act (Sections 34000 et. seq. of the Water Code of the State of California). The District is governed by a Board of Directors made up of five members elected by the qualified voters in the District. The purpose of the District is to finance, construct, operate and maintain a water and wastewater system to serve properties within the District's boundaries.

The El Toro Water District Public Facilities Corporation (Corporation) was organized on May 21, 1993 pursuant to the Non-Profit Public Benefit Corporation Law of the State of California (Title 1, Division 2, Part 2 of the California Corporation Code), solely for the purpose of providing financial assistance to the District. The Corporation, an entity legally separate from the District, is governed by substantially all the board members of the District. The Corporation is inactive at this time.

The criteria used in determining the scope of the financial reporting entity is based on the provisions of Governmental Accounting Statements No. 61, *The Financial Reporting Entity*. The District is the primary governmental unit based on the foundation of a separately elected governing board that is elected by the citizens in a general popular election. Component units are legally separate organizations for which the elected officials of the primary government are financially accountable. The District is financially accountable if it appoints a voting majority of the organization's governing body and: 1) It is able to impose its will on that organization, or 2) There is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary government.

**B. Basis of Accounting and Measurement Focus**

The District reports its activities as an enterprise fund, which is used to account for operations that are financed and operated in a manner similar to a private business enterprise, where the intent of the District is that the costs of providing water to its service area on a continuing basis be financed or recovered primarily through user charges (water sales), sewer service fees, capital grants and similar funding. Revenues and expenses are recognized on the full accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred, regardless of when the related cash flows take place.

Operating revenues and expenses, such as water sales and water purchases, result from exchange transactions associated with the principal activity of the District. Exchange transactions are those in which each party receives and gives up essentially equal values. Management, administration, and depreciation expenses are also considered operating expenses. Other revenues and expenses, not included in the above categories, are reported as non-operating revenues and expenses.

**C. Financial Reporting**

The District's basic financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP), as applied to enterprise funds. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The District solely operates as a special-purpose government which means it is only engaged in business-type activities; accordingly, activities are reported in the District's proprietary fund.

**El Toro Water District  
Notes to the Financial Statements, continued  
For the Fiscal Year Ended June 30, 2014**

**(1) Reporting Entity and Summary of Significant Accounting Policies, continued**

**D. Assets, Liabilities and Net Position**

**1. Use of Estimates**

The preparation of the basic financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities they also include disclosures of contingent assets and liabilities at the date of the financial statements and the reported changes in net position during the reporting period. Actual results could differ from those estimates.

**2. Cash and Cash Equivalents**

Substantially all of the District's cash is invested in interest bearing accounts. The District considers all highly liquid investments with a maturity of three months or less to be cash equivalents.

**3. Investments and Investment Policy**

The District has adopted an investment policy directing the Chief Financial Officer to invest the District's funds in financial institutions.

Changes in fair value that occur during a fiscal year are recognized as investment income reported for that fiscal year. Investment income includes interest earnings, changes in fair value, and any gains or losses realized upon the liquidation or sale of investments.

**4. Accounts Receivable**

The District extends credit to customers in the normal course of operations. Management deems all accounts receivable as collectible at year-end. Accordingly, an allowance for doubtful accounts has not been recorded.

**5. Property Taxes-Ad Valorem**

The Orange County Assessor's Office assesses all real and personal property within the County each year. The Orange County Tax Collector's Offices bills and collects the District's share of property taxes. The Orange County Treasurer's Office remits current and delinquent property tax collections to the District throughout the year. Property tax in California is levied in accordance with Article 13A of the State Constitution at one percent (1%) of countywide assessed valuations.

Property taxes receivable at year-end are related to property taxes collected by the Orange County which have not been credited to the District's cash balance as of June 30. The property tax calendar is as follows:

Lien date	January 1
Levy date	July 1
Due dates	November 10 and February 10
Collection dates	December 11 and April 11

**6. Prepaid Expenses**

Certain payments to vendors reflects costs or deposits applicable to future accounting periods and are recorded as prepaid items in the basic financial statements.

**7. Capital Assets**

Capital assets acquired and/or constructed are capitalized at historical cost. District policy has set the capitalization threshold for reporting capital assets at \$5,000. Donated assets are recorded at estimated fair market value at the date of donation. Upon retirement or other disposition of capital assets, the cost and related accumulated depreciation are removed from the respective balances and any gains or losses are recognized.

**El Toro Water District  
Notes to the Financial Statements, continued  
For the Fiscal Year Ended June 30, 2014**

**(1) Reporting Entity and Summary of Significant Accounting Policies, continued**

**D. Assets, Liabilities and Net Position, continued**

**7. Capital Assets, continued**

Depreciation is recorded on a straight-line basis over the estimated useful lives of the assets as follows:

	<u>Estimated Useful Life</u>
Building	25 to 40 years
Vehicles	5 to 25 years
Office furniture and equipment	5 to 10 years
Computer software	5 to 10 years
Land improvements	20 to 50 years
 Water Facilities:	
Reservoir	100 years
Transmission and distribution	20 to 60 years
Filtration plant	30 to 40 years
Other plant and equipment	5 to 15 years
 Sanitation Facilities:	
Collection and transmission	15 to 50 years
Treatment and disposal plant	15 to 30 years
Other plant and equipment	5 to 15 years

**8. Construction-in-Process**

The cost of acquisition and construction of major plant and equipment is recorded as construction in process (CIP). As facilities are constructed by the District and become operative, they are transferred from CIP to the plant and equipment accounts, or are expensed if determined that the cost does not meet the requirements of the capitalization policy.

**9. Compensated Absences**

The District's policy is to permit employees hired prior to July 1, 1997 to accumulate earned vacation up to a total of 160 hours and employees hired after July 1, 1997 to accumulate earned vacation up to a total of 240 hours, with amounts exceeding the limit being paid out as part of the employee's current regular compensation.

The District's sick leave policy is to permit employees to accumulate sick leave up to a total of 960 hours. At the end of each calendar year, any amounts exceeding the limit will be transferred to vacation time for employees hired prior to July 1, 1997 and paid out 50% to those hired after July 1, 1997 at the employee's current regular compensation rate. A factor of 5% times the number of complete years of employment will be applied to the hours accumulated over 960 hours to determine the number of hours to be transferred or paid out.

**10. Comparative Data**

Selected information regarding the prior year has been included in the accompanying financial statements. The information included in the accompanying financial statements for the prior year has been presented 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 District's prior year financial statements, from which this selected financial data was derived.

**El Toro Water District**  
**Notes to the Financial Statements, continued**  
**For the Fiscal Year Ended June 30, 2014**

**(1) Reporting Entity and Summary of Significant Accounting Policies, continued**

**11. Net Position**

The financial statements utilize a net position presentation. Net position is categorized as follows:

- **Net investment in capital assets** – This component of net position consists of capital assets, net of accumulated depreciation and reduced by any outstanding debt against the acquisition, construction or improvement of those assets.
- **Restricted Net Position** – This component of net position consists of constraints placed on net position use through external constraints imposed by creditors, grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.
- **Unrestricted Net Position** – This component of net position consists of the net amount of assets that are not included in the determination of *restricted* or *investment in capital assets, net of related debt*.

**12. Water Sales and Sewer Services**

Water sales and sewer services are billed on a monthly cyclical basis and recognize the respective revenues when they are earned.

**13. Capital Contributions**

Capital contributions represent cash and capital asset additions contributed to the District by property owners, granting agencies or real estate developers desiring services that require capital expenditures or capacity commitment.

**14. Capital and Operating Grants**

When a grant agreement is approved and eligible expenditures are incurred, the amount is recorded as a capital or operating grant receivable on the statement of net position and as capital grant contribution or operating grant revenue, as appropriate, on the statement of revenues, expenses and changes in net position.

**15. Budgetary Policies**

The District adopts an annual non-appropriated budget for planning, control, and evaluation purposes. Budgetary control and evaluation are affected by comparisons of actual revenues and expenses with planned revenues and expenses for the period. Encumbrance accounting is not used to account for commitments related to unperformed contracts for construction and services.

**El Toro Water District**  
**Notes to the Financial Statements, continued**  
**For the Fiscal Year Ended June 30, 2014**

**(2) Cash and Investments**

Cash and investments as of June 30, are classified in the accompanying financial statements as follows:

		<u>2014</u>
Cash and cash equivalents	\$	9,543,932
Investments		7,011,860
Restricted – cash and cash equivalents		<u>2,856,335</u>
Total cash and investments	\$	<u><u>19,412,127</u></u>

Cash and investments as of June 30, consist of the following:

		<u>2014</u>
Cash on hand	\$	700
Deposits with financial institutions		882,365
Investments		<u>18,529,062</u>
Total cash and investments	\$	<u><u>19,412,127</u></u>

***Investments Authorized by the California Government Code and the District's Investment Policy***

The table below identifies the investment types that are authorized by the District in accordance with the California Government Code (or the District's investment policy, where more restrictive). The table also identifies certain provisions of the California Government Code (or the District's investment policy, where more restrictive) 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>
U.S. Treasury obligations	5 years	None	None
Federal agency and bank obligations	5 years	None	None
Certificates-of-deposit (negotiable or placed)	1 year	30%	None
Commercial paper (prime)	270 days	10%	10%
Bankers Acceptance	180 days	15%	None
Money market mutual funds	N/A	10%	None
California Local Agency Investment Fund (LAIF)	N/A	\$30 million	None
California Asset Management Program (CAMP)	N/A	50%	None

***Investment in State Investment Pool***

The District is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by the California Government Code 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.

**El Toro Water District**  
**Notes to the Financial Statements, continued**  
**For the Fiscal Year Ended June 30, 2014**

**(2) Cash and Investments, continued**

***Investment in California Asset Management Program***

The California Asset Management Program (the CAMP) is a public joint powers authority which provides California Public Agencies with investment management services for surplus funds and comprehensive investment management, accounting and arbitrage rebate calculation services for proceeds of tax-exempt financings. The CAMP currently offers the Cash Reserve Portfolio, a short-term investment portfolio, as a means for Public Agencies to invest these funds. Public Agencies that invest in the Pool (Participants) purchase shares of beneficial interest. Participants may also establish individual, professionally managed investment accounts (Individual Portfolios) by separate agreement with the Investment Advisor. The District has a separate account with the Investment Advisor to manage part of the CAMP portfolio which consists of \$6,010,688 of United States Government Sponsored Agency Securities and \$1,001,172 of U.S. Treasury Obligations at June 30, 2014.

***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 purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio matures or comes close to maturity evenly over time as necessary to provide requirements for cash flow and liquidity needed for operations. Information about the sensitivity of the fair values of the District's investments to market interest rate fluctuations is provided by the following table that shows the distribution of the District's investments by maturity date:

Investments at June 30, 2014, consisted of the following:

<u>Investment Type</u>	<u>Amount</u>	<u>Remaining Maturity (in Months)</u>		
		<u>12 months or less</u>	<u>13 to 24 months</u>	<u>25-60 months</u>
United States Government Sponsored Agency Securities:				
Federal Home Loan Mortgage Corporation	\$ 1,002,201	1,002,201	-	-
Federal Home Loan Bank	5,008,487	1,000,691	3,007,193	1,000,603
U.S. Treasury Obligations	1,001,172	-	1,001,172	-
California Asset Management Program (CAMP)	1,829,037	1,829,037	-	-
Local Agency Investment Fund (LAIF)	9,688,165	9,688,165	-	-
<b>Total</b>	<b>\$ 18,529,062</b>	<b>13,520,094</b>	<b>4,008,365</b>	<b>1,000,603</b>

***Credit Risk***

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 table below is the minimum rating required by (where applicable) the California Government Code, the District's investment policy, or debt agreements, and the actual ratings, as reported by Standard and Poor's for each investment are as follows:

Credit ratings at June 30, 2014, consisted of the following:

<u>Investment Type</u>	<u>Amount</u>	<u>Minimum Legal Rating</u>	<u>Ratings</u>		
			<u>AAA</u>	<u>AA +</u>	<u>Unrated</u>
United States Government Sponsored Agency Securities:					
Federal Home Loan Mortgage Corporation	\$ 1,002,201	N/A	-	1,002,201	-
Federal Home Loan Bank	5,008,487	N/A	-	5,008,487	-
U.S. Treasury Obligations	1,001,172	N/A	-	1,001,172	-
California Asset Management Program (CAMP)	1,829,037	N/A	-	-	1,829,037
Local Agency Investment Fund (LAIF)	9,688,165	N/A	-	9,688,165	-
<b>Total</b>	<b>\$ 18,529,062</b>		<b>-</b>	<b>16,700,025</b>	<b>1,829,037</b>



**El Toro Water District**  
**Notes to the Financial Statements, continued**  
**For the Fiscal Year Ended June 30, 2014**

**(2) Cash and Investments, continued**

***Concentration of Credit Risk***

The District's investment policy contains no limitations on the amounts that can be invested in any one issuer as beyond that stipulated by the California Government Code. Investments in any one issuer (other than for external investment pools) that represent 5% or more of total District's investments at June 30, 2014 are as follows:

<u>Issuer</u>	<u>Investment Type</u>	<u>Amount</u>	<u>Percent</u>
Federal Home Loan Mortgage Corporation	United States Government Sponsored Agency Securities	\$ 1,002,201	5.41%
Federal Home Loan Bank	United States Government Sponsored Agency Securities	\$ 5,008,487	27.03%

***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 California Government Code and the District's investment policy does not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits, 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. Of the bank balances, up to \$250,000 held at each institution were federally insured and the remaining balance is collateralized in accordance with the Code; however, the collateralized securities are not held in the District's name.

The custodial credit risk for *investments* is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The Code and the District's investment policy contains legal and policy requirements that would limit the exposure to custodial credit risk for investments. With respect to investments, custodial credit risk generally applies only to direct investments in marketable securities. Custodial credit risk does not apply to a local government's indirect investment in securities through the use of mutual funds or government investment pools (such as LAIF).

The carrying amount of the District's cash deposits was \$564,243 at June 30, 2014. At June 30, 2014, total bank balances of deposits in the amount of \$577,567 were fully insured by the Federal Deposit Insurance or collateralized as required by California law.

**(3) Note Receivable – AMP (Allen – McColloch Pipeline)**

On July 1, 1994, El Toro Water District signed an agreement along with the Municipal Water District of Orange County (MWDOC) and several other participants for the sale of capacity rights in the Allen – McColloch Pipeline (AMP) to the Metropolitan Water District of Southern California (Metropolitan). The terms of the overall sale consisted of three components paid by (1) an initial payment of \$11,000,000, (2) \$59,800,000 to be paid in annual installments of \$4,600,000 plus interest commencing July 1, 1994 through and including July 1, 2006, and (3) principal and interest on the 1989 Certificates of Participation issued by MWDOC. The note was fully received in the fiscal year 2014.

**El Toro Water District**  
**Notes to the Financial Statements, continued**  
**For the Fiscal Year Ended June 30, 2014**

**(4) Capital Assets**

Major capital assets additions during the year include upgrades and extensions of the District's water and wastewater pumping, water transmission and distribution systems and plant facilities in the following schedules:

Changes in capital assets for the year ended June 30, 2014, were as follows:

	<u>Balance 2013</u>	<u>Additions/</u>	<u>Deletions/ Transfers</u>	<u>Balance 2014</u>
<b>Non-depreciable assets:</b>				
Land and land rights	\$ 7,451,586	-	-	7,451,586
Construction-in-process	14,522,547	22,990,259	(5,499,383)	32,013,423
<b>Total non-depreciable assets</b>	<u>21,974,133</u>	<u>22,990,259</u>	<u>(5,499,383)</u>	<u>39,465,009</u>
<b>Depreciable assets:</b>				
Capacity rights	342,382	-	-	342,382
Sources of supply	19,755,564	43,405	-	19,798,969
Pumping	11,787,446	5,049,683	-	16,837,129
Treatment	31,478,046	519,859	-	31,997,905
Transmission and collection	17,515,094	127,572	-	17,642,666
General plant facilities	11,698,130	200,985	-	11,899,115
<b>Total depreciable assets</b>	<u>92,576,662</u>	<u>5,941,504</u>	<u>-</u>	<u>98,518,166</u>
<b>Accumulated depreciation:</b>				
Capacity rights	(198,620)	(6,846)	-	(205,466)
Sources of supply	(8,918,232)	(367,614)	-	(9,285,846)
Pumping	(7,669,617)	(503,633)	-	(8,173,250)
Treatment	(20,112,096)	(1,069,001)	-	(21,181,097)
Transmission and collection	(8,004,170)	(363,138)	-	(8,367,308)
General plant facilities	(9,127,481)	(471,165)	-	(9,598,646)
<b>Total accumulated depreciation</b>	<u>(54,030,216)</u>	<u>(2,781,397)</u>	<u>-</u>	<u>(56,811,613)</u>
<b>Total depreciable assets, net</b>	<u>38,546,446</u>	<u>3,160,107</u>	<u>-</u>	<u>41,706,553</u>
<b>Total capital assets, net</b>	<u>\$ 60,520,579</u>	<u>26,150,366</u>	<u>(5,499,383)</u>	<u>81,171,562</u>

***Construction-In-Process***

The District is involved in various construction projects throughout the year. In 2014, the District started the recycled water expansion project. Once completed, projects are capitalized and depreciated over the life of the asset. The balance of construction-in-process was \$32,013,423 at June 30, 2014.

Construction-in-process consisted of the following projects as of June 30:

	<u>2014</u>
Recycled water distribution system expansion	\$ 20,040,271
Recycled water tertiary treatment plant	8,042,627
Baker water treatment plant	3,364,247
GIS/CMMS master plan	264,853
Effluent P.S. electrical improvement project	107,202
Various other projects	194,222
<b>Total construction-in-process</b>	<u>\$ 32,013,423</u>

**El Toro Water District**  
**Notes to the Financial Statements, continued**  
**For the Fiscal Year Ended June 30, 2014**

**(5) Compensated Absences**

Changes to compensated absences for 2014, were as follows:

	Balance 2013	Earned	Taken	Balance 2014	Current Portion	Long-term Portion
\$	1,220,984	509,317	(372,283)	1,358,018	339,505	1,018,514

**(6) Long-Term Debt**

Changes in long term debt at June 30, 2014 were as follows:

	2013	Additions	Principal Payments	2014
Installment payment agreements:				
Laguna Hills Company	\$ 427,542	-	(427,542)	-
Laguna Hills Sanitation, Inc.	194,336	-	(194,336)	-
Main extension contracts	6,180	-	-	6,180
State revolving fund loans:				
Wastewater treatment plant upgrade	2,708,107	-	(522,439)	2,185,668
Northline lift station improvement project	3,797,767	-	(155,606)	3,642,161
Recycled water treatment plant project	-	16,995,763	-	16,995,763
Baker water treatment plant	-	1,123,184	-	1,123,184
Total long-term debt	7,133,932	18,118,947	(1,299,923)	23,952,956
Less: current portion	(1,306,103)			(697,847)
Long-term portion	\$ 5,827,829			23,255,109

***Installment Payment Agreements***

The Installment Payment Agreements are the result of the acquisition of the Laguna Hills Water Company and the Laguna Hills Sanitation, Inc. The agreements provides for annual combined principal and interest payments of \$1,300,000. The payments are for 30 years, maturing on March 15, 2014 and include interest at 12% per annum. The outstanding balances were paid during the fiscal year 2014.

***Main Extension Contracts***

The Main Extension Contracts are payable to the developers without interest. The payments are based on a percentage of revenue received from units served by the water main. The contracts must be repaid in not more than 25 years, but may be paid off in advance at the option of the District. The outstanding balance at June 30, 2014 was \$6,180.

***State Revolving Fund Loan – Wastewater Treatment Plant Upgrade***

In December 1995, the District entered into an agreement with the California State Water Resources Control Board (SWRCB) for a Revolving Fund Loan (the Loan) in an amount of \$9,570,000 with an imputed interest rate of less than 1.50% per annum for the Wastewater Treatment Plant upgrade project. The loan is scheduled to mature in 2018. Principal and interest are payable annually on May 1<sup>st</sup> at a imputed interest rate of less than 1.5%.

Future annual debt service requirements on the loan are as follows:

Fiscal Year	Principal	Interest	Total
2015	\$ 531,859	39,408	571,267
2016	541,448	29,819	571,267
2017	551,211	20,056	571,267
2018	561,150	10,117	571,267
Total	\$ 2,185,668	99,400	2,285,068

**El Toro Water District  
Notes to the Financial Statements, continued  
For the Fiscal Year Ended June 30, 2014**

**(6) Long-Term Debt, continued**

***State Revolving Fund Loan – Northline Lift Station Improvement Project***

In October 2010, the District entered into an agreement with the California State Water Resources Control Board (SWRCB) for a State Revolving Fund Loan (Loan) in an amount of \$3,918,590. The loan carries an interest rate of 2.70% per annum for the Northline station improvement project. The loan is scheduled to mature in 2032. Principal and interest are payable annually on January 12<sup>th</sup> at the interest rate of 2.70%.

Future annual debt service requirements on the loan are as follows:

<u>Fiscal Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 159,808	98,338	258,146
2016	164,123	94,023	258,146
2017	168,554	89,592	258,146
2018	173,105	85,041	258,146
2019 - 2023	938,205	352,525	1,290,730
2024 - 2028	1,071,890	218,840	1,290,730
2029 - 2032	966,476	66,108	1,032,584
Total	<u>\$ 3,642,161</u>	<u>1,004,467</u>	<u>4,646,628</u>

***State Revolving Fund Loan – Recycled Water Treatment Plan Project***

In February 2013, the District entered into an agreement with the California State Water Resources Control Board (SWRCB) for a loan in an amount not-to-exceed \$28,327,037 with an interest rate of 1.70% per annum for the Recycled Water Treatment Plan project. As of June 30, 2014, eligible costs for reimbursement were \$16,995,763 and accrued as a long-term debt liability on the financial statements.

***Baker Water Treatment Plant Agreement***

In December 2013, the District entered into the Baker Water Treatment Plant Agreement, along with five other public entities relating to the Baker treatment plant. In January 2014, the District entered into an installment sale agreement with the Irvine Ranch Water District (IRWD) for the purchase of the District's portion of rights, title and interest to the capacity, not-to-exceed the amount of \$12,500,000. As of June 30, 2014, project funds were \$1,123,184 and accrued as a long-term debt liability on the financial statements.

**(7) Deferred Compensation Savings Plan**

The District contributes to the El Toro Water District Retirement Savings Plan and Trust (the Plan), which is qualified defined contribution pension plan under Section 401(a) and 401(k) of the Internal Revenue Code. The Plan is administered by the District.

As of December 1, 2005, the District executed an amendment to the Plan authorizing the District (as Employer) to match an amount equal to 50% of each participant's contributions to either 401(k) or 457 Plans, but no more than 12%. The District's contributions are limited to deposits toward the 401(k) plan.

In addition, the District contributes an amount equal to 9% of compensation for a plan year, for all qualified participants regardless of whether they are employee on the last day of the plan year, and regardless of whether they made any salary deferrals to the plan.

Federal law requires deferred compensation assets to be held in trust for the exclusive benefit of the participants. Accordingly, the District is in compliance with this legislation.

Therefore, these assets are not the legal property of the District, and are not subject to claims of the District's general creditors. Market value of the plan assets held in trust at June 30, 2014 was \$21,662,648.

**El Toro Water District  
Notes to the Financial Statements, continued  
For the Fiscal Year Ended June 30, 2014**

**(7) Deferred Compensation Savings Plan, continued**

The District has implemented GASB Statement No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*. Since the District has little administrative involvement and does not perform the investing function for this plan, the assets and related liabilities are not shown on the statement of net position.

**(8) Other Post-Employment Benefits Payable**

During the fiscal year ended June 30, 2009, the District implemented GASB Statement No. 45, which changed the accounting and financial reporting used by local government employers for other post-employment benefits (OPEB). Previously, the costs of such benefits were generally recognized as expenses of local government employers on a pay-as-you-go basis. The reporting requirements for these benefit programs as they pertain to the District are set forth below.

***Plan Description – Eligibility***

The District pays all or a portion of the cost of health insurance for retirees (including prescription drug benefits) under any group plan offered by the Association of California Water Agencies/Joint Powers Insurance Authority (ACWA/JPIA) Health Program, subject to certain restrictions as determined by the District.

Membership in the OPEB plan consisted of the following members as of June 30:

	2014
Active plan members	53
Retirees and beneficiaries receiving benefits	16
Separated plan members entitled to but not yet receiving benefits	-
	69
Total plan membership	69

***Plan Description – Benefits***

The District offers post employment medical benefits to retired employees who satisfy the eligibility rules. Certain spouses and surviving spouses are also eligible to receive benefits. Retirees may enroll in any medical plan available through the District's Association of California Water Agencies/Joint Powers Insurance Authority (ACWA/JPIA) Health Program, a cost-sharing multiple-employer medical coverage plan. The contribution requirements of eligible retired employees and the District are established and may be amended by the Board of Directors.

***Funding Policy***

The District is required to accrue the *Annual Required Contribution (ARC) of the Employer*, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The District will accrue a fixed contribution towards the cost of the post-employment benefit plan for those employees who meet the required service years for retirement from the District. The District funds the plan on a pay-as-you-go basis and maintains reserves (and records a liability) for the difference between pay-as-you-go and the actuarially determined ARC cost.

***Annual OPEB Cost and Net OPEB Obligation***

For the year ended June 30, 2014, the District's ARC cost was \$963,954. The District's net OPEB payable obligation amounted to \$3,394,636 for the year ended June 30, 2014. The District contributed \$130,211 in age adjusted contributions for current retiree OPEB premiums, for the year ended June 30, 2014.

**El Toro Water District  
Notes to the Financial Statements, continued  
For the Fiscal Year Ended June 30, 2014**

**(8) Other Post-Employment Benefits Payable, continued**

***Annual OPEB Cost and Net OPEB Obligation, continued***

The balance at June 30, consists of the following:	<u>2014</u>	
Annual OPEB expense:		
Annual required contribution (ARC)	\$	963,954
Interest on net OPEB obligation		104,295
Adjustment to annual required contribution		<u>(150,785)</u>
Total annual OPEB expense		917,464
Change in net OPEB payable obligation:		
Age adjusted contributions made		<u>(130,211)</u>
Total change in net OPEB payable obligation		787,253
OPEB payable – beginning of year		<u>2,607,383</u>
OPEB payable – end of year	\$	<u><u>3,394,636</u></u>

The District's annual OPEB cost, the percentage of the annual OPEB cost contributed to the Plan, and the net OPEB obligation for fiscal year 2014 and the three preceding years were as follows:

<u>Three-Year History of Net OPEB Obligation</u>					
Fiscal Year Ended	Annual OPEB Cost	Annual Contribution	% of Annual OPEB Cost Contributed	Net OPEB Obligation	
6/30/2012	\$ 700,970	121,180	17.29%	\$ 2,060,817	
6/30/2013	692,244	145,678	21.04%	2,607,383	
6/30/2014	917,464	130,211	14.19%	3,394,636	

See Page 26 for the Schedule of Funding Status.

***Actuarial Methods and Assumptions***

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. Calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and the pattern of sharing of costs between the employer and plan members to that point. Consistent with the long-term perspective of actuarial calculations, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities for benefits.

The following is a summary of the actuarial assumptions and methods:

Valuation date	July 1, 2013
Actuarial cost method	Projected unit credit
Amortization method	Level dollar
Remaining amortization period	30 Years as of the valuation date
Asset valuation method	30 Year smoothed market
Actuarial assumptions:	
Discount rate	4.0%
Project salary increase	3.0%
Inflation - discount rate	4.0%
Healthcare cost trend rate	8.0%

**El Toro Water District**  
**Notes to the Financial Statements, continued**  
**For the Fiscal Year Ended June 30, 2014**

**(9) Net Position**

Calculation of net position as of June 30, were as follows:	<u>2014</u>
Net investment in capital assets	
Capital assets – not being depreciated	\$ 39,465,009
Capital assets, net – being depreciated	41,706,553
Current:	
Loans payable	(697,847)
Non-current:	
Loans payable	<u>(23,255,109)</u>
<b>Total net investment in capital assets</b>	<u>57,218,606</u>
Restricted for debt service:	
Restricted – cash and cash equivalents	<u>2,856,335</u>
<b>Total restricted for debt service</b>	<u>2,856,335</u>
Unrestricted net position:	
Non-spendable net position:	
Materials and supplies inventory	597,528
Prepaid expenses and other deposits	<u>98,547</u>
Total non-spendable net position	<u>696,075</u>
Spendable net position are designated as follows:	
Operating reserve	<u>8,826,436</u>
Total spendable net position	<u>8,826,436</u>
<b>Total unrestricted net position</b>	<u>9,522,511</u>
<b>Total net position</b>	<u>\$ 69,597,452</u>

**(10) Risk Management**

The District is exposed to various risks of loss related to torts, theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District is a member of the Association of California Water Agencies/Joint Powers Insurance Authority (ACWA/JPIA), an intergovernmental risk sharing joint powers authority created to provide self-insurance programs for California water agencies. The purpose of the ACWA/JPIA is to arrange and administer programs of self-insured losses and to purchase excess insurance coverage. At June 30, 2014, the District participated in the liability and property programs of the ACWA/JPIA as follows:

- General and auto liability, public officials and employees' errors and omissions: Total risk financing self-insurance limits of \$2,000,000, combined single limit at \$2,000,000 per occurrence. The JPIA purchases additional excess coverage layers: \$60 million per occurrence for general, auto and public officials liability, which increases the limits on the insurance coverage noted above.

**El Toro Water District  
Notes to the Financial Statements, continued  
For the Fiscal Year Ended June 30, 2014**

**(10) Risk Management, continued**

In addition to the above, the District also has the following insurance coverage:

- Employee dishonesty coverage up to \$1,500,000 with a \$5,000 deductible per loss includes public employee dishonesty, forgery or alteration and theft, disappearance and destruction coverage.
- Property loss coverage is up to \$100,000,000 with a \$1,000 deductible; the ACWA/JPIA is self-insured up to \$50,000 and excess insurance has been purchased.
- Underground Storage Tank Pollution Liability, the District is insured up to \$1,000,000 with a \$10,000 deductible; the Authority is self-insured up to \$500,000 and excess insurance coverage has been purchased to cover losses ranging from \$500,000 to \$1,000,000.
- Dam failure liability coverage up to \$20.0 million per occurrence; the ACWA/JPIA is self-insured up to \$50,000 and excess insurance coverage has been purchased.
- Workers' compensation insurance up to California statutory limits for all work related injuries/illnesses covered by California law. The ACWA/JPIA is self-insured up to \$2.0 million and excess insurance coverage has been purchased.

Settled claims have not exceeded any of the coverage amounts and there were no reductions in the District's insurance coverage during the year ending June 30, 2014. Liabilities are recorded when it is probable that a loss has been incurred, and the amount of the loss can be reasonably estimated net of the respective insurance coverage.

Liabilities include an amount for claims that have been incurred but not reported (IBNR). There was no IBNR claims payable as of June 30, 2014.

**(11) Governmental Accounting Standards Board Statements Issued, Not Yet Effective**

The Governmental Accounting Standards Board (GASB) has issued several pronouncements prior to June 30, 2014, that has effective dates that may impact future financial presentations.

***Governmental Accounting Standards Board Statement No. 68***

In June 2012, the GASB issued Statement No. 68 – *Accounting and Financial Reporting for Pensions— an amendment of GASB Statement No. 27*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency.

This Statement replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, as well as the requirements of Statement No. 50, *Pension Disclosures*, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements 27 and 50 remain applicable for pensions that are not covered by the scope of this Statement. The provisions of Statement 68 are effective for fiscal years beginning after June 15, 2014. The impact of the implementation of this Statement to the District's financial statements has not been assessed at this time.



**El Toro Water District**  
**Notes to the Financial Statements, continued**  
**For the Fiscal Year Ended June 30, 2014**

**(11) Governmental Accounting Standards Board Statements Issued, Not Yet Effective, continued**

***Governmental Accounting Standards Board Statement No. 69***

In January 2013, the GASB issued Statement No. 69 – *Government Combinations and Disposals of Government Operations*. The objective of this Statement is to provide new accounting and financial reporting standards for government mergers and acquisitions and for government operations that have been transferred or sold. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2013. The impact of the implementation of this Statement to District's financial statements has not been assessed at this time.

***Governmental Accounting Standards Board Statement No. 71***

In November 2013, the GASB issued Statement No. 71 – *Pension Transition for Contributions made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68*. The objective of this Statement is to address an issue regarding application of the transition provisions of Statement No. 68, *Accounting and Financial Reporting for Pensions*. The issue relates to amounts associated with contributions, if any, made by a state or local government employer or non-employer contributing entity to a defined benefit pension plan after the measurement date of the government's beginning net pension liability. The provisions of this Statement are required to be applied simultaneously with the provisions of GASB Statement No. 68. The impact of the implementation of this Statement to District's financial statements has not been assessed at this time.

**(12) Commitments and Contingencies**

***Construction Contracts***

The District has a variety of agreements with private parties relating to the installation, improvement or modification of water and wastewater facilities and distribution systems within its service area. The financing of such construction contracts is being provided primarily from the District's replacement reserves and capital contributions.

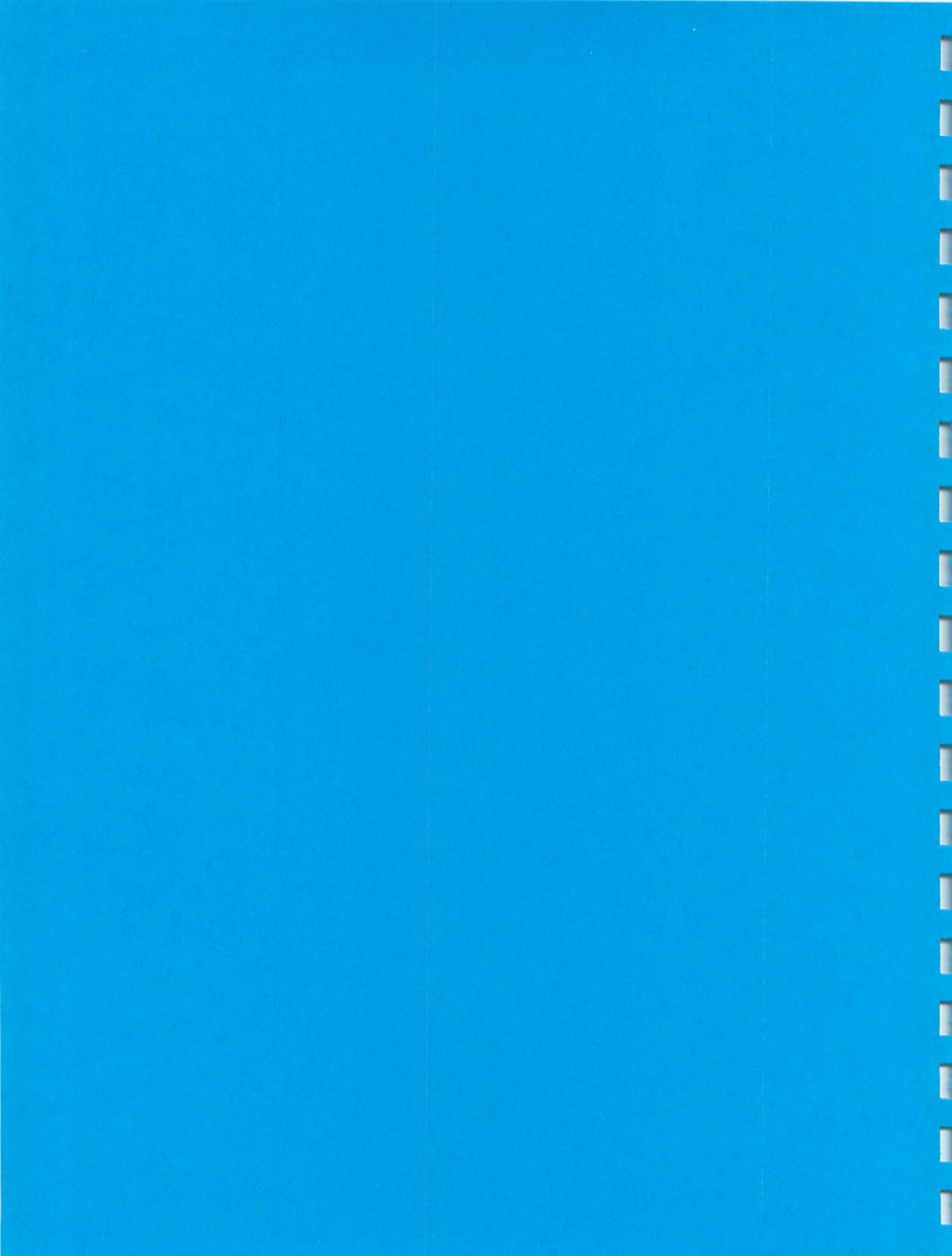
***Litigation***

In the ordinary course of operations, the District is subject to claims and litigation from outside parties. After consultation with legal counsel, the District believes the ultimate outcome of such matters, if any, will not materially affect its financial condition.

**(13) Subsequent Events**

Events occurring after June 30, 2014, have been evaluated for possible adjustment to the financial statements or disclosure as of October 10, 2014, which is the date the financial statements were available to be issued. The District is not aware of any subsequent events that would require recognition or disclosure in the financial statements.

## **Required Supplementary Information**



**El Toro Water District  
Schedule of Funding Status  
For the Fiscal Years Ended June 30, 2014**

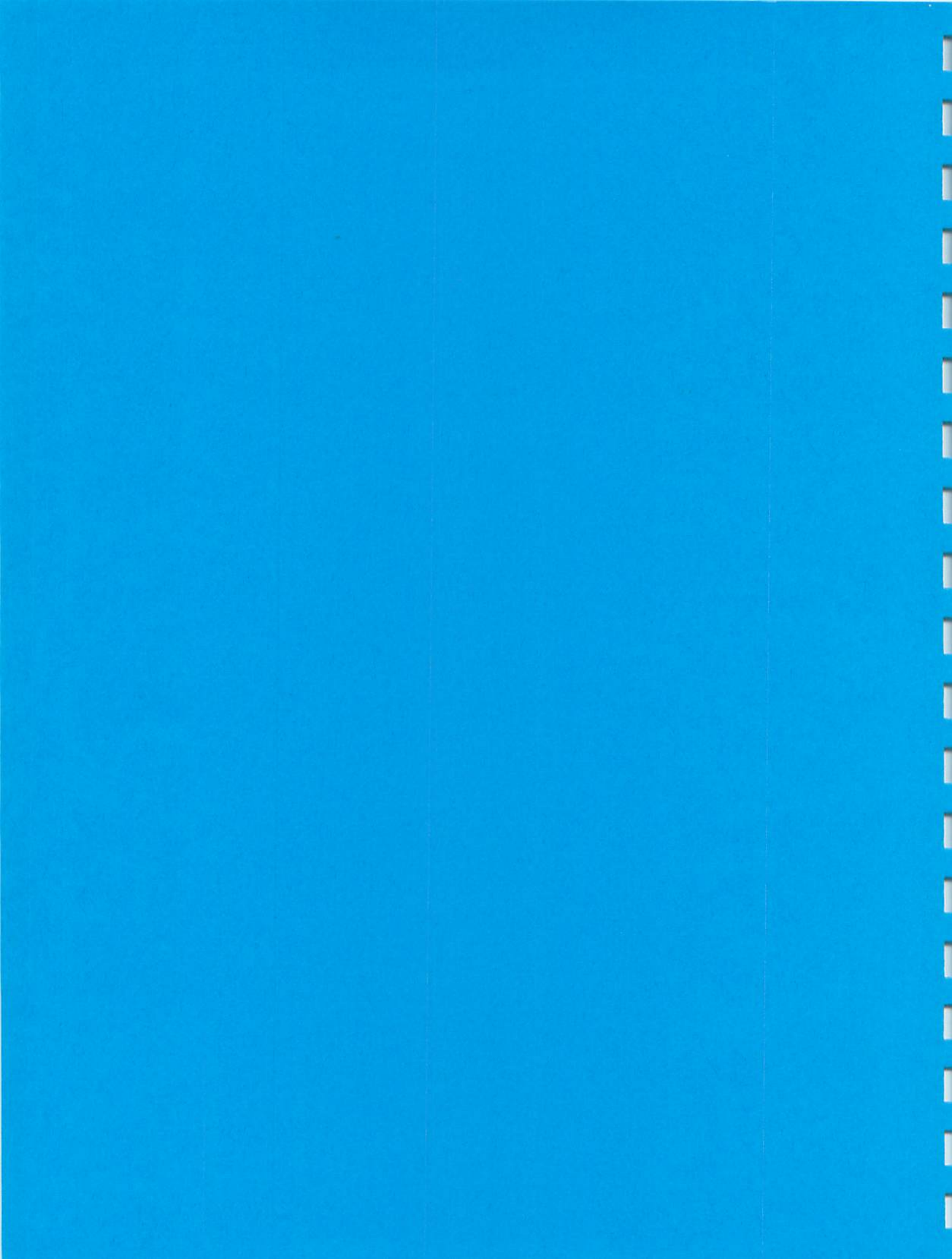
**(1) Other Post-Employment Benefits Payable**

<u>Actuarial Valuation Date</u>	<u>Actuarial Asset Value</u>	<u>Actuarial Accrued Liability Entry Age</u>	<u>Unfunded Actuarial Accrued Liability</u>	<u>Funded Ratio</u>	<u>Covered Payroll</u>	<u>Unfunded Actuarial Liability as Percentage of Covered Payroll</u>
7/1/2007	\$ -	4,398,864	4,398,864	0.0%	4,200,911	104.71%
7/1/2010	-	6,244,208	6,244,208	0.0%	5,366,236	116.36%
7/1/2013	-	9,358,165	9,358,165	0.0%	4,058,095	230.60%

Funding progress is presented for the year(s) that an actuarial study has been prepared since the effective date of GASB Statement 45. Actuarial review and analysis of the post-employment benefits liability and funding status is performed every three years or annually, if there are significant changes in the plan. The next scheduled actuarial review and analysis of the post-employment benefits liability and funding status will be performed in fiscal year 2017, based on the year ending June 30, 2016.

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# **Report on Internal Controls and Compliance**





Charles Z. Fedak, CPA, MBA  
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## **Independent Auditor's Report on Internal Controls Over Financial Reporting And on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards***

Board of Directors  
El Toro Water District  
Lake Forest, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the El Toro Water District (District) as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprises the District's basic financial statements, and have issued our report thereon dated October 10, 2014.

### **Internal Control Over Financial Reporting**

In planning and performing our audits of the financial statements, we considered the District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audits, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.



**Independent Auditor's Report on Internal Controls Over Financial Reporting  
And on Compliance and Other Matters Based on an Audit of Financial Statements  
Performed in Accordance with *Government Auditing Standards*, (continued)**

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the District's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Charles Z. Fedak & Company, CPAs - An Accountancy Corporation*

**Charles Z. Fedak & Company, CPAs - An Accountancy Corporation**  
Cypress, California  
October 10, 2014