

**EAST PALO ALTO SANITARY DISTRICT
BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013**

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**EAST PALO ALTO SANITARY DISTRICT
BASIC FINANCIAL STATEMENTS
For the Years Ended June 30, 2013**

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
East Palo Alto Sanitary District
East Palo Alto, California

Report on Financial Statements

We have audited the accompanying financial statements of the East Palo Alto Sanitary District (District) as of and for the year ended June 30, 2013, 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 prior year financial statements were audited by other auditor whose report dated November 6, 2012 was unqualified.

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 the financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District as of June 30, 2013, and changes in financial position and, cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of Matters

Management adopted the provisions of Governmental Accounting Standards Board Statement 63 - *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* which became effective during the year ended June 30, 2013 and changed certain statement titles and nomenclature in the financial statements.

The emphasis of this matter does not constitute a modification to our opinion.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with 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.



Pleasant Hill, California
December 17, 2013

**EAST PALO ALTO SANITARY DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2013**

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements are comprised of two components: 1) the financial statements and 2) notes to the financial statements that explain in more detail some of the information in the financial statements.

Required Financial Statements

The financial statements of the District report information about the District using accounting methods similar to those used by private-sector companies. These statements provide both long term and short-term information about the District's overall financial status.

The Statement of Net Position presents information on all of the District's assets and liabilities, with the difference between the two reported as net position. This statement provides information about the nature and the amounts of investments in resources (assets) and the obligations to District creditors (liabilities). It provides one way to measure the financial health of the District by providing the basis for evaluating the capital structure of the District and assessing the liquidity and financial flexibility of the District. However, there are several outside nonfinancial factors that need to be considered; such as changing economic conditions, population and customer growth, and new or changed rules and regulations.

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 whether the District has successfully recovered all its cost through its user fees.

The final required statement is the Statement of Cash Flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. This statement provides answers to such questions as where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period.

Financial Analysis of the District

As previously noted, net position may serve over time as a useful indicator of an entity's financial position. In the case of the District, assets exceeded liabilities by \$14,045,252 at the close of the most recent fiscal year. As can be seen in Table A , on the next page, the largest portion of the District's net position (27%) reflect its investment in capital assets (e.g., sewers, buildings, machinery and equipment), less any related debt used to acquire those assets that is still outstanding. These capital assets are used primarily in the collection and treatment of wastewater throughout the District's service area. The related debt will be repaid with resources provided by system users through rates and fees.

**EAST PALO ALTO SANITARY DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2013**

**Table A
Summary of Net Position**

A summary of the statements of net position as of June 30, 2013 and 2012 is shown in the following table:

	<u>2013</u>	<u>2012</u>	<u>Change</u>
Current assets	\$ 10,311,237	\$ 9,289,573	\$ 1,021,664
Noncurrent assets	99,357	112,520	(13,163)
Net capital assets	<u>6,189,693</u>	<u>6,279,949</u>	<u>(90,256)</u>
Total assets	<u>16,600,287</u>	<u>15,682,042</u>	<u>918,245</u>
Current liabilities	496,498	488,384	8,114
Noncurrent liabilities	<u>2,058,537</u>	<u>2,321,601</u>	<u>(263,064)</u>
Total liabilities	<u>2,555,035</u>	<u>2,809,985</u>	<u>(254,950)</u>
Net position	<u>\$ 14,045,252</u>	<u>\$ 12,872,057</u>	<u>\$ 1,173,195</u>

Net position increased \$1,173,195 in 2013. The increases are a combination of income in the form of connection fees, assessments, and other income.

Current assets increased by \$1,021,664 compared to the prior year primarily due to:

- An increase in cash of \$1,030,724 as detailed in the statement of cash flows on page 10.

Noncurrent assets decreased \$13,163 primarily due to amortization expenses and a decrease in notes receivable.

Current liabilities increased by \$8,114 due to an increase in accounts payable of \$32,177, decrease in accrued liabilities of \$43,693 and an increase in current portion of long term debt of \$19,630.

**EAST PALO ALTO SANITARY DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2013**

**Table B
Summary of Revenues
Expenses and Changes in Net Position**

	<u>2013</u>	<u>2012</u>	<u>Change</u>
Total operating revenues	\$ 4,130,107	\$ 4,874,888	\$ (744,781)
Total operating expenses	<u>(3,860,449)</u>	<u>(3,550,562)</u>	<u>(309,887)</u>
Operating Income (loss)	269,658	1,324,326	(1,054,668)
Total nonoperating revenues and expenses	<u>903,537</u>	<u>271,092</u>	<u>632,445</u>
Increase in net position	1,173,195	1,595,418	(422,223)
Net position, beginning of year	<u>12,872,057</u>	<u>11,276,639</u>	<u>1,595,418</u>
Net position, end of year	<u><u>\$ 14,045,252</u></u>	<u><u>\$ 12,872,057</u></u>	<u><u>\$ 1,173,195</u></u>

While the Summary of Net Position (Table A) shows the change in of net position, (Table B) shows the Summary of Revenues, Expenses, and Changes in Net Position and provides details as to the nature and source of these changes.

Table B shows that during 2013 total operating revenues decreased by \$744,781. Operating expenses increased by \$309,887. Non operating revenue and expenses increased by \$632,445. The major factors which contributed to these results include:

- The decrease in operating revenues of \$744,781 was primarily the result of not receiving a miscellaneous reimbursement for a designated capital project.
- The increase in operating expenses of \$309,887 was due to a decrease in personnel services of \$169,716, an increase in purchased services of \$508,041, a decrease in depreciation of \$5,803 and a decrease in other expenses of \$22,635.
- The increase of \$632,445 in non-operating revenues and expenses was due to an increase in interest income of \$ 5,613, an increase in property tax collections of \$157,217, an increase in interest expense of \$641, and an increase in other revenue of \$470,256.

**EAST PALO ALTO SANITARY DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2013**

BUDGETARY HIGHLIGHTS

The District has an annual operating budget that is approved by its Board of Directors. Capital projects are approved on a project by project basis within the annually approved capital budget. The 2013 expenses were under the approved budget.

The District Engineer is currently preparing a revised 10-year Sewer Master Plan which will identify and propose a master schedule for future sewer rehabilitation and replacement projects.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

As of June 30, the District's investment in capital assets amounted to \$6.19 million and \$6.28 million (net of accumulated depreciation) as shown in Table C for 2013 and 2012, respectively. In 2013, the District spent \$133,134 on Cured in place pipe, \$43,695 on building renovations and \$12,382 on furniture.

**Table C
Capital Assets**

	2013	2012	Change
Land	\$ 184,601	\$ 184,601	\$ -
Cured in place pipe	1,474,518	1,341,384	\$ 133,134
Sewer collection facilities	5,582,702	5,582,702	\$ -
Buildings	2,388,217	2,344,522	\$ 43,695
Furniture and equipment	1,904,045	1,891,663	\$ 12,382
Accumulated depreciation	(5,344,390)	(5,064,923)	(279,467)
Net capital assets	<u>\$ 6,189,693</u>	<u>\$ 6,279,949</u>	<u>\$ (90,256)</u>

**EAST PALO ALTO SANITARY DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2013**

Debt Administration

The District has financed its construction program primarily through the issuance of revenue bonds. Additional information on the District's long-term debt can be found in Note 5 to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The service area of the District is best described as mature. The District is not in a growth situation but one in which the system is continually televised, upgraded and repaired on an as-needed basis.

Requests for Information

The financial report is designed to provide a general overview of the District's finances and operations for all those with an interest in the District's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

Office of the General Manager
East Palo Alto Sanitary District
901 Weeks Street
East Palo Alto, CA 94303

EAST PALO ALTO SANITARY DISTRICT
STATEMENT OF NET POSITION
JUNE 30, 2013

ASSETS

Current Assets:

Cash and investments (Note 2)	\$10,294,174
Prepaid insurance	17,063
Total Current Assets	<u>10,311,237</u>

Noncurrent Assets:

Notes receivable	36,782
OPEB asset (Note 10)	16,430
Other assets	<u>46,145</u>

Capital assets (Note 3):

Land	184,601
Sewer collection facilities	5,582,702
Cured in place pipe	1,474,518
Buildings	2,388,217
Furniture and equipment	1,904,045
Less accumulated depreciation	<u>(5,344,390)</u>
Total capital assets, net	<u>6,189,693</u>

Total Non-Current Assets	<u>6,289,050</u>
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TOTAL ASSETS	<u>16,600,287</u>
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LIABILITIES

Current Liabilities

Accounts payable	50,677
Accrued liabilities	51,865
Long-term debt, current portion (Note 5)	<u>393,956</u>
Total Current Liabilities	<u>496,498</u>

Noncurrent Liabilities

Long-term debt (Note 5)	<u>2,058,537</u>
Total Long-Term Liabilities	<u>2,058,537</u>
Total Liabilities	<u>2,555,035</u>

NET POSITION (Note 8)

Net investment in capital assets	3,737,200
Unrestricted	<u>10,308,052</u>
Total Net Position	<u><u>\$14,045,252</u></u>

See accompanying notes to financial statements

EAST PALO ALTO SANITARY DISTRICT
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2013

OPERATING REVENUES:

Sewer service charges	\$4,109,771
Other revenues	<u>20,336</u>
Total Operating Revenues	<u>4,130,107</u>

OPERATING EXPENSES:

Personnel services	1,230,565
Purchased services	2,039,568
Utilities, fuel and supplies	71,545
Depreciation and amortization	305,212
Other expenses	<u>213,559</u>
Total Operating Expenses	<u>3,860,449</u>

NET OPERATING INCOME	<u>269,658</u>
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NONOPERATING REVENUE (EXPENSE)

Property taxes	472,635
Pass through receipts	417,522
Interest income	66,514
Interest expense	(105,868)
Other revenue	<u>52,734</u>
Nonoperating revenue, net	<u>903,537</u>

CHANGES IN NET POSITION	1,173,195
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NET POSITION AT BEGINNING OF YEAR	<u>12,872,057</u>
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NET POSITION AT END OF YEAR	<u><u>\$14,045,252</u></u>
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See accompanying notes to financial statements

EAST PALO ALTO SANITARY DISTRICT
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2013

CASH FLOWS FROM OPERATING ACTIVITIES	
Receipts from customers and users	\$4,156,230
Payments to suppliers	(2,353,251)
Payments to employees	<u>(1,230,565)</u>
Cash Flows provided by Operating Activities	<u>572,414</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
Property taxes	472,635
Pass through receipts	<u>417,522</u>
Net Cash Flows provided by Noncapital Financing Activities	<u>890,157</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Acquisition and construction of capital assets	(189,211)
Principal paid on debt	(379,977)
Proceeds from SRF loan	136,543
Interest paid on debt	(105,868)
Payment of note receivable	3,848
Other	<u>36,304</u>
Cash Flows provided (used) by Capital and Related Financing Activities	<u>(498,361)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:	
Interest received	<u>66,514</u>
Cash Flows from Investing Activities	<u>66,514</u>
NET CASH FLOWS	1,030,724
Cash and cash equivalents at beginning of year	<u>9,263,450</u>
Cash and cash equivalents at end of year	<u><u>\$10,294,174</u></u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES	
Operating income	\$269,658
Adjustment to reconcile operating income to net cash provided (used) by operating activities:	
Depreciation and amortization expense	305,212
Change in assets and liabilities:	
Receivables, net	26,123
Prepaid expenses	(17,063)
Accounts payable and accrued expenses	<u>(11,516)</u>
Net cash provided by operating activities	<u><u>\$572,414</u></u>

See accompanying notes to financial statements

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. *Description of the Reporting Entity*

The financial statements of East Palo Alto Sanitary District (District) include the financial activities of the District as well as the financial activity of the East Palo Alto Sanitary District Financing Corporation (Corporation), a component unit of the District. The Corporation is a nonprofit public benefit corporation established in fiscal year 1991 to provide financial assistance to the District by financing improvements to the District's sewer collection system and to refinance the purchase and renovation of the District's administration building. The Corporation has no employees. The District is governed by a five member Board of Directors elected at large to four year terms by residents within the District. These Directors also serve as Directors of the Corporation.

B. *Basis of Presentation and Accounting*

Basic Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America. The Governmental Accounting Standards Board is the acknowledged standard setting body for establishing accounting and financial reporting standards followed by governmental entities in the United States.

These Standards require that the financial statements described below be presented.

The Statement of Net Position and the Statement of Activities display information about the East Palo Alto Sanitary District. Business-type activities are financed in whole or in part by fees charged to external parties.

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as interest income and connection fees, result from nonexchange transactions or ancillary activities.

Enterprise funds are accounted for on the flow of economic resources measurement focus utilizing full accrual accounting. Under this method, assets and revenues are recorded when earned, and liabilities and expenses are recorded when the related obligations are incurred.

C. *Budgets and Budgetary Accounting*

East Palo Alto Sanitary District adopts an operating budget at the beginning of each year for the following fiscal year. The District General Manager is authorized to transfer any unencumbered amounts from one department to another within the same major account and to transfer any unencumbered appropriation from one line item account to another within the same major account. The major accounts are defined as salaries and employee benefits, maintenance and operation, capital outlay and reserves. Any additional appropriations require approval by the Board of Directors.

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Cash and Cash Equivalents

For purposes of the statement of cash flows, cash equivalents include time deposits, certificates of deposit, and all highly liquid debt instruments with original maturities of three months or less.

E. Compensated Absences

The District records the expense of employees' vacation and sick leave benefits in the period in which they accumulate and become vested. At June 30, 2013, the balance is \$40,481, and is included in Accrued Liabilities on the Statement of Net Position.

F. Capital Assets

The cost of additions to utility plant and major replacements of property is capitalized. Costs include material, direct labor, transportation and indirect items such as interest, engineering, supervision and employee fringe benefits. Contributed property is recorded at estimated fair market value at time of acquisition. Capital assets are defined by the District as assets with an initial, individual cost of more than \$500 and an estimated useful life in excess of one year.

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

Sewer collection facilities	50 years
Building	30 years
Furniture and Equipment	10 years
Computers	5 years

G. Sewer Service Charges

Sewer service charges are billed and collected, on behalf of the District, by San Mateo County (the County) as a separate component of semi-annual property tax billings. Property taxes are levied on March 1 and are due in equal installments on November 1 and February 1. The County remits all amounts due, under the Teeter Plan.

H. Sewer Connection Fees

Connection fees represent a one-time contribution of resources to the District imposed on contractors and developers for the purpose of financing growth-related construction and improvements. Connection fees are recognized as other non-operating revenues in the statement of revenues, expenses and changes in net position. Any cumulative fees collected in excess of amounts expended are shown as restricted net position.

I. Bond Issuance Costs

Bond issuance costs are recorded as an asset and are amortized on straight-line basis over the life of the related debt issue.

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

J. *Use of Estimates*

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

K. *Implementation of Governmental Accounting Standards Board (GASB) Statements*

GASB Statement No. 60 – In November 2010, the GASB issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*. The objective of this Statement is to improve financial reporting by addressing issues related to service concession arrangements (SCAs), which are a type of public-private or public-public partnerships. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2011. This Statement had no impact on the District's financial statements for fiscal year ending June 30, 2013.

GASB Statement No. 61 – In November 2010, the GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus – an amendment of GASB Statements No. 14 and No. 34*. The objective of this Statement is to improve financial reporting for a governmental financial reporting entity. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2012. This Statement did not have a material impact on the District's financial statements for fiscal year ending June 30, 2013.

GASB Statement No. 62 – In December 2010, the GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The objective of this Statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the FASB and AICPA pronouncements, which does not conflict with or contradict GASB pronouncements. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2011. This Statement did not have a material impact on the District's financial statements for fiscal year ending June 30, 2013.

GASB Statement No. 63 – In June 2011, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. This Statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources. In addition to assets, the statement of financial position or balance sheet will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position or fund balance that applies to a future period(s) and so will *not* be recognized as an outflow of resources (expense/expenditure) until then. In addition to liabilities, the statement of financial position or balance sheet will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of net position or fund balance that applies to a future period(s) and so will *not* be recognized as an inflow of resources (revenue) until that time.

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2011. This Statement changed certain financial statement titles and nomenclature on the District's financial statements for fiscal year ending June 30, 2013.

NOTE 2 – CASH AND INVESTMENTS

A. *Policies and Classification*

California Law requires banks and savings and loan institutions to pledge government securities with a market value of 110% of the District's cash on deposit, or first trust deed mortgage notes with a market value of 150% of the deposit, as collateral for these deposits. Under California Law this collateral is held in a separate investment pool by another institution in the District's name and places the District ahead of general creditors of the institution.

The District's investments are carried at fair value, as required by generally accepted accounting principles. The District adjusts the carrying value of its investments to reflect their fair value at each fiscal year end, and it includes the effects of these adjustments in income for that fiscal year.

The District's cash and investments consist of the following at June 30, 2013:

Deposits with financial institutions	\$86,711
Cash and investments with San Mateo County Treasurer	<u>10,207,463</u>
Total cash and investments	<u><u>\$10,294,174</u></u>

The District has authorized staff to invest cash with the San Mateo County Treasurer in a series of pooled accounts with cash from various other governmental entities within the County, for investment purposes. The County's investment policies are governed by State statutes. In addition, the County has an investment committee, which prescribes written investment policies regarding the types of investments that may be made. The policies limit amounts that may be invested in any one financial institution or amounts, which may be invested in long-term instruments. Interest earned from such time deposits and investments is allocated quarterly to the District based on its average daily cash balances. The fair value of the account at June 30, 2013 was provided by the County Treasurer.

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 3 – CAPITAL ASSETS

Changes in property, plant and equipment accounts are summarized below:

	Balance at June 30, 2012	Additions	Transfers	Balance at June 30, 2013
Capital assets not being depreciated:				
Land	\$184,601			\$184,601
Construction in Progress	1,341,384	\$133,134	(\$1,474,518)	
Total capital assets not being depreciated	1,525,985	133,134	(1,474,518)	184,601
Capital assets being depreciated:				
Sewer collection facilities	5,582,702			5,582,702
Cured in place pipe			1,474,518	1,474,518
Buildings	2,344,522	43,695		2,388,217
Furniture and equipment	1,891,663	12,382		1,904,045
Total capital assets being depreciated:	9,818,887	56,077	1,474,518	11,349,482
Less accumulated depreciation for:				
Sewer collection facilities	2,358,144	111,654		2,469,798
Cured in place pipe		48,411		48,411
Buildings	1,247,819	87,711		1,335,530
Furniture and equipment	1,458,960	31,691		1,490,651
Total accumulated depreciation	5,064,923	\$279,467		5,344,390
Net capital assets being depreciated	4,753,964			6,005,092
Total Capital Assets, net	\$6,279,949			\$6,189,693

NOTE 4 – CAPACITY RIGHTS IN TREATMENT PLANT

The District has a contract with the City of Palo Alto whereby the District has rights to a specified capacity (11.90%) of the capacity of their sewage treatment facilities. The carrying value of such rights represents the District's share of construction costs relating to expansion and improvements of the City's treatment plant, net of amortization. The District is amortizing such cost (\$85,421 per year) over twenty five years, the approximate life of the treatment plant.

The District is also required to pay a portion of the operating cost on an annual basis for the treatment of the sewage. For the year ending June 30, 2013, such annual operating cost was \$75,566.

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 5 – LONG-TERM DEBT

A. Current Year Transactions and Balances

Long-term debt at June 30, 2013 is summarized as follows:

	Original Issue Amount	Balance June 30, 2012	Additions	Retirements	Balance June 30, 2013	Amount due within one year
2000 Installment sale of bonds						
5.75%, due 10/01/2014	\$3,070,500	\$772,100		\$243,100	\$529,000	\$257,100
Palo Alto 1990 Utility Revenue Bonds						
5.75%, due 6/30/2024	469,595	289,856		16,741	273,115	19,159
Palo Alto 2000 Utility Revenue Bonds						
5.75%, due 6/30/2024	573,000	356,788		22,745	334,043	23,302
Vactor Truck Note						
4.75%, due 3/31/2016	270,000	188,306		43,815	144,491	45,921
State Revolving Fund Loan						
2.60%, due 1/31/32	1,225,420	1,088,877	\$136,543	53,576	1,171,844	48,474
Total Long-Term Debt		2,695,927	\$136,543	\$379,977	2,452,493	\$393,956
Less:						
Amount due within one year		(374,326)			(393,956)	
Total Long-Term Debt, net		\$2,321,601			\$2,058,537	

B. 2000 Installment Sale of Bonds

Represents indebtedness to Municipal Leasing Associates, Inc. in connection with the discharge of a 1990 Installment Sale Agreement used to finance the acquisition and construction of the District's sewer system improvements. The bonds are payable from revenues of the District.

C. Palo Alto 1990 Utility Revenue Bonds

Represents the District's portion of the City of Palo Alto's (City) debt related to the treatment plant (see Note 4). The District is liable to the City for this debt as long as the District utilizes the City's treatment plant. The bonds are payable from revenues of the District.

D. Palo Alto 2000 Utility Revenue Bonds

Represents a portion of the Palo Alto 1990 Utility Revenue Bonds which was refinanced. The bonds are payable from revenues of the District.

E. Vactor Truck Note

Represents a note with Municipal Finance Corporation for the purchase of a sewer vacuum truck. This note is payable from revenues of the District.

F. State Revolving Fund Loan

Represents a loan from the State Water Resources Control Board to finance the construction of the Cured in Place Siphoning Project. This loan is payable from revenues of the District.

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 5 – LONG-TERM DEBT (Continued)

G. Debt Service Requirements

For The Year Ending June 30	Principal	Interest	Total
2014	\$393,956	\$91,303	\$485,259
2015	414,367	70,503	484,870
2016	148,260	56,839	205,099
2017	101,488	51,370	152,858
2018	105,590	47,432	153,022
2019 - 2023	592,178	172,080	764,258
2024 - 2028	400,392	68,391	468,783
2029 - 2032	296,262	19,504	315,766
Total payments due	<u>\$2,452,493</u>	<u>\$577,422</u>	<u>\$3,029,915</u>

NOTE 9 – DEFINED BENEFIT PENSION PLAN

Substantially all District employees are eligible to participate in pension plans offered by California Public Employees Retirement System (CALPERS), an agent multiple employer defined benefit pension plan which acts as a common investment and administrative agent for its participating member employers. CALPERS provides retirement and disability benefits, annual cost of living adjustments and death benefits to plan members, who must be public employees and beneficiaries. The District's employees participate in the Miscellaneous Plan. Benefit provisions under the Plan are established by State statute and District resolution. Benefits are based on years of credited service, equal to one year of full time employment. Funding contributions for the Plan are determined annually on an actuarial basis as of June 30 by CALPERS; the District must contribute these amounts. The District's labor contracts require it to pay employee contributions as well as its own. The Plans' provisions and benefits in effect at June 30, 2013, are summarized as follows:

	<u>Miscellaneous</u>
Benefit vesting schedule	5 years service
Benefit payments	monthly for life
Retirement age	50
Monthly benefits, as a % of annual salary	2.0 - 2.7%
Required employee contribution rates	8%
Required employer contribution rates	17.523%
Annual pension cost, all paid	\$156,582

Assembly Bill (AB) 340 pension reform created the Public Employees' Pension Reform Act (PEPRA) that implemented new benefit formulas and final compensation period, as well as new contribution requirements for new employees hired on or after January 1, 2013 who meet the definition of new member under PEPRA.

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 9 – DEFINED BENEFIT PENSION PLAN (Continued)

The bill limits new members to a retirement package that provides for a 2% at 62, three year average. However, the District has negotiated a 2% at 60, three year average retirement benefit which would apply to any new employee who had previously served with a CalPERS participating agency within the previous six month period.

CALPERS determines contribution requirements using a modification of the Entry Age Normal Method. Under this method, the District's total normal benefit cost for each employee from date of hire to date of retirement is expressed as a level percentage of the related total payroll cost. Normal benefit cost under this method is the level amount the District must pay annually to fund an employee's projected retirement benefit. This level percentage of payroll method is used to amortize any unfunded actuarial liabilities. The District does not have a net pension obligation since it pays these actuarially required contributions monthly. Annual Pension Costs, representing the payment of all contributions required by CALPERS, for the last three years were as follows:

<u>Fiscal Year Ending</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
<i>Miscellaneous Plan</i>			
June 30, 2011	\$162,481	100%	\$0
June 30, 2012	144,838	100%	0
June 30, 2013	156,582	100%	0

CALPERS uses the market related value method of valuing the Plan's assets. Significant actuarial assumptions used to compute the actuarially determined contribution requirement for fiscal year 2013 include an investment rate of return of 7.50%, net of administrative expenses and is assumed inflation at 2.75%. Annual salary increases are assumed to vary by duration of service. Changes in liability due to plan amendments, changes in actuarial assumptions, or changes in actuarial methods are amortized as a level percentage of payroll on a closed basis over twenty years. Investment gains and losses are accumulated as they are realized and amortized over a rolling thirty year period.

As required by State law, effective July 1, 2005, the District's Plan was terminated, and the employees in the plan were required by CALPERS to join a new State-wide pool. One of the conditions of entry to these pools was that the District true-up any unfunded liability in the former Plan, either by paying cash or by increasing its future contribution rates through a Side Fund offered by CALPERS. The District satisfied this Miscellaneous Plan's unfunded liability by agreeing to contribute additional amounts to its normal contribution rates over the next 20 years.

**EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013**

NOTE 9 – DEFINED BENEFIT PENSION PLAN (Continued)

The schedule of funding progress presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits. CALPERS' latest actuarial value (which differs from market value) and funding progress for the State-wide pools are shown below:

Actuarial (In thousands)						
Valuation Date	Entry Age Accrued Liability	Value of Assets	Unfunded (Overfunded) Liability	Funded Ratio	Annual Covered Payroll	Unfunded (Overfunded) Liability as % of Payroll
2010	\$2,297,871,345	\$1,815,671,616	\$482,199,729	79.0%	\$434,023,381	111.1%
2011	2,486,708,579	1,981,073,089	505,635,490	79.7%	427,300,410	118.3%
2012	2,680,181,441	2,178,799,790	501,381,651	81.3%	417,600,034	120.1%

Audited annual financial statements and ten-year trend information are available from CALPERS at P.O. Box 942709, Sacramento, CA 94229-2709.

NOTE 10 – POST RETIREMENT BENEFITS

The District provides post-retirement benefits to eligible employees in the form of reimbursement for post-retirement health insurance premiums. Retired employees have a choice of remaining on the District's group health insurance plan or purchasing a plan of their choice. Reimbursement is made quarterly upon receipt of proof of payment. The District's contribution is capped at the amount of the Kaiser premium which was set at \$1,019 per month per individual for fiscal year 2012-2013, \$676 per month per individual for fiscal year 2011-2012, and \$556 for fiscal year 2010-2011.

The obligation of the District to provide these benefits is determined annually by the Board of Directors.

In order to qualify for postemployment medical benefits, an employee must retire from the District with at least 5 years of service and be over 50 years of age.

The District follows the provisions of Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This Statement establishes uniform financial reporting standards for employers providing postemployment benefits other than pensions (OPEB). The provisions of this statement are applied prospectively and do not affect prior year's financial statements. Required disclosures are presented below.

The District joined the California Employers' Retiree Benefit Trust (CERBT), an agent multiple-employer plan administered by CALPERS, consisting of an aggregation of single-employer plans.

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 10 – POST RETIREMENT BENEFITS (Continued)

Funding Policy and Actuarial Assumptions

The District's policy is to fund minimally the Annual Required Contribution (ARC) of these benefits by accumulating assets with CERBT discussed above pursuant to the District's annual budget approved by Board. The annual required contribution (ARC) was determined as part of the July 1, 2011 actuarial valuation using the entry age normal actuarial cost method. This is a projected benefit cost method, which takes into account those benefits that are expected to be earned in the future as well as those already accrued. The actuarial assumptions included (a) 7.50% investment rate of return, (b) 3% inflation rate, (c) 3.25% projected annual salary increase, and (d) health care cost trend rates of 7.00% to 8.50% for medical benefits. The actuarial methods and assumptions used include techniques that smooth the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets. Actuarial calculations reflect a long-term perspective and 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 revision at least tri-ennially as results are compared to past expectations and new estimates are made about the future. The District's OPEB unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll using a 30 year amortization period on a closed basis.

Funding Progress and Funded Status

Generally accepted accounting principles permit contributions to be treated as OPEB assets and deducted from the Actuarial Accrued Liability when such contributions are placed in an irrevocable trust or equivalent arrangement. As a result, the District has calculated and recorded the Net OPEB Asset, representing the difference between the ARC, amortization and contributions, as presented below:

Annual OPEB expense:	
Annual required contribution (ARC)	\$74,317
Interest on net OPEB obligation (asset)	(304)
Adjustment to annual required contribution	359
Total annual OPEB expense	74,372
Change in net OPEB payable obligation:	
Contributions paid to trust	(74,317)
Premiums paid	(16,485)
Total payments	(90,802)
Total change in net OPEB payable obligation	(16,430)
OPEB obligation (asset) - beginning of year	
OPEB obligation (asset) - end of year	(\$16,430)

The actuarial accrued liability (AAL) representing the present value of future benefits, included in the actuarial study dated July 1, 2011, amounted to \$560,420. The AAL is partially funded since assets have been transferred into CERBT.

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 10 – POST RETIREMENT BENEFITS (Continued)

The Plan's annual required contributions and actual contributions for the last three fiscal years are set forth below:

<u>Fiscal Year</u>	<u>Annual OPEB Cost (AOC)</u>	<u>Actual Contribution</u>	<u>Percentage of AOC Contributed</u>	<u>Net OPEB Obligation (Asset)</u>
June 30, 2011	\$75,887	\$0	\$0	\$75,887
June 30, 2012	77,406	153,293	198%	0
June 30, 2013	74,372	90,802	122%	(16,430)

The Schedule of Funding Progress presents trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits. Trend data from the last three actuarial studies are presented below:

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets (A)</u>	<u>Entry Age Actuarial Accrued Liability (B)</u>	<u>Unfunded (Overfunded) Actuarial Accrued Liability (A – B)</u>	<u>Funded Ratio (A/B)</u>	<u>Covered Payroll (C)</u>	<u>Unfunded (Overfunded) Actuarial Liability as Percentage of Covered Payroll [(A – B)/C]</u>	<u>Interest Rate</u>
1/1/2008	\$101,295	\$455,360	\$354,065	22.25%	\$690,872	51.25%	7.75%
7/1/2011	227,878	560,420	332,542	40.66%	777,420	42.78%	7.50%

NOTE 11 – NET POSITION

Net Position is the excess of all the District's assets and deferred outflows of resources, over all its liabilities and deferred inflows of resources, regardless of fund. The following captions apply only to Net Position, which is determined only at the Government-wide level, and are described below:

Net investment in capital assets describes the portion of Net Position which is represented by the current net book value of the District's capital assets, less the outstanding balance of any debt issued to finance these assets.

Unrestricted describes the portion of Net Position which is not restricted to use.

EAST PALO ALTO SANITARY DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2013

NOTE 12 – 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 disaster. The District joined together with other entities to form the California Sanitation Risk Management Authority (CSRMA), a public entity risk pool currently operating a common risk management and insurance program for 60 member entities. The purpose of CSRMA is to spread the adverse effects of losses among the member entities and to purchase excess insurance as a group, thereby reducing its cost. The District pays annual premiums to CSRMA for its general liability, property damage, workers compensation insurance and automobile coverage. Settled claims for CSRMA have not exceeded coverage in any of the past three fiscal years.

CSRMA is governed by a Board composed of one representative from each member agency. The Board controls the operations of CSRMA including selection of management and approval of operating budgets, independent of any influence by member entities.

CSRMA is not a component unit of the District, and the District's share of CSRMA's assets, liabilities, and equity has not been calculated.