GRANADA SANITARY DISTRICT

MANAGEMENT REPORT

FOR THE YEAR ENDED JUNE 30, 2012

GRANADA SANITARY DISTRICT

Management Report
For the Year Ended June 30, 2012

Table of Contents

FECHTER
& COMPANY
Certified Public Accountants

Craig R. Fechter, CPA, MST
Scott A. German, CPA

Board of Directors of the
Granada Sanitary District
Granada, California

In planning and performing our audit of the financial statements of the Granada Sanitary District for the year ended June 30, 2012, we considered the District's internal control structure to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure.

Our consideration of the internal control would not necessarily disclose all matters in the internal control that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce, to a relatively low level, the risk that errors or irregularities in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

We will review the status of these comments during our next audit engagement. We will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations. We thank the District's staff for its cooperation on this audit.

Fechter & Company, CPAs

Fechter & Company, CPAs

May 25th, 2013
Sacramento, CA

1870 Avondale Avenue Suite 4 | Sacramento, CA 95825 | ph 916-333-5360 | fax 916-333-5370
www.fechtercpa.com
Member of the American Institute of Certified Public Accountants Tax Section
and California Society of CPAs

GRANADA SANITARY DISTRICT

Required Communication
For the Year Ended June 30, 2012

The Auditor's Responsibility under U.S. Generally Accepted Auditing Standards

As stated in our engagement letter, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute assurance that the financial statements are free of material misstatement and are fairly presented in accordance with U.S. generally accepted accounting principles. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting.

As part of obtaining reasonable assurance about whether the District financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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 audit.

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the District are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by the District during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

GRANADA SANITARY DISTRICT

Required Communications
For the Year Ended June 30, 2012

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate(s) affecting the financial statements were:

- Capital asset lives and depreciation expense

Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of financial statements. An audit adjustment may or may not indicate matters that could have a significant effect on the District's financial reporting process. The following audit adjustment, made by us on an annual basis, indicates a matter that could have a significant effect on the District's financial reporting process:

- Posting current year depreciation expense
- Posting year-end accounts payable.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Consultations with Other Independent Auditors

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the District's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing our audit.

GRANADA SANITARY DISTRICT

Basic Financial Statements and Supplemental Information

Years Ended June 30, 2012 and 2011

GRANADA SANITARY DISTRICT

Basic Financial Statements and Supplemental Information

Years Ended June 30, 2012 and 2011

Table of Contents

INDEPENDENT AUDITORS' REPORT

Governing Board
Granada Sanitary District
El Granada, California

We have audited the accompanying basic financial statements of Granada Sanitary District as of and for the years ended June 30, 2012 and 2011 as listed in the table of contents. These basic financial statements are the responsibility of Granada Sanitary District's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, *Government Auditing Standards*, issued by the Comptroller General of the United States, and the State Controller's Minimum Audit Requirements for California Special Districts. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the basic financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall basic financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of Granada Sanitary District, as of June 30, 2012 and 2011, and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America, as well as accounting systems prescribed by the State Controller's office for special districts.

The information identified in the accompanying table of contents as Management's Discussion and Analysis is not a required part of the basic financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and do not express an opinion on it.

Fechter & Company, Certified Public Accountants

Sacramento, California
May 25th, 2013

This section of the Granada Sanitary District's (District) annual report presents management's discussion and analysis of the District's financial performance during the fiscal year ended June 30, 2011. Please read it in conjunction with the District's financial statements which follow this section.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report includes this management discussion and analysis report, the independent auditors' report, and the basic financial statements of the District. The basic financial statements also include notes that explain in more detail some of the information in the financial statements.

BASIC FINANCIAL STATEMENTS

The District's financial statements include the statements of net assets, statements of revenues, expenses and changes in net assets, statements of cash flows, and the statements of fiduciary net assets. These statements are prepared in a manner similar to commercial enterprises. The purpose of the statement of net assets is to report all assets and liabilities of the District as of the date of the statement. The difference between the assets and liabilities is net assets, which represents the portion of total assets not encumbered by debt. Assets and liabilities are reported at historical purchase cost, except for investments, which are reported at fair market value in accordance with accounting pronouncements. Long-term infrastructure assets such as pump stations and sewer lines are reduced by depreciation based upon the expected remaining life of the underlying asset. The District records assets on its books when it takes ownership and liabilities when it incurs the obligation to pay, whether or not it has actually been billed.

Proprietary Funds

The District uses an Enterprise Fund to account for its sewer service. The proprietary fund financial statements include statements of net assets, statements of revenues, expenses, and changes in net assets, and statements of cash flows. These statements are accounted for on an economic resources measurement focus using the accrual basis of accounting similar to commercial enterprises.

Sewer service is provided through the service area of the District, except for the area designated as rural. The basic unit of charge used to calculate sewer service and connection fees is called an Equivalent Residential Unit (ERU), which equates to an estimated 221 gallons per day of wastewater flow. All single family homes are charged 1 ERU as their sewer service charge. Commercial properties are charged a sewer service fee based upon a formula which takes into account their water usage for the year, as well as a strength of wastewater component. The charge per ERU for FY 2011/12 was $383, which is increased from the prior year. Sewer service charges are used to fund the ongoing operations of the District, including administration, operations, treatment, collections, and depreciation set aside costs.

Fiduciary Funds

The District uses an Agency Fund to account for resources held for the benefit of parties outside the government. Statements of fiduciary net assets are included in the District's basic financial statements and are accounted for on an economic resources measurement focus using the accrual basis of accounting.

The Assessment District was formed and funded in 1996 for the purpose of providing the District's share of funds for the expansion of the Sewer Authority Midcoastside (SAM) Wastewater Treatment Plant. It was created under the Municipal Improvement Act of 1913 and the Improvement Bond Act of 1915 in combination with the Integrated Financing District Act. A total of $8.1 million dollars in bonds were originally issued, backed by an assessment on 1,618 parcels. The bonds were refinanced in 2003 at a lower interest rate. Due to the pay-down of principal and pre-payments from some assessed parcels, $6.1 million dollars in bonds were issued backed by assessments on 1,355 parcels.

STATEMENT OF NET ASSETS

The total assets of the District decreased $403,728 from June 30, 2012, due primarily to depreciation of aging assets. Current assets decreased from $4,214,616 to $3,305,486, primarily due to large amounts of construction on sewer lines. The District uses its cash reserve as a set aside for short and long term replacement of capital assets. The item titled "Due from County of San Mateo" represents receivables due from the County. The District utilizes the County's property tax roll to collect its annual sewer service charges. The County collects these charges on the property tax bills sent to tax payers, and then sends monthly payments to the District based upon payments received. The "Advance to Assessment District to fund bond reserve account" decreased substantially due to a payment of approximately $135,000 made to the District by the Assessment District.

OPERATING REVENUES AND EXPENSES

A summary of the District's statements of revenues, expenses and changes in net assets is presented below, along with any changes management considers significant from the previous year.

OPERATING REVENUES	2012	2011	Increase (Decrease)
Sewer service charges	$1,202,309	$1,135,900	$66,409

- Increase due to increase in sewer service charge from $365 to $383 per ERU.

OPERATING EXPENSES			
SAM Sewer collection and treatment	$850,497	$844,984	$5,513

- These are the costs paid to the Sewer Authority Midcoastside Joint Powers Authority to manage and operate the treatment plant, as well as provide sewer cleaning, inspection, and maintenance services on a contract basis for the GSD sewer system. SAM's treatment costs increased over the prior year, mainly due to equipment replacement, while collections costs remained relatively unchanged.

• Administrative and general expenses	$881,624	$702,388	$179,236

NON OPERATING REVENUES			
Property taxes	$689,467	$682,347	$7,120

- Slight increase from prior year due to increased assessments.

Interest income	$13,515	$18,398	($4,883)

- Interest income decreased dramatically due to decreasing interest rates for the LAIF fund, as well as slightly decreased District cash reserves.

BUDGETARY PROCESS

The District budget is presented to the Board of Directors for their comments each year at the regular May District Board Meeting, and is approved at the June meeting. The budget is basically comprised of two functions: administration, which comprises the general office work, permitting, management, legal, and financial aspects of the business; and sewer operations, which represents the District's share of the costs for the SAM wastewater treatment plant operations and maintenance, as well as the costs for maintaining the District's pipeline and pump station system. The SAM treatment, collection and administrative budget accounts for approximately $1,232,738 of the District's $1,717,138 annual operational expenditures, or 72% of the total budget. Capital projects are budgeted along with the operations budget.

CAPITAL ASSETS

The District's capital assets are comprised of its sewer lines, pump stations, force mains, and its share of the SAM Wastewater Treatment Plant (29.5%). The District currently operates and maintains 1 pump station and 34 miles of sewer pipeline. The annual depreciation calculation is based upon the estimated useful life of the assets. Actual repairs, upgrades, or replacements to capital assets are based upon review of the assets' physical conditions as well as the expected useful life of the asset.

LONG-TERM DEBT

The District's only long-term debt was issued as a Certificate of Participation (COP) for $1,145,000 in 1996, and was refinanced as a bank loan in 2002 at a lower interest rate. The COP was used to pay for cost overruns associated with the SAM Wastewater Treatment Plant Expansion that year. More information on this item is included in Note 8 to the basic financial statements.

ECONOMIC FACTORS AFFECTING CURRENT FINANCIAL POSITION

The recent economic downturn could have some impact on the District's finances, due to decreased property tax revenues. There are no other known or expected economic factors which should affect the District's financial position in the near future.

CONTACTING THE DISTRICT'S FINANCIAL MANAGER

This financial report is designed to provide our customers and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have any questions about this report or need additional financial information, please contact the Granada Sanitary District at 650-726-7093.

GRANADA SANITARY DISTRICT
STATEMENT OF NET ASSETS
June 30, 2012

ASSETS	2012	2011
Current Assets:		
Cash and investments	$ 3,203,995	$ 4,010,777
Due from County of San Mateo	52,063	195,816
Interest receivable	3,260	4,773
Prepaid expenses	106,886	3,250
Total current assets	3,366,204	4,214,616
Capital assets, net of accumulated depreciation	6,558,438	6,328,367
Non-current assets:		
Investment in Sewer authority Mid-Coastside	5,439,304	5,650,119
Advance to assessment district to fund bond reserve account	20,087	154,316
Advance to assessment district to fund noncontingent assessment acquisition	300,000	300,000
Advance to Montara Sanitary District, net of allowance	-	-
Total non-current assets	5,759,391	6,104,435
TOTAL ASSETS	$ 15,684,033	$ 16,647,418
LIABILITIES AND NET ASSETS		
Current liabilities:		
Accounts payable and accrued liabilities	$ 35,907	$ 245,406
Interest payable	7,015	8,201
Current portion of long-term debt	75,000	72,000
Deposits held for others	5,924	799
Total current liabilities	123,846	326,406
Note payable, net of current portion	350,000	425,000
Total liabilities	473,846	751,406
Net Assets		
Invested in capital assets, net	6,558,438	6,328,367
Unrestricted	8,651,749	9,567,645
Total net assets	15,210,187	15,896,012
TOTAL LIABILITIES AND NET ASSETS	$ 15,684,033	$ 16,647,418

The accompanying notes are an integral part of these financial statements

GRANADA SANITARY DISTRICT
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2012

	2012	2011
Operating revenues:		
Sewer service charges	$ 1,202,309	$ 1,135,900
Total operating revenues	1,202,309	1,135,900
Operating expenses:		
SAM Sewage collection and treatment	850,497	844,984
Depreciation	215,047	215,012
Administration and general	881,624	702,388
Total operating expenses	1,947,168	1,762,384
Operating income (loss)	(744,859)	(626,484)
Non-operating revenues and (expenses):		
Property tax revenue	689,467	682,347
Interest income	13,515	18,398
Equity income (loss)	(422,176)	(413,226)
Interest expense	(21,634)	(27,494)
Other revenues	66,663	49,052
Capital contributions (connection fees)	14,100	23,500
Total non-operating revenues and (expenses)	339,935	332,577
Change in net assets	(404,924)	(293,907)
Beginning net assets	15,896,012	17,380,250
Prior period adjustment	(280,901)	(1,190,331)
Ending net assets	$ 15,210,187	$ 15,896,012

GRANADA SANITARY DISTRICT
STATEMENT OF CASH FLOWS
For the Year Ended June 30, 2012

	2012	2011
Cash flows from operating activities:		
Receipts from customers	$ 1,258,034	$ 1,057,994
Payments to suppliers and employees	(1,830,016)	(1,347,559)
Net cash provided by operating activities	(571,982)	(289,565)
Cash Flows from non-capital financing activities:		
Receipts from property taxes and other operating income	734,577	871,472
Net cash provided by non-capital financing activities	734,577	871,472
Cash flows from capital and related financing activities:		
Connection fees collected	14,100	23,500
Payments on long-term debt	(72,000)	(68,000)
Interest paid	(22,820)	(29,948)
Other revenues	66,663	49,052
Repayment of advance to assessment district bond reserve account	135,000	130,000
Acquisition and construction of capital assets	(893,216)	(656,400)
Capital assessments paid	(211,361)	-
Net cash provided by (used in) capital and related financing activities	(983,634)	(551,796)
Cash flows from investing activities:		
Interest income	14,257	22,918
Net cash provided by investing activities	14,257	22,918
Net increase (decrease) in cash and cash equivalents	(806,782)	53,029
Cash and cash equivalents, beginning of year	4,010,777	3,957,748
Cash and cash equivalents, end of year	$ 3,203,995	$ 4,010,777
Reconciliation of operating income (loss) to net cash provided by (used) by operating activities:	$ (744,859)	$ (626,484)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Depreciation	215,047	215,012
(Increase) decrease in accounts receivable	55,725	(77,906)
Increase (decrease) in accounts payable and accrued liabilities	(204,374)	199,813
Increase in prepaid expenses	(103,636)	-
Adjustment to prior year construction in progress	210,115	-
Net cash provided (used) by operating activities	$ (571,982)	$ (289,565)

The accompanying notes are an integral part of these financial statements

GRANADA SANITARY DISTRICT
STATEMENT OF FIDUCIARY NET ASSETS
June 30, 2012

ASSETS	2012	2011
Cash and cash equivalents	$ 81,605	$ 87,290
Due from County of San Mateo	-	16,618
Investments	3,008,020	3,087,914
Total Assets	$ 3,089,625	$ 3,191,822
LIABILITIES		
Due to (from) other funds	$ -	$ -
Deposits held for others	2,769,538	2,737,506
Advance to assessment district to fund bond reserve account	20,087	154,316
Advance to assessment district to fund noncontingent assessment acquisition	300,000	300,000
Total Liabilities	$ 3,089,625	$ 3,191,822

The accompanying notes are an integral part of these financial statements

Note 1 – Organization and Summary of Significant Accounting Policies

Organization

Granada Sanitary District (District) was created in 1958 under the provisions of Section 6400 of the State of California Health and Safety Code. An elected board of directors governs the District and has the power to construct, maintain, and operate facilities for the collection, treatment, and disposal of wastewater and solid waste for the benefit of the lands and inhabitants within the San Mateo County communities of El Granada, Princeton-by-the-Sea, Miramar, and northern Half Moon Bay.

Reporting Entity

The accounts of the District are organized on the basis of funds or account groups, each of which is considered to be a separate accounting entity. The operations of each fund are accounted for by providing a separate set of self-balancing accounts which are comprised of each fund's assets, liabilities, fund balance, revenues and expenditures or expenses, as appropriate. Government resources are allocated to and for individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled. The District's funds consist of the following:

Proprietary Fund Type - Enterprise Fund

The Enterprise Fund is used to account for operations (a) that are financed and operated in a manner similar to private business enterprises - where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes. All assets and liabilities associated with the Enterprise Fund's activities are included in the statement of net assets.

Fiduciary Fund Type - Agency Fund

The Agency Fund (Assessment District) is used to account for assets held by the District in a trustee capacity or as an agent for individuals, private organizations, other funds and/or other governments. Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. All assets and liabilities associated with the Assessment District's activities are included in the statement of fiduciary net assets.

Basis of Accounting

Basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

Both the Enterprise Fund and the Agency Fund are accounted for on an economic resources measurement focus using the accrual basis of accounting in accordance with generally accepted accounting principles. Under this basis of accounting, revenues are recognized when earned except property taxes which are recognized in the year they are levied and expenses are recognized when the related liability is incurred.

The District applies all Governmental Accounting Standards Board (GASB) pronouncements as well as the Financial Accounting Standards Board pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements and the State Controller's

Note 1 – Organization and Summary of Significant Accounting Policies, continued

Minimum Audit Requirements for California Special Districts. The District has elected not to apply FASB statements and interpretations issued subsequent to November 30, 1989.

Risk Management
The District is a member of the California Sanitation Risk Management Authority (CSRMA) which provides general liability coverage. Participation in the CSRMA risk sharing pool provides the District general liability coverage up to $750,000 and excess coverage up to $10 million.

Capital Assets
Capital assets for the Enterprise Fund are recorded at cost to the District for purchases or at an estimated cost when assets are contributed. Depreciation is charged to expense for all capital assets and is computed using the straight-line method over the estimated useful lives of five to 50 years.

Property Tax Revenues and Sewer Service Charges
Property taxes and sewer service charges are billed and collected by the County of San Mateo through the property tax billings. Real property taxes are levied against owners of record. The taxes are due in two installments on November 1 and February 1 and become delinquent after December 10 and April 10, respectively. Property taxes are based on assessed values of real property. A revaluation of all real property must be made upon sale or completion of construction. Amounts due from the County of San Mateo include both property taxes and sewer service charges.

Connection Fees
Connection fees consist of charges to homes and businesses for connecting to the District's sewer system.

Operating Revenues and Expenses
The District's operating revenues are those revenues generated from the primary operation of the District's sewer service. Operating expenses are those expenses that are essential to the primary operation of its sewer system. All other revenues and expenses are reported as non-operating revenues and expenses.

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

Investments
Investments in mutual funds and debt instruments are carried at fair value as determined in an active market. Investments in the State of California Local Agency Investment Fund are carried at cost which approximates fair value and are included in cash and cash equivalents in the statements of net assets.

Cash and Cash Equivalents
For purposes of the statements of cash flows, the District considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents.

Note 2 – Cash and Cash Equivalents

The District's cash and cash equivalents are held in federally insured deposit accounts with financial institutions and an external investment pool.

External Investment Pool

The District invests in the California State Treasurer's Local Agency Investment Fund (LAIF). LAIF was established in 1977, is regulated by California Government Code Section 16429, and under the day-to-day administration of the State Treasurer. As of June 30, 2012, LAIF had approximately $71 billion in investments.

LAIF determines fair value on its investment portfolio based on market quotations for those securities where market quotations are readily available, and on amortized cost of best estimate for those securities where market value is not readily available. The District's investments with LAIF at June 30, 2012 included a portion of the pooled funds invested in structured notes and asset-backed securities. These investments are described as follows.

Structured Notes are debt securities (other than asset-backed securities) whose cash flow characteristics (coupon rate, redemption amount, or stated maturity) depend upon one or more indices and / or that have embedded forwards or options.

Asset-Backed Securities, the bulk of which are mortgage-backed securities, entitle their purchasers to receive a share of the cash flows from a pool of assets such as principal and interest repayments from a pool of mortgages (such as Collateralized Mortgage Obligations) or credit card receivables.

Investments are subject to certain types of risks, including interest rate risk, custodial credit risk, credit quality risk, and concentration of credit risk. The following describes those risks.

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. The District does not have a formal policy regarding interest rate risk.

Custodial Credit Risk

Custodial credit risk is the risk that the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The District does not have a formal policy regarding custodial credit risk. The California Government Code and the District's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure District deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits. With respect to investments, custodial credit risk does not apply to a local government's indirect investment in securities through the use of mutual funds or investment pools such as LAIF.

Note 2 – Cash and Cash Equivalents, continued

Credit Risk
Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The District does not have a formal policy regarding credit risk. LAIF does not receive a rating from a nationally recognized statistical rating organization.

Concentration of Credit Risk
The District has limitations on the amount that can be invested in any one issue beyond that stipulated by the California Government Code.

The FDIC insured the bank balances up to $250,000 for each bank, except for non-interest bearing transaction accounts at institutions participating in FDIC's Temporary Liquidity Guarantee Program, which are provided with unlimited deposit guarantee.

The District's cash and cash equivalents consist of the following at June 30, 2012:

	Carrying Amount	Depositary Balance
Amounts insured by federal deposit insurance, or collateralized with securities held by the District in its name.	$ (45,288)	$ 344,807
Amounts held on deposit with the State of California Local Agency Investment Fund, collateralized by investments registered in the State's name.	3,249,164	3,249,164
	$ 3,203,876	$ 3,593,971

The District's cash and cash equivalents are presented as $3,203,995 in the statements of net assets and $87,290 in the statements of fiduciary net assets. The difference between the carrying amount and the depositary balance represents outstanding checks and deposits in transit.

Note 2 – Cash and Cash Equivalents, continued

The District's cash and cash equivalents consist of the following at June 30, 2011:

	Carrying Amount	Depositary Balance
Amounts insured by federal deposit insurance, or collateralized with securities held by the District in its name.	$ 139,641	$ 140,076
Amounts held on deposit with the State of California Local Agency Investment Fund, collateralized by investments registered in the State's name.	3,871,136	3,871,136
	$ 4,010,077	$ 4,011,212

The District's cash and cash equivalents are presented as $4,010,777 in the statements of net assets and $87,290 in the statements of fiduciary net assets. The difference between the carrying amount and the depositary balance represents outstanding checks and deposits in transit.

Note 3 – Agency Fund

In 1994, Granada Sanitary District established the Assessment District to finance the expansion of the sewage treatment facility owned and maintained by the Sewer Authority Mid-Coastside. Special Assessment Limited Obligation Improvement Bonds were issued through the Assessment District to generate the funds necessary to meet the District's portion of the expansion costs. The Agency Fund is used to account for the debt service transactions of the Assessment District. The District acts as an agent with respect to the collection of special assessments from property owners and the payment of principal and interest to special assessment debt holders. The only investments reported by the District are held in the Agency Fund which consist of mutual funds and debt instruments held by a trustee.

Note 4 – Capital Assets

Changes in capital assets consist of the following for the year ended June 30, 2012:

	June 30, 2011	Additions	Deletions	Reclass/Adj.	June 30, 2012
Equipment	$ 52,934	$ -	$ -	$ (30,781)	$ 22,153
Collection and conveyance facilities	9,280,123	-	-	245,161	9,525,284
Less accumulated depreciation	(4,689,303)	(215,047)	-	6,842	(4,897,508)
	4,643,754	(215,047)	-	221,222	4,649,929
Construction in progress	808,079	893,216	-	(669,320)	1,031,975
Land	876,534	-	-	-	876,534
	$ 6,328,367	$ 678,169	$ -	$ (448,098)	$ 6,558,438

Depreciation expense for the year-end June 30, 2012 was $215,047.

Changes in capital assets consist of the following for the year ended June 30, 2011:

	June 30, 2010	Additions	Deletions	Reclass/Adj.	June 30, 2011
Equipment	$ 52,934	$ 9,916	$ -	$ 20,865	$ 52,934
Collection and conveyance facilities	9,280,123	-	-	1,352,579	9,280,123
Less accumulated Depreciation	(4,689,303)	(215,012)	-	(1,497,211)	(4,689,303)
	4,643,754	(205,096)	-	(123,767)	4,643,754
Construction in progress	808,079	631,010	-	(20,865)	808,079
Land	876,534	15,474	-	25,500	876,534
	$ 6,328,367	$ 441,388	$ -	$ (119,132)	$ 6,328,367

Depreciation expense for the year-end June 30, 2011 was $215,012.

Note 5 – Investment in Sewer Authority Mid-Coastside

Sewer Authority Mid-Coastside (Authority) was created by a Joint Exercise of Powers Agreement between the City of Half Moon Bay, the Granada Sanitary District, and the Montara Sanitary District. The Authority was established to construct, maintain, and operate facilities for the collection, treatment, and disposal of wastewater for the benefit of the lands and inhabitants within the member agencies' respective boundaries. Audited financial statements of the Authority are available at its office in Half Moon Bay, California.

The following is a summary of financial information of the Authority from its June 30, 2012 and 2011 audited financial statements:

	2012	2011
Total assets	$ 18,729,205	$ 19,627,282
Total liabilities	655,095	474,335
Net assets	$ 18,074,110	$ 19,152,947
Operating revenues	$ 3,929,243	$ 4,286,103
Operating expenses	5,401,026	5,488,483
Operating loss	(1,471,783)	(1,202,380)
Total non-operating revenues, net	40,678	49,307
Net loss	$ (1,431,105)	$ (1,153,073)

Each member's ownership at June 30, 2012 consists of the City of Half Moon Bay 50.5%, Granada Sanitary District 29.5%, and Montara Sanitary District 20%.

The decreases in the District's equity in the Authority for the year ended June 30, 2012 and 2011 of $318,257 and $413,226, respectively, and are included in the statements of revenues, expenses, and changes in net assets.

Total payments made to the Authority for operations, maintenance, collections and capital for the years ended June 30, 2012 and 2011 were $1,232,736 and $1,395,288, respectively.

Note 6 – Advances to Assessment District

As part of the bond issuance financed through the Assessment District, the District was required to make two separate advances to the Agency Fund. In August 1996 the District transferred $600,000 into the Bond Reserve Fund of the Assessment District to be used as a reserve for the payment of future bond interest and principal. During the years ended June 30, 2012 and 2011, repayments of $135,000 and $130,000 were received from the Assessment District.

The District was also required to advance $700,000 in August of 1996 into the Noncontingent Assessment Fund of the Assessment District. The advance was used to purchase noncontingent assessments for undevelopable parcels within the District. No interest income has been recorded on this advance since

Note 6 – Advances to Assessment District, continued

payment of principal and interest depends on the future growth and development of other parcels within the Assessment District.

Note 7 – Advance to Montara Sanitary District

Due to financial difficulties experienced by the Montara Sanitary District (MSD) in 1996, they were unable to continue funding their portion of the plant expansion of the Authority. The District advanced $1,085,094 of the plant expansion costs on behalf of MSD. According to the Authority funding agreement, there is no repayment schedule, and reimbursement of the advance will occur only if MSD requires additional capacity in the sewage treatment facility. The future capacity needs of MSD are unknown at this time and thus, due to the lack of a firm repayment schedule and unknown future payment requirements of MSD, the District has recorded an allowance of the full amount of initial debt ($1,085,094) to reflect the uncertainty of future repayment.

The District calculates interest on the advance at a rate of 7.278%. Management has determined that the likelihood of any interest payment is remote, therefore an allowance for doubtful accounts has been placed on the full accrued interest balance of approximately $996,946 and $917,973 at June 30, 2012 and 2011, respectively.

Note 8 – Note Payable

On August 1, 1996 the District financed a portion of the sewage treatment plant expansion with the issuance of a Certificate of Participation in the amount of $1,145,000. The terms of the agreement include annual principal payments beginning September 1, 1997 and continuing until September 1, 2016. Interest is payable semi-annually on March 1 and September 1 of each year and the rate had varied between 4.75% and 6.75%. The District refinanced the Certificate of Participation with a note payable in August of 2002 at a fixed interest rate of 4.95%. The payment terms remained the same as the original agreement.

Principal maturities of the note payable at June 30, 2012 consist of the following:

Year Ending June 30,	Principal	Interest	Total
2013	$ 75,000	$ 19,181	$ 94,181
2014	79,000	15,370	94,370
2015	86,000	11,286	97,286
2016	90,000	6,930	96,930
2017	95,000	2,351	97,351
	$ 425,000	$ 55,118	$ 480,118

Note 9 – Special Assessment Debt

During 1996 the District issued Special Assessment Limited Obligation Improvement Bonds in the amount of $8,188,583 to finance the expansion of the sewage treatment plant owned and operated by the Authority. The Agency Fund is used to account for the debt service transactions. The District refinanced the bonds in September 2004 with an interest rate ranging from 2.25% to 6.125% payable semi-annually. The bond principal is paid annually with a final maturity date of September 2022. At June 30, 2012 and 2011 $4,460,000 and $4,595,000 are outstanding. The District is not obligated to repay this debt, but only acts as an agent for the property owners by collecting assessments, forwarding collections to special assessment debt holders, and initiating foreclosure proceedings.

Note 10 – Operating Lease Commitment

The District leases office space with monthly rent of $2,496 plus additional maintenance costs. The lease originally expired November 2007 but was extended until November 2011 with monthly rent increased to $3,000 plus additional maintenance costs. The lease is now month-to-month. The District also leases a copier on multi-year lease.

Future minimum lease payments at June 30, 2012 consist of the following:

Year Ending June 30,	
2013	$ 3,829
	$ 3,829

Note 11 – Contingent Liabilities

Contingent liabilities of an indeterminable amount include normal recurring pending claims and litigation related to the District's operations. According to outside legal counsel, none of the litigation is expected to have a material effect on the financial statements. Therefore, no provision for losses has been included in these financial statements.

Note 12 – Employees' Retirement Plan

Plan Description
The District's defined benefit pension plan, (the "Plan"), provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. The Plan is part of the Public Agency portion of the California Public Employees Retirement System (PERS), a cost sharing multiple-employer plan administered by PERS, which acts as a common investment and administrative agent for participating public employers within the State of California. A menu of benefit provisions as well as other requirements is established by State statutes within the Public Employees' Retirement Law.

The District selects optional benefit provisions from the benefit menu by contract with PERS and adopts

Note 12 – Employees' Retirement Plan, continued

those benefits through Board Action. PERS issues a separate annual financial report. Copies of the PERS' annual financial report may be obtained from the PERS Executive Office 400 P Street – Sacramento, California 95814.

Funding Policy

Active plan members in the Plan are required to contribute 7% of their annual covered salary. The District is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. The District pays the employee and employer's portion for retirement. The actuarial methods and assumptions used are those adopted by the PERS Board of Administration.

The required employer contribution rate for fiscal years ended June 30, 2012 and 2011 were 23.583% and 20.073%, respectively. The contribution requirements of the plan members are established by State statute and the employer contribution rate is established and may be amended by PERS.

Annual Pension Cost

For fiscal years ended June 30, 2012 and 2011, the District's annual pension cost was $30,879 and 27,585, respectively, which was equal to the District's required and actual contribution. The required contribution was determined as part of the June 30, 2009 actuarial valuation using the entry age normal actuarial cost method. The actuarial assumptions included: (a) 7.75% investment rate of return (net of administrative expenses); (b) projected annual salary increases that vary by age, duration of service, and type of employment; (c) 3.0% inflation; (d) 3.25% payroll growth; and (e) individual salary growth based on a merit scale varying by duration of employment coupled with an assumed annual inflation of 3.0% and an annual production growth of 0.25%. The actuarial value of PERS assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a 15-year period (smoothed market value) depending on the size of investment gains and/or losses.

Three Year Trend Information of PERS

Year Ended June 30,	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
2010	16,047	100%	-
2011	27,585	100%	-
2012	30,879	100%	-

Note 13 – Reclassifications

The financial statements may not be comparable with previous years as the District has classified certain expense line items differently from the previous years.

Note 14 – Prior Period Adjustment

During the 2012 fiscal year the District reviewed its assets placed in service from previous years and determined an amount of assets placed in service did not add to the useful life of its assets and decided to remove the amounts from its depreciation schedule.

Note 15 – Subsequent Events

The District has evaluated subsequent events through June 8, 2013, which is the date the basic financial statements were available to be issued.