

**EMERALD BAY SERVICE DISTRICT  
ANNUAL FINANCIAL REPORT**

With Independent Auditors' Report

For the Year Ended June 30, 2018

**EMERALD BAY SERVICE DISTRICT**

**ANNUAL FINANCIAL REPORT**

**FOR THE YEAR ENDED JUNE 30, 2018**

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**VAVRINEK, TRINE, DAY & CO., LLP**  
Certified Public Accountants

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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
Emerald Bay Service District

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the governmental activities and the general fund of the Emerald Bay Service District (the District) as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

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

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

### ***Auditors' Responsibility***

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the 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 entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

### ***Opinions***

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and the general fund of the District as of June 30, 2018, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Emphasis of Matter***

As described in Note 12 to the financial statements, the District restated net position as of July 1, 2017 to remove notes payable and related accrued interest from the General Fund as they do not use current financial resources. Our opinion is not modified with respect to this matter.

### ***Other Matters***

#### ***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3-9 and budgetary comparison information on pages 30-31 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

#### ***Other Information***

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's basic financial statements. The functional expenditures budgetary comparison schedule on pages 32-33 is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The functional expenditures budgetary comparison schedule has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

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

In accordance with *Government Auditing Standards*, we have also issued our report dated December 3, 2018, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the District's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

*Yaurinek, Trine, Day & Co., LLP*

Laguna Hills, California  
December 3, 2018

**EMERALD BAY SERVICE DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
JUNE 30, 2018**

As management of the Emerald Bay Service District (District), we offer readers of the statements, this narrative overview and analysis of the financial activities of the District ended June 30, 2018. We encourage readers to consider the information presented here in conjunction with the District's basic financial statements, which can be found on pages 10 to 29 of this report.

**Operational Overview**

The Emerald Bay Service District (District) was organized on November 20, 1961, under the Community Services District Law by resolution of the Board of Supervisors of the County of Orange, California to provide services to the Emerald Bay residents. Currently, the District has been authorized by the Orange County Local Agency Formation Commission to provide sewage, solid waste, water, fire protection, parks and recreation, health and safety, weed abatement, emergency response, law enforcement, security and other public services to the Emerald Bay Community.

The residents of the Emerald Bay Community have a long history of volunteerism. The District's elected officials voluntarily serve the community and do not receive compensation, benefits or reimbursement for out of pocket expenses incurred while conducting District business. Under the Orange County Fire Authority, the Emerald Bay Fire Station continues to be one of the three remaining level 1 stations that are serviced by volunteers.

The District is a non-enterprise special district, which means that the revenues are derived from property taxes and no fees are charged for the services provided. The sphere of influence for the District is directly related to the Emerald Bay Community Association (EBCA).

The District has one employee, the General Manager, who provides supervision for the day to day operation of the District's facilities. The District contracts the services of a registered professional engineer who provides project plans and equipment specifications and a Certified Public Accountant who provides monthly board reports and compliance reporting. Additionally, the District contracts for administrative and field support from the EBCA employees and rents office space in the EBCA's Community Center. The District also leases from the EBCA the property needed to support the District's sewer and water facilities. The District's attorney is the law firm of Stradling Yocca Carlson & Rauth.

**Financial Highlights**

- The assets of the District exceeded its liabilities at the close of the most recent fiscal year by \$10,002,018 (net position). Of this amount \$2,167,000 (unrestricted net position) may be used to meet the District's ongoing obligations to citizens and creditors.
- The District's total net position increased by \$138,010. This increase is attributable to the investment in capital assets and expenditures being under budget.
- Cash and investments available to the District decreased by \$1,130,005 primarily as the result of the District's investment in capital improvements and repayment of debt during the year.

**EMERALD BAY SERVICE DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS, (Continued)  
JUNE 30, 2018**

- As of the close of the current fiscal year, the District's Governmental Fund reported an ending fund balance of \$2,217,149, a decrease of \$841,296 from the prior year. The decrease is a result of the Governmental Fund recording capital outlay and debt principal payments as expenses in the year of payment. At June 30, 2018, \$1,617,149 is available for spending at the District's discretion and \$600,000 has been assigned for future capital projects.

**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 three components:

1. Government-wide financial statements
2. Fund financial statements
3. Notes to the basic financial statements

This report also contains other supplementary information in addition to the basic financial statements.

**Government-Wide Financial Statements** - The government-wide financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

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. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The statement of activities presents information showing how the District's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

The government-wide financial statements can be found on pages 10 and 11 of this report.

**Fund Financial Statements** - A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The District, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

**EMERALD BAY SERVICE DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS, (Continued)  
JUNE 30, 2018**

**Governmental funds** - Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balance provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The District adopts an annual appropriated budget for its general fund. A budgetary comparison schedule has been provided for the general fund to demonstrate compliance with this budget and the subsequent approved budget adjustments as part of required supplementary information.

The fund financial statements can be found on pages 12 to 15 of this report. The required supplementary information can be found on pages 30 to 31.

**Notes to the financial statements** - The notes provide additional information that is essential to gain a full understanding of the data provided in the government-wide and fund financial statements. The notes to the basic financial statements can be found on pages 16 to 29 of this report.

**Government-Wide Financial Analysis**

As noted earlier, net position may serve, over time, as a useful indicator of a District's financial position. In the case of the District, assets exceeded liabilities by \$10,002,018 at the close of the most recent fiscal year.

Approximately 78% percent of the District's net position reflects its investment in capital assets (e.g., infrastructure and equipment). The District uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending.

**EMERALD BAY SERVICE DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS, (Continued)  
JUNE 30, 2018**

**Emerald Bay Service District  
Statement of Net Position – Governmental Activities**

	<u>June 30, 2018</u>	<u>June 30, 2017</u>
Assets		
Current and other assets	\$ 2,359,598	\$ 3,586,488
Capital assets	<u>14,064,695</u>	<u>13,360,891</u>
Total Assets	<u>\$ 16,524,293</u>	<u>\$ 16,947,379</u>
Current liabilities	\$ 467,446	845,635
Noncurrent liabilities	<u>5,954,829</u>	<u>6,237,736</u>
Total Liabilities	<u>6,422,275</u>	<u>7,083,371</u>
Net Position:		
Invested in capital assets	7,835,018	6,857,850
Unrestricted	<u>2,167,000</u>	<u>3,006,158</u>
Total Net Position	<u>\$ 10,002,018</u>	<u>\$ 9,864,008</u>

None of the District's net position is subject to external restrictions. The balance of unrestricted net position may be used to meet the District's ongoing obligations.

**Emerald Bay Service District  
Statement of Activities – Governmental Activities**

	<u>June 30, 2018</u>	<u>June 30, 2017</u>	<u>Change</u>
General revenues:			
Property tax	\$ 2,379,517	\$ 2,226,212	\$ 153,305
Investment income	30,612	33,649	(3,037)
Other	<u>17,350</u>	<u>2,400</u>	<u>14,950</u>
Total general revenues	<u>2,379,517</u>	<u>2,262,261</u>	<u>165,218</u>
Program Revenues – Operating Grants and contributions	12,292	62,452	(50,160)
Expenses:			
General government	1,255,318	1,148,420	106,898
Public services	501,581	274,562	227,019
Recreation and safety	325,066	362,448	(37,382)
Interest and fiscal charges	<u>219,796</u>	<u>229,426</u>	<u>(9,630)</u>
Total expenses	<u>2,301,761</u>	<u>2,014,856</u>	<u>286,905</u>
Change in net position	138,010	309,857	(171,847)
Net position – beginning of year	<u>9,864,008</u>	<u>9,554,151</u>	<u>309,857</u>
Net position – end of year	<u>\$ 10,002,018</u>	<u>\$ 9,864,008</u>	<u>\$ 138,010</u>

**EMERALD BAY SERVICE DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS, (Continued)  
JUNE 30, 2018**

**Financial Analysis of the Government's Funds**

As noted earlier, the District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

**Governmental Funds** - The focus of the District's governmental funds is to provide information on near-term inflows, outflows and balances of spendable resources. Such information is useful in assessing the District's financing requirements. In particular, unassigned fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

At June 30, 2018, the District's governmental fund reported an ending balance of \$2,217,149, a decrease of \$841,296 from the prior year. Unassigned fund balance of \$1,617,149 is available for spending at the District's discretion. The Board has assigned \$600,000 for future capital improvement projects.

The fund balance of the District's general fund decreased by \$841,296 during the current fiscal year. This decrease can be compared to a decrease of \$3,141,243 in the prior fiscal year. Key factors in the changes are as follows:

- Capital expenditures for infrastructure and equipment decreased from \$3,686,943 in the prior fiscal year to \$1,371,450 in the current fiscal year.
- Interest earnings and change in fair value of investments decreased by \$3,037. This decrease is primarily the result of a lower investment balance in the State of California Local Agency Investment Fund as funds were expended for capital outlay.
- As required by the Bond Indenture Agreement, the District has expended the full amount borrowed on construction related to the Main Gate Safety Improvement Project as well as additional water, sewer and storm drain infrastructure projects.

**General Fund Budgetary Highlights**

The preliminary budget was adjusted as necessary by action of the Board in accordance with laws and policy. The following is a comparison of actual revenues and expenditures to the Final Board Approved Budget:

- The District estimated a conservative 2% increase in property taxes when developing and approving the original budget approved in June 2017. Subsequently the Board approved budget adjustments in March 2018 to more accurately project the actual revenue. Actual revenues exceeded the Final Budget by \$111,597 or 4.8%.

**EMERALD BAY SERVICE DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS, (Continued)  
JUNE 30, 2018**

- General government expenditures were \$824,586 or 4.4% less than the final budget; public services, water and sewer expenditures were \$264,667 or 26.2% less than the final budget, and recreation and safety expenditures were \$325,066 or 6.5% less than the final budget. In summary, the total operating expenditures were under budget by \$154,381 or 9.8% below the total final approved budget.
  
- Capital expenditures for infrastructure and equipment were \$1,371,450 or \$293,050 less than the final budget, due to projects being canceled, deferred, or in process. Excess appropriations were not carried forward during the budget process, instead each project was evaluated and if any funds were needed to complete the project they were reappropriated upon approval of the fiscal year 2018-19 budget.

**Capital Asset and Debt Administration**

**Capital Assets** - The District spent \$1,371,450 on infrastructure assets and equipment.

Additional information on the District's capital assets can be found in Note 5 on page 26 of the notes to the financial statements.

**Long-term debt** - At the end of the current fiscal year the District's debt consisted of bond financing issued for \$7,000,000 in April 2015 with an outstanding balance of \$6,229,677 at June 30, 2018. Additional information can be found in Note 6 starting on page 26 of the notes to the financial statements.

**Economic Factors and Next Year's Budgets and Rates**

The Mihaylo College of Business and Economics at the California State University Fullerton reported that Orange County economic indicators continue on an upward trend. This upward trend has continued for eight years with the last decrease in the third quarter of 2009. Real estate continues to appreciate and is expected to increase an additional 4% in 2019. Demand for homes in Orange County still remains high. The District's Property tax revenue is expected to see continued increases as homes continue to be sold, removed and replaced within the Emerald Bay Community.

Assessed property values continue to increase for the addresses included within the District's property tax allocations. Since 2011 the County of Orange, including Emerald Bay, has seen a steady appreciation in real estate pricing, which in turn, has a direct effect on assessed valuations of properties within the District.

**EMERALD BAY SERVICE DISTRICT  
MANAGEMENT'S DISCUSSION AND ANALYSIS, (Continued)  
JUNE 30, 2018**

The District's Board of Directors and staff relied on this information during the development of the Fiscal Year 2018-19 annual budget. Increases in estimated property taxes are estimated to be 4% for the upcoming year.

This financial report is designed to provide a general overview of the Emerald Bay Service District's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report, or requests for additional financial information, should be addressed to the District's Office: Emerald Bay Service District, 600 Emerald Bay, Laguna Beach, California 92651.

## **BASIC FINANCIAL STATEMENTS**

**GOVERNMENT-WIDE FINANCIAL STATEMENTS**

**EMERALD BAY SERVICE DISTRICT**

**STATEMENT OF NET POSITION  
JUNE 30, 2018**

	<u>Governmental Activities</u>
<b>ASSETS:</b>	
Cash and investments	\$ 2,216,740
Taxes receivable	35,685
Reimbursement agreement receivables	28,529
Due from Emerald Bay Community Association	35,597
Interest receivable	9,541
Other assets	33,506
Capital assets, net of accumulated depreciation	14,064,695
Total assets	<u>16,424,293</u>
<b>LIABILITIES:</b>	
Accounts payable and accrued expenses	112,628
Accrued interest payable	50,149
Due to Emerald Bay Community Association	29,821
Current portion of long-term liabilities	274,848
Total current liabilities	<u>467,446</u>
Non-current portion of long-term liabilities	5,954,829
Total liabilities	<u>6,422,275</u>
<b>NET POSITION:</b>	
Net investment in capital assets	7,835,018
Unrestricted	2,167,000
Total net position	<u>\$ 10,002,018</u>

See accompanying notes to the financial statements.

**EMERALD BAY SERVICE DISTRICT**

**STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED JUNE 30, 2018**

<b>Functions/Programs</b>	<b>Expenses</b>	<b>Program Revenues Operating Grants and Contributions</b>	<b>Net (Expenses) and Changes in Net Position</b>
Governmental activities:			
General government	\$ 1,255,318	\$ -	\$ (1,255,318)
Public services water and sewer services	501,581	-	(501,581)
Recreation and safety	325,066	12,292	(312,774)
Interest and fiscal charges	219,796	-	(219,796)
Total governmental activities	\$ 2,301,761	\$ 12,292	\$ (2,289,469)
	General revenues:		
	Taxes		2,379,517
	Investment income		30,612
	Miscellaneous		17,350
	Total general revenues		2,427,479
	Change in net position		138,010
	Net position - beginning of year		9,864,008
	Net position - end of year		\$ 10,002,018

See accompanying notes to the financial statements.

**FUND FINANCIAL STATEMENTS**

**EMERALD BAY SERVICE DISTRICT**

**BALANCE SHEET  
GOVERNMENTAL FUND  
JUNE 30, 2018**

	<u>General Fund</u>
ASSETS:	
Cash and investments	\$ 2,216,740
Taxes receivable	35,685
Reimbursement agreement receivables	28,529
Interest receivable	9,541
Due from Emerald Bay Community Association	35,597
Other assets	33,506
Total assets	<u>\$ 2,359,598</u>
LIABILITIES AND FUND BALANCE:	
Liabilities:	
Accounts payable and accrued expenses	\$ 112,628
Due to Emerald Bay Community Association	29,821
Total liabilities	<u>142,449</u>
Fund balance:	
Assigned - future capital improvements	600,000
Unassigned	1,617,149
Total fund balance	<u>2,217,149</u>
Total liabilities and fund balance	<u>\$ 2,359,598</u>

See accompanying notes to the financial statements.

**EMERALD BAY SERVICE DISTRICT**

**RECONCILIATION OF THE GOVERNMENTAL FUND BALANCE SHEET  
TO THE STATEMENT OF NET POSITION  
JUNE 30, 2018**

Fund balance of governmental fund	\$ 2,217,149
Amounts reported for governmental activities in the statement of net position are different because:	
Capital assets used in governmental activities are not current financial resources and therefore are not reported in the governmental funds.	
Capital assets, net of accumulated depreciation	14,064,695
Long-term liabilities are not due and payable in the current period and therefore are not reported in the governmental funds.	
Bonds payable	(6,229,677)
Accrued interest payable on long-term liabilities do not require the use of current financial resource and therefore are not reported in the governmental funds.	
Interest payable	(50,149)
Net position of governmental activities	<u>\$ 10,002,018</u>

See accompanying notes to the financial statements.

**EMERALD BAY SERVICE DISTRICT**

**STATEMENT OF REVENUES, EXPENDITURES AND  
CHANGES IN FUND BALANCE  
GOVERNMENTAL FUND  
FOR THE YEAR ENDED JUNE 30, 2018**

	<u>General Fund</u>
REVENUES:	
Taxes	2,379,517
Intergovernmental	12,292
Investment income	30,612
Other	17,350
Total revenues	<u>2,439,771</u>
EXPENDITURES:	
Current:	
General government	824,586
Public services water and sewer services	264,667
Recreation and safety	325,066
Capital outlay	1,371,450
Debt service:	
Principal retirement	273,364
Interest and fiscal charges	221,934
Total expenditures	<u>3,281,067</u>
Net change in fund balance	(841,296)
Fund balance, beginning, as restated	<u>3,058,445</u>
Fund balances, ending	<u><u>\$ 2,217,149</u></u>

See accompanying notes to the financial statements.

**EMERALD BAY SERVICE DISTRICT**

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES  
AND CHANGES IN FUND BALANCE OF THE GOVERNMENTAL FUND TO THE  
STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED JUNE 30, 2018**

Net change in fund balance - governmental fund: \$ (841,296)

Amounts reported for governmental activities in the statement of activities are different because:

Governmental funds report capital outlays as expenditures. However in the statement of activities, those costs are capitalized and the assets are depreciated over their estimated useful lives.

Capital outlay	1,371,450
Depreciation expense	(667,646)

Repayment of long-term liabilities is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net position:

Notes payable	7,758
Bonds payable	265,606

Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. These expenses include changes in interest payable.

2,138

Change in net position of governmental activities	<u>\$ 138,010</u>
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See accompanying notes to the financial statements.

## **EMERALD BAY SERVICE DISTRICT**

### **NOTES TO FINANCIAL STATEMENTS JUNE 30, 2018**

#### ***NOTE 1 – ORGANIZATIONAL BACKGROUND***

The Emerald Bay Service District (the “District”) was organized on November 20, 1961, under the Community Services District Law to provide services to the residents living in the unincorporated area of Orange County, California known as Emerald Bay. The District was authorized by an election held on November 14, 1961, and subsequently approved by a resolution of the Board of Supervisors of Orange County. Currently, the District has been authorized by the Orange County Local Agency Formation Commission to provide collection, transfer and disposal of solid waste; collection, treatment and disposal of sewage; fire protection; law enforcement; parks and recreation; security services; street improvement, maintenance and repair; water supply; and weed abatement services to the Emerald Bay community.

The District is governed by a five-member Board of Directors who are elected by the community residents through a general election. The District is authorized to provide a wide range of services, such as drainage improvements, road improvements, maintenance, protection and other services typically provided by a city. The members of the Board of Directors of District serve without compensation, benefits, or reimbursement of out of pocket expenses, and authorize policies, policy renewals, appropriations limit, annual budget and the budget amendments.

#### ***NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES***

##### **A. Basis of Presentation and Measurement Focus**

The District’s basic financial statements are prepared in conformity with generally accepted accounting principles in the United States of America. The Governmental Accounting Standards Board (GASB) is the acknowledged standard-setting body for establishing accounting and financial reporting standards followed by governmental entities in the United States. The basic financial statements of the District are composed of the following:

- Government-wide financial statements
- Fund financial statements
- Notes to the basic financial statements

Government-wide financial statements display information about the District as a whole. These statements include a single column for the governmental activities of the primary government. The statement of activities demonstrates the degree to which the direct expenses of a given function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function.

Government-wide financial statements are presented using the economic resources measurement focus and the full accrual basis of accounting. Accordingly, all of the District’s assets and liabilities, including capital assets and long-term liabilities, are included in the accompanying statement of net position. The statement of activities presents changes in net position. Under the full accrual basis of accounting, revenues are recognized in the period in which they are earned, while expenses are recognized in the period in which the liability is incurred. As a result, amounts paid to acquire capital assets are capitalized as assets in the government-wide financial statements, rather than reported as an expenditure. Proceeds of long-term debt are recorded as a liability in the government-wide financial statements, rather than as another financing source. Amounts paid to reduce long-term indebtedness of the District are reported as a reduction of the related liability, rather than as an expenditure.

**EMERALD BAY SERVICE DISTRICT**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2018**

***NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED***

**A. Basis of Presentation and Measurement Focus, Continued**

The District’s governmental fund statements include a balance sheet and a statement of revenues, expenditures, and changes in fund balance. In the fund financial statements, governmental funds are accounted for on a spending or “current financial resources” measurement focus and modified accrual basis of accounting. Accordingly, only current assets and current liabilities are included on the balance sheet. The statement of revenues, expenditures, and changes in fund balance present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets. Under the modified accrual basis of accounting, revenues are recognized in the accounting period in which they become both measurable and available to finance expenditures of the current period. Measurable means that the amounts can be estimated, or otherwise determined. Available means that the amounts were collected during the reporting period or soon enough thereafter to be available to finance the expenditures accrued for the reporting period. For this purpose, the District considers revenues to be available if they are collected within 60 days of the end of the current fiscal year. Expenditures are recorded in the accounting period in which the related fund liability is incurred.

The District reports the following major governmental funds:

General Fund - The General Fund is the general operating fund of the District. It is used to account for all financial resources except those required to be accounted for in another fund, and is currently the only fund of the District.

**B. Cash and Investments**

The District’s cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturity of three months or less from the date of acquisition. Cash and cash equivalents are combined with investments and displayed as cash and investments.

Highly liquid money market investments are stated at amortized cost. All other investments are reported at fair value. Fair value is the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date.

The District applies fair value to investments, and disclosures related to the fair value hierarchy. The fair value hierarchy, which has three levels, is based on the valuation inputs used to measure fair value: Level 1 inputs are quoted market prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

**EMERALD BAY SERVICE DISTRICT**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2018**

***NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED***

**C. Capital Assets**

Capital assets, which include infrastructure and equipment, are reported in the governmental activities column in the government-wide financial statements. Assets are recorded at historical cost, or estimated historical cost, if purchased or constructed. Donated assets are valued at acquisition value at the date of donation. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. The District utilizes a capitalization threshold of \$5,000.

Depreciation is provided using the straight-line method over the estimated useful lives of the asset as follows:

	<u>Years</u>
Infrastructure	10 - 30
Equipment	3 - 5

The governmental fund financial statements do not present capital assets. Instead, capital asset purchases are reported as capital outlay expenditures. As such, capital assets are shown as a reconciling item in the reconciliation of the governmental fund balance sheet to the statement of net position.

**D. Property Taxes**

Secured property taxes attach as an enforceable lien on real property as of January 1 of each year. Property taxes are levied by the County on July 1. The first installment of taxes is due on November 1 and becomes delinquent on December 10. The second installment of taxes is due February 1 and becomes delinquent on April 10. The County is permitted by State law (Proposition 13) to levy taxes at 1% of full market value (at time of purchase) and can increase the assessed values no more than 2% per year.

District property taxes are recognized when levied, to the extent that they result in current receivables and are collected within an availability period of 60 days after year end. The District participates in the County of Orange Teeter Plan guaranteed payments. The County of Orange collects an administration fee from the District for its services. The District receives a percentage of the basic 1% ad valorem tax rate allowed on property within the Emerald Bay Service District. Property taxes are remitted to the District from the County of Orange at various times throughout the year. Property taxes are recognized as revenue in the General Fund in the year for which they are levied, in accordance with the modified accrual basis of accounting.

## EMERALD BAY SERVICE DISTRICT

### NOTES TO FINANCIAL STATEMENTS JUNE 30, 2018

#### *NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED*

##### E. Fund Equity

Fund balances are reported in the fund financial statements in the following classifications:

- Nonspendable - includes amounts that are (a) not in spendable form, or (b) legally or contractually required to be maintained intact. The "not in spendable form" criterion includes items that are not expected to be converted to cash, for example: inventories, prepaid amounts, and long-term notes receivable.
- Restricted - includes amounts from resources that constraints placed on the use of them are either (a) externally imposed by creditors (i.e. debt covenants) grantors, contributors, or laws or regulations of other governments, or (b) imposed by law through constitutional provisions or enabling legislation. Restrictions may effectively be changed or lifted only with the consent of resource providers.
- Committed - includes amounts that can only be used for the specific purposes determined by a formal action of the District's highest level of decision-making authority, the District's Board of Directors (Board). Commitments may be changed or lifted only by the Board taking the same formal action that imposed the constraint originally (for example: resolution).
- Assigned - comprises amounts intended to be used by the Board for specific purposes that are neither restricted nor committed. Intent is expressed by (a) the Board or (b) a body (for example: a budget or finance committee) or official to which the Board has delegated the authority to assign amounts to be used for specific purposes. The District has delegated this authority to the General Manager.
- Unassigned - is the residual classification for the General Fund and includes all amounts not contained in the other classifications. Unassigned amounts are technically available for any purpose.

The District does not currently have any nonspendable, restricted, or committed fund balances. In circumstances when an expenditure is made for a purpose for which amounts are available in multiple fund balance classifications, fund balance is depleted in the order of restricted, committed, assigned or unassigned.

On June 22, 2017, the District's Board also adopted a reserve policy with the following requirements:

- Operating reserves with a minimum amount of six months of operating expenses to a maximum of eight months of operating expenses – these funds can be used to meet operational cash flow requirements consistent with the District's annual budget. As described above, the FY 2018-19 totaled \$1,939,897, including budgeted debt service payments. As such, six to eight months would represent between \$969,949 and \$1,293,265.

**EMERALD BAY SERVICE DISTRICT**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2018**

***NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED***

- Capital reserves may be authorized through the budget process by the Board. Capital reserves may be used for unplanned or unbudgeted capital replacement, when procured in accordance with District’s purchasing policy. For the year ended June 30, 2018, the District has assigned \$600,000 for Future Capital Improvements.
- Emergency/Contingency reserves may be used in the event of a natural disaster, economic downturn, or any other event that the Board deems to be a qualifying situation in which the use of emergency or contingency reserves is necessary. As of June 30, 2018, the Board has established a balance of \$125,000 for the Contingency Reserve, which is reported as part of unassigned fund balance.

As of June 30, 2018, the unassigned fund balance totaled \$1,617,149, which includes the Emergency/Contingency reserve and the minimum fund balance/operating reserves described above.

**F. Classification of Net Position**

On the statement of net position, net position is classified into two components which are defined as follows:

- Net investment in capital assets - This component of net position consists of capital assets, net of accumulated depreciation, and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
- Unrestricted net position - This component of net position represents the residual net position that does not meet the definition of the categories above, and the net equity available to the District.

**G. Long-term Liabilities**

Long-term debt and other financed obligations are reported as liabilities in the government-wide financial statements. The governmental fund financial statements do not present long-term debt and other financed obligations. Principal payments and reductions in obligations are reported as debt service expenditures. As such, long-term debt and other financed obligations are shown as reconciling items in the Reconciliation of Governmental Funds Balance Sheet to the Statement of Net Position.

## EMERALD BAY SERVICE DISTRICT

### NOTES TO FINANCIAL STATEMENTS JUNE 30, 2018

#### *NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED*

##### H. New GASB Pronouncements

###### **Effective in Future Years**

###### GASB Statement No. 83

In November 2016, GASB issued Statement No. 83, *Certain Asset Retirement Obligations*. This Statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital asset should recognize a liability based on the guidance in this Statement. This Statement also requires disclosure of information about the nature of a government's ARO, the methods and assumptions used for the estimates of the liabilities, and the estimated remaining useful life of the associated tangible capital assets. The requirements of this Statement are effective for reporting periods beginning after June 15, 2018, or the 2018-19 fiscal year. The District has not determined the effect of the Statement.

###### GASB Statement No. 84

In January 2017, GASB issued Statement No. 84, *Fiduciary Activities*. The objective of this Statement is to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. The requirements of this Statement are effective for reporting periods beginning after December 15, 2018, or the 2019-20 fiscal year. The District has not determined the effect of this Statement.

###### GASB Statement No. 87

In June 2017, GASB issued Statement No. 87, *Leases*. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities. The Statement is effective for the reporting periods beginning after December 15, 2019, or 2020-2021 fiscal year. The District has not determined the effect of the Statement.

###### GASB Statement No. 89

In June 2018, GASB issued Statement No. 89, *Accounting for Interest Cost Incurred Before the End of Construction Period*. The objectives of this Statement are to enhance the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period and to simplify accounting for interest cost incurred before the end of a construction period. The requirements of this Statement are effective for reporting periods beginning after December 15, 2019, or 2020-2021 fiscal year. The District has not determined the effect of the Statement.

###### GASB Statement No. 90

In August 2018, GASB issued Statement No. 90, *Majority Equity Interests*. The objectives of this Statement are to improve the consistency and comparability of reporting of government's majority equity interest in a legally separate organization and to improve the relevance of financial statement information for certain component units. The requirements of this Statement are effective for reporting periods beginning after December 15, 2018, or 2019-2020 fiscal year. The District has not determined the effect of the Statement.

**EMERALD BAY SERVICE DISTRICT**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2018**

***NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, CONTINUED***

I. Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of certain balances, and the related reported amounts of revenues and expenses/expenditures during the reporting period. Actual results could differ from those estimates.

***NOTE 3 – CASH AND INVESTMENTS***

Cash and investments in fair value at June 30, 2018, consist of the following:

Deposits with financial institutions:

Balance per Bank	\$ 158,605
less: reconciling items	(9,220)
Balance per books	<u>149,385</u>
Cash Preferred Deposit*	56,532
Local Agency Investment Fund	<u>2,010,823</u>
Total Cash and Investments	<u><u>\$ 2,216,740</u></u>

\*Not FDIC insured

Cash in Bank

The carrying amount of the District’s cash is covered by Federal depository insurance up to \$250,000. As described above, as of June 30, 2018, the District’s Cash Preferred Deposit was not FDIC insured, but other deposits were not exposed to custodial credit risks.

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The California Government Code does not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110 percent of the total amount deposited by the public agencies. California law also allows financial institutions to secure deposits by pledging first trust deed mortgage notes having a value of 150 percent of the secured public deposits. The District’s deposits were not held in accounts collateralized in accordance with government code.

**EMERALD BAY SERVICE DISTRICT**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2018**

***NOTE 3 – CASH AND INVESTMENTS, CONTINUED***

Local Agency Investment Fund

The District is a voluntary participant in Local Agency Investment Fund (LAIF), which is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California and the Pooled Money Investment Board. The State Treasurer's Office pools these funds with those of other governmental agencies in the State and invests the cash. The fair value of the District's investment in this pool, which approximates cost, is not reported in the accompanying financial statements based upon the District's 24 hour liquidity value. The fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio) is disclosed in the accompanying notes to the financial statements. The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis and reported as cash equivalents in the statement of net position. Included in LAIF's investment portfolio are collateralized mortgage obligations, mortgage-backed securities, other asset backed securities, and floating rate securities issued by Federal Agencies, government-sponsored enterprises and corporations.

The Pooled Money Investment Board has established policies, goals, and objectives to make certain that their goal of safety, liquidity, and yield are not jeopardized. The value of the LAIF deposits as of June 30, 2018, was \$2,010,823 and had a weighted average maturity of 193 days. LAIF is not rated as to credit risk by a nationally recognized statistical rating organization.

Authorized Investments:

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

Investment Type Authorized by State Law	Authorized By Investment Policy	*Maximum Maturity	*Maximum Percentage of Portfolio	*Maximum Investment In One Issue
U.S. Treasury Obligations	Yes	6 years**	None	None
Negotiable Certificates of Deposit	Yes	5 years**	30%	20%
Money Market Mutual Funds	Yes	N/A	20%	10%
Local Agency Investment Fund (LAIF)	Yes	N/A	None	\$ 65,000,000

\* Based on state law requirements or investment policy requirements, whichever is more restrictive.

\*\*Government Code restricts investment maturities to 5 years unless authorized by the Board.

**EMERALD BAY SERVICE DISTRICT**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2018**

***NOTE 3 – CASH AND INVESTMENTS, CONTINUED***

Disclosures Relating to Fair Value Measurements:

The District categorizes its fair value measurements within the fair value hierarchy established by GAAP. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs, including matrix pricing models; Level 3 inputs are significant unobservable inputs.

Deposits and withdrawals to and from LAIF are made on the basis of \$1 and not at fair value. Accordingly, the District's investment in LAIF of \$2,010,823 at June 30, 2018 is measured based on uncategorized inputs not defined as level 1, level 2, or level 3.

***NOTE 4 – DUE FROM EMERALD BAY COMMUNITY ASSOCIATION AND OTHER RELATED PARTY TRANSACTIONS***

The Board of Directors of the District entered into a Management Services Agreement with the Emerald Bay Community Association (EBCA), a legally separate but geographically identical entity. The term of the agreement extends to June 30, 2021. Under the agreement, the District pays for management services. In FY 2017-18, the management service expense was \$260,032, which included office rent administrative expenses, lease of EBCA property upon which the District facilities are located, plus specific percentages of designated employees of EBCA. As of June 30, 2018, there was balance of \$29,821 due to EBCA for services rendered during FY 2017-18 under this agreement.

The District also paid for \$105,936 to EBCA during the year for the District's portion of sewer pipeline and storm drain cleaning costs.

Certain costs related to the Main Gate Project and infrastructure maintenance and improvement were split between the District and EBCA. At June 30, 2018, there was balance of \$35,597 Due from EBCA.

**EMERALD BAY SERVICE DISTRICT**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2018**

**NOTE 5 – CAPITAL ASSETS**

During the year ended June 30, 2018, the District’s capital assets consisted of following:

	June 30, 2017	Additions	Deletions	June 30, 2018
<b>Capital assets, being depreciated:</b>				
Water infrastructure	1,440,947	249,843	-	1,690,790
Sewer infrastructure and capacity rights	3,462,557	299,227	-	3,761,784
General infrastructure	2,865,908	-	-	2,865,908
Main Gate	7,666,902	822,380	-	8,489,282
Equipment	156,807	-	-	156,807
Total capital assets, being depreciated	15,593,121	1,371,450	-	16,964,571
<b>Less accumulated depreciation for:</b>				
Net assets being depreciated	(2,232,230)	(667,646)	-	(2,899,876)
Total capital assets, net	\$ 13,360,891	\$ 703,804	\$ -	\$ 14,064,695

Depreciation expense of \$430,732 was allocated to general government and \$236,914 was charged to the public services water and sewer services for the year ended June 30, 2018 on the Statement of Activities.

**NOTE 6 – LONG TERM LIABILITIES**

The following is a summary of long-term liabilities of the District for the year ended June 30, 2018:

	Balance			Balance June 30, 2018	Classification	
	June 30, 2017	Additions	Deletions		Due Within One Year	Due More Than One Year
Notes payable	\$ 7,758	\$ -	\$ (7,758)	\$ -	\$ -	\$ -
Bonds payable	6,495,283	-	(265,606)	6,229,677	274,848	5,954,829
Total	\$ 6,503,041	\$ -	\$ (273,364)	\$ 6,229,677	\$ 274,848	\$ 5,954,829

Notes Payable

The District had a note payable with an original principal of \$43,922 bearing 4% interest, payable monthly through February 2018. During the year, the remaining balance of \$7,758 in principal was paid in full, along with interest of \$118. As of June 30, 2018, the remaining balance is \$0.

Installment Sales Agreement – Bond Payable

In April 2015, the District entered into an Installment Sale Agreement with Municipal Finance Corporation for \$7,000,000 for the purpose of financing the Main Gate Safety Improvement Project and other storm drain, sewer and water infrastructure improvements, collectively referred to as the 2015 Project. Interest accrues at 3.45% per year. Combined interest and principal payments total \$243,711, and are due April 7 and October 7 of each year through April 7, 2035. For the year ended June 30, 2018, the District paid \$265,606 in principal, and \$221,816 in interest.

**EMERALD BAY SERVICE DISTRICT**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2018**

***NOTE 6 – LONG TERM LIABILITIES, CONTINUED***

The District may prepay in whole or in part on any date on or after April 7, 2020 and before April 7, 2025 at a prepayment price equal to 101% of the principal amount of the Installment Payments plus accrued interest, or on any date on or after April 7, 2025 at a prepayment price equal to the principal amount of Installment Payments plus accrued interest.

All revenues of the District, including property tax revenues, are pledged to the repayment of the notes. The annual debt service requirements on the agreement is as follows:

<u>Fiscal Year Ended</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
June 30, 2019	274,848	212,574	487,422
June 30, 2020	284,412	203,010	487,422
June 30, 2021	294,309	193,113	487,422
June 30, 2022	304,550	182,871	487,422
June 30, 2023	315,148	172,274	487,422
June 30, 2024 - June 30, 2028	1,748,070	689,039	2,437,109
June 30, 2029 - June 30, 2033	2,074,129	362,980	2,437,109
June 30, 2034 - June 30, 2035	934,211	40,632	974,844
	<u>\$ 6,229,677</u>	<u>\$ 2,056,493</u>	<u>\$ 8,286,170</u>

***NOTE 7 – INSURANCE PROGRAM***

The District is exposed to various risks of loss related to torts; thefts of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disaster. The District is a member of the Special District Risk Management Authority (SDRMA). The SDRMA is a risk-pooling self-insurance authority, created under the provisions of the California Government Code Sections 6500 et. seq. The purpose of the SDRMA is to spread the adverse effects of losses among the member entities and to purchase excess insurance as a group, thereby reducing its cost. A copy of the SDRMA audit report may be obtained from SDRMA at 1112 I Street, Suite 300, Sacramento, California 95814.

Member agencies pay an annual premium to the SDRMA and are determined annually by the governing board. The District's policy limits for workers' compensation insurance is \$5,000,000 per occurrence, with no deductible. The District's policy limits for property and liability insurance are \$1,000,000,000 per covered loss for property damage, \$100,000,000 per covered loss for boiler and machinery, \$2,000,000 per covered loss for pollution, and \$10,000,000 per occurrence for general liability, which includes automobile, errors and omissions of officers.

**EMERALD BAY SERVICE DISTRICT**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2018**

***NOTE 7 – INSURANCE PROGRAM, CONTINUED***

The following is a summary of the insurance policies carried by the District for the fiscal year ended June 30, 2018:

<i>Comprehensive Business Policy - SDRMA</i>	
General property	\$ 1,000,000,000
Boiler and machinery	100,000,000
Pollution	2,000,000
 <i>Mobile Equipment - SDRMA</i>	
Mobile/Contractors equipment	1,000,000,000
 <i>General liability - SDRMA</i>	
Bodily Injury and Property Damage	10,000,000
Public Officials Personal	500,000
Employment Benefits	10,000,000
Employee/Public Officials E & O	10,000,000
Employment Practices Liability	10,000,000
Employee/Public Officials Dishonesty	1,000,000
 <i>Workers' Compensation Program - SDRMA</i>	
Employers Liability	5,000,000
 <i>Auto Liability - SDRMA</i>	
Auto, Bodily Injury, & Property Damage	10,000,000

Settled claims have not exceeded any of the District's coverage amounts in the last three fiscal years, and there were no reductions in coverage from the previous fiscal year.

***NOTE 8 – JOINT POWER AUTHORTIES (JPA)***

**South Orange County Wastewater Authority (a California Joint Powers Authority) (SOCWA)**

The District is one of ten member agencies that participate in SOCWA. SOCWA treats, beneficially reuses, and disposes of wastewater in South Orange County. SOCWA operates three wastewater treatment plants (“WWTP”) and two ocean outfalls in the region. SOCWA has ten member agencies, including three cities and seven water districts. A Board of Directors consisting of representatives from member agencies governs SOCWA. The Board of Directors governs the operations of SOCWA, including selection of management and approval of the annual budget. SOCWA has Project Committees that member agencies participate in financially at various levels, depending on their capacity rights. Each WWTP is a project, as well as various other physical facilities, such as outfall pipelines.

## **EMERALD BAY SERVICE DISTRICT**

### **NOTES TO FINANCIAL STATEMENTS JUNE 30, 2018**

#### ***NOTE 8 – JOINT POWER AUTHORTIES (JPA), CONTINUED***

The District's overall participation level is approximating 0.4% of SOCWA. The District deposits money with SOCWA to cover its share of operation and capital in the project committees in which the District participates. At fiscal year-end SOCWA analyzes its actual costs and refunds or collects additional money from its members as appropriate. Construction deposits made to SOCWA for capital projects are recorded as capital assets. The District paid \$133,218 for operating and maintenance, and \$87,059 for capital projects to SOCWA for the year ended June 30, 2018.

SOCWA, the District, and two other SOCWA members are currently involved in a legal dispute with the Moulton Niguel Water District. The District expended \$145,126 in legal fees related to this legal dispute for the fiscal year ended June 30, 2018.

To obtain complete financial information from SOCWA please contact SOCWA's Controller at 34156 Del Obispo Street, Dana Point, California, 92629.

#### ***NOTE 9 – FIRE STATION LEASE***

The District has provided the Orange County Fire Authority (OCFA) a rent-free lease of the fire station located within the District's boundaries. The lease has been provided to the OCFA under a three party mutual lease agreement with the OCFA and the EBCA dated March 28, 2013. The original lease was for a term of 5 years. At the expiration of the initial term, the District exercised the 1 year lease extension which is currently in effect.

#### ***NOTE 10 – AFFILIATED ORGANIZATIONS***

As described in Note 1, the District's purpose includes providing fresh water supply and fire protection to the residents of the District. Currently, the Laguna Beach County Water District (LBCWD) provides the District's residents with its fresh water supply on behalf of the District. The infrastructure for the fresh water supply is under the District's administration; however, the charges for the supplied fresh water to the residents billed by the LBCWD directly.

#### ***NOTE 11 – REIMBURSEMENT AGREEMENT***

On June 20, 2018, the District entered into a reimbursement agreement with the owners of #12/#20/#22 Emerald Bay. The properties are in development, and require new water service. Under the agreement, the District is responsible for \$65,000 of the project costs for infrastructure, with the property owners paying the remaining \$18,000 of the project costs. As of June 30, 2018, the project has not yet been started.

Additionally, as of June 30, 2018, the District reported a receivable of \$28,529 from owners within the District related to a reimbursement of improvements made by the District which benefited the owners. The amount was received by the District in October 2018.

**EMERALD BAY SERVICE DISTRICT**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2018**

***NOTE 12 – RESTATEMENT***

The District has restated certain balances within the General Fund as described below. The restatement resulted in the following adjustments to fund balance as of July 1, 2017:

	<u>General Fund</u>
Beginning of year, as previously reported Fund balance	\$ 2,998,400
Effect of removal of notes payable and related accrued interest and debt activity from General Fund as they don't use current financial resources:	
Accrued Interest	52,287
Notes Payable	<u>7,758</u>
Beginning of year, as restated:	
Fund balance	<u><u>\$ 3,058,445</u></u>

The proforma effect of the restatement on the impacted balances is shown below:

	June 30, 2017 Previously reported	Restatement	June 30, 2017 Restated
General Fund:			
Accrued Interest	\$ 52,287	\$ (52,287)	\$ -
Notes Payable	7,758	(7,758)	-

The restatement impacted the results of operations for the year ended June 30, 2017 as follows:

	June 30, 2017 Previously reported	Restatement	June 30, 2017 Restated
General Fund:			
Change in Fund balance	\$ (3,141,243)	\$ 10,002	\$ (3,131,241)

**REQUIRED SUPPLEMENTARY INFORMATION**

**EMERALD BAY SERVICE DISTRICT**

**SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN  
FUND BALANCE – BUDGET AND ACTUAL – GENERAL FUND  
FOR THE YEAR ENDED JUNE 30, 2018**

	Original Budget	Final Budget	Actual	Variance Positive (Negative)
<b>Revenues:</b>				
Taxes	\$ 2,270,550	\$ 2,307,974	\$ 2,379,517	\$ 71,543
Intergovernmental	-	-	12,292	12,292
Investment income	7,000	7,000	30,612	23,612
Other	13,200	13,200	17,350	4,150
Total revenues	<u>2,290,750</u>	<u>2,328,174</u>	<u>2,439,771</u>	<u>111,597</u>
<b>Expenditures:</b>				
Current:				
General government	633,050	862,300	824,586	37,714
Public services water and sewer services	374,600	358,600	264,667	93,933
Recreation and safety	339,300	347,800	325,066	22,734
Capital outlay	1,624,754	1,664,500	1,371,450	293,050
Debt service:				
Principal retirement	273,364	273,364	273,364	-
Interest and fiscal charges	225,974	225,974	221,934	4,040
Total expenditures	<u>3,471,042</u>	<u>3,732,538</u>	<u>3,281,067</u>	<u>451,471</u>
Net change in fund balance	<u>(1,180,292)</u>	<u>(1,404,364)</u>	<u>(841,296)</u>	<u>563,068</u>
Fund Balance, beginning as restated	<u>3,058,445</u>	<u>3,058,445</u>	<u>3,058,445</u>	
Fund Balance, ending	<u>\$ 1,878,153</u>	<u>\$ 1,654,081</u>	<u>\$ 2,217,149</u>	<u>\$ 563,068</u>

See accompanying notes to the required supplementary information.

**EMERALD BAY SERVICE DISTRICT**

**NOTE TO REQUIRED SUPPLEMENTARY INFORMATION  
FOR THE YEAR ENDED JUNE 30, 2018**

***NOTE 1 – BUDGETS AND BUDGETARY ACCOUNTING***

The District's budget for the General Fund is prepared annually and approved and adopted in accordance with the provisions of the Board of Directors. Any deficiency of budgeted revenues compared to budgeted expenditures is financed from beginning unrestricted fund balance.

Unexpended and unencumbered appropriations of the governmental fund automatically lapse at the end of the fiscal year for noncapital projects. The level at which expenditures may not legally exceed appropriations is the fund level.

**OTHER INFORMATION**

**EMERALD BAY SERVICE DISTRICT**

**GENERAL FUND  
FUNCTIONAL EXPENDITURES BUDGETARY COMPARISON SCHEDULE  
FOR THE YEAR ENDED JUNE 30, 2018**

	Original Budget	Final Budget	Actual	Variance Positive (Negative)
<b>General government</b>				
Staff salary	\$ 92,250	\$ 92,500	\$ 90,000	\$ 2,500
Payroll taxes	7,200	7,200	7,074	126
Workers compensation	1,600	1,600	1,351	249
Employee benefits	12,000	14,000	13,693	307
Personnel administration	4,000	4,000	1,442	2,558
Property tax collection fees	6,000	6,000	5,760	240
County of Orange - tax administration charge	16,000	16,000	12,878	3,122
Administration miscellaneous expense	5,000	5,000	5,012	(12)
Computer services	2,500	2,500	2,357	143
Insurance	47,000	47,000	33,257	13,743
Telephone	3,500	3,500	2,101	1,399
Memberships and contributions	9,000	9,000	8,064	936
Management services	258,000	258,000	260,032	(2,032)
LAFCO annual contribution	10,000	10,000	9,775	225
Lease Vehicle/truck	9,000	9,000	6,742	2,258
District website	2,000	2,000	1,177	823
Accounting fees	40,000	40,000	44,464	(4,464)
Audit	8,000	8,000	7,900	100
Legal fees	60,000	300,000	300,463	(463)
Professional services - engineering	20,000	10,000	1,128	8,872
Engineer surveys and expenses	1,000	1,000	-	1,000
Annual regulatory permits	8,000	8,000	6,581	1,419
Plan check fees	10,000	8,000	3,335	4,665
Interest expense	1,000	-	-	-
Total general government	633,050	862,300	824,586	37,714
<b>Public services water and sewer services</b>				
Sewage treatment services	138,000	138,000	133,218	4,782
North Coast Interceptor	20,000	22,000	-	22,000
Maintenance Equipment	13,000	13,000	2,846	10,154
Maintenance vehicle fuel and repairs	13,000	13,000	8,515	4,485
Sewer Lift Station - Monthly Inspections	6,000	6,000	1,639	4,361
Sewer lift station - electricity	13,000	13,000	7,604	5,396
Sewer list station - water	2,000	2,000	2,503	(503)
Supplies and chemicals	2,000	2,000	639	1,361
Sewer repair and maintenance	55,000	55,000	22,637	32,363
Sewer pipeline system cleaning	54,600	54,600	56,146	(1,546)
Water and sewer system condition assessment	50,000	40,000	25,313	14,687
Water conservation	5,000	-	2,557	(2,557)
Misc. water expense	3,000	-	1,050	(1,050)
Total public services water and sewer services	374,600	358,600	264,667	93,933

(continued)

**EMERALD BAY SERVICE DISTRICT**

**GENERAL FUND**

**FUNCTIONAL EXPENDITURES BUDGETARY COMPARISON SCHEDULE, CONTINUED  
FOR THE YEAR ENDED JUNE 30, 2018**

	Original Budget	Final Budget	Actual	Variance Positive (Negative)
<b>Recreation and safety</b>				
Beach Lifeguards	127,000	164,500	159,661	4,839
Fireworks	39,000	39,000	37,037	1,963
Fireworks - Barge	27,000	27,000	24,210	2,790
Fireworks - Chase Boat	2,000	2,000	1,700	300
Fuel mod/weed abatement	42,000	42,000	42,297	(297)
Emergency Storm Contingency	30,000	15,000	-	15,000
Storm drain cleaning	48,300	48,300	49,790	(1,490)
Drills and Training	5,000	1,000	125	875
EOC Supplies/Miscellaneous	5,000	5,000	2,426	2,574
CERT Communications	8,000	1,000	4,313	(3,313)
Miscellaneous/CERT Expense	6,000	3,000	3,507	(507)
Total Recreation and safety	<u>339,300</u>	<u>347,800</u>	<u>325,066</u>	<u>22,734</u>
Debt service	499,338	499,338	495,298	4,040
Capital outlay	<u>1,624,754</u>	<u>1,664,500</u>	<u>1,371,450</u>	<u>293,050</u>
Total expenditures	<u>\$ 3,471,042</u>	<u>\$ 3,732,538</u>	<u>\$ 3,281,067</u>	<u>\$ 451,471</u>

**OTHER REPORT**



**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Directors  
Emerald Bay Service District

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities and the General Fund of the Emerald Bay Service District (District) as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated December 3, 2018. Our report included an emphasis of matter regarding the District's restatement of the General Fund, as of July 1, 2017.

**Internal Control over Financial Reporting**

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and responses as items 2018-001, 2018-002, and 2018-003 that we consider to be significant deficiencies.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs as item 2018-004.

## **District's Response to Findings**

The District's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. The District's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

## **Purpose of this Report**

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

*Yavrinek, Trine, Day & Co., LLP*

Laguna Hills, California  
December 3, 2018

**EMERALD BAY SERVICE DISTRICT  
SCHEDULE OF FINDINGS AND RESPONSES  
FOR THE FISCAL YEAR ENDED JUNE 30, 2018**

*Finding Number 2018-001*

**FINANCIAL REPORTING AND CLOSING**

*Criteria:*

There should be sufficient procedures in place to allow for the proper classification and timely reporting of financial information in accordance with generally accepted accounting principles.

*Condition:*

During the audit, we identified adjustments for the following:

- Restatement of fund balance of the General Fund for \$60,045 to exclude notes payable and accrued interest on debt, as these balances do not use current financial resources, and are excluded from governmental funds.
- Bank reconciling items – \$20,691 of adjustments to cash described under Finding Number 2018-002.
- Reclassification of fund balance to report \$600,000 as assigned fund balance, and reclassify remaining amounts as unassigned fund balance in accordance with GAAP.
- Adjustments to the footnotes to include long term liability rollforward and 5-year repayment schedule required in accordance with GAAP.

*Context:*

The condition was noted during our audit of the District for the year ended June 30, 2018.

*Effect:*

Journal entries were posted, and the financial statement footnotes were modified, in order to fairly present the financial statements.

*Cause:*

The District's procedures did not allow for the proper classification or timely reporting of information required for financial reporting.

*Recommendation:*

We recommend the District review its closing policies and procedures to ensure amounts are properly classified and properly reported in a timely manner.

**EMERALD BAY SERVICE DISTRICT  
SCHEDULE OF FINDINGS AND RESPONSES, CONTINUED  
FOR THE FISCAL YEAR ENDED JUNE 30, 2018**

*Views of Responsible Officials and Planned Corrective Actions:*

The District will evaluate and adjust the financial reporting and closing to be more timely and to conform with GAAP.

*Finding Number 2018-002*

**BANK RECONCILIATIONS**

*Criteria:*

Bank reconciliations should be prepared and reviewed on a timely basis. A signature demonstrating the performance of the preparation and review should be evident. To strengthen the segregation of duties between those who post to the general ledger and those who handle cash receipts and disbursements, review of the bank reconciliation should be performed by a separate individual for additional review and transparency.

*Condition:*

We noted the June 2018 bank reconciliation was prepared on a timely basis. However there were no signatures of the preparer or reviewer as evidence of the reconciliation preparation or review. Further, we identified two outstanding checks written in January 2018 on the reconciliation which had not cleared the bank as of June 30, 2018. As a result, journal entries were proposed and posted:

- \$14,091 – amounts related to a duplicate check – outstanding check and related expenditure were reversed
- \$6,600 – check was not received by the vendor – as a result, the District identified an additional accrual due to vendor, resulting in reversing the check, and recording a \$15,303 payable as of June 30, 2018.

*Context:*

The condition was noted during our review of the internal controls over the bank reconciliation process, as well as our testwork over the June 30, 2018 bank reconciliation.

*Effect:*

Journal entries were posted in order to fairly present the cash balances as of June 30, 2018.

*Cause:*

The District did not consistently document preparation and review of the bank reconciliations.

*Recommendation:*

As a key internal control, the process could be strengthened through including the signatures of the preparer and reviewer. Additionally, in small organizations, additional review of the bank reconciliation may be beneficial in strengthening the segregation of duties and overall control environment. We recommend the District implement procedures to ensure that the preparation and review of the bank reconciliations is formally documented, and the reconciliations are reviewed by a separate individual.

Additionally, we recommend the District consider a policy for treatment of stale checks.

**EMERALD BAY SERVICE DISTRICT  
SCHEDULE OF FINDINGS AND RESPONSES, CONTINUED  
FOR THE FISCAL YEAR ENDED JUNE 30, 2018**

***Views of Responsible Officials and Planned Corrective Actions:***

Staff will prepare and submit a monthly package to the General Manager and Treasurer which will include a copy of the District's checking account statement, the Bank Reconciliation Report and the check register for their review. Checks that are over 90 days old will be researched and voided or reissued.

***Finding Number 2018-003***

**JOURNAL ENTRIES**

***Criteria:***

There should be sufficient segregation of duties over journal entries, including authorization, custody of assets (check writing), and recordkeeping (posting to the general ledger). This includes secondary review of all journal entries posted to the system.

***Condition:***

We noted journal entries are generally prepared and posted by the same individual, with no evidence of secondary review.

***Context:***

The condition was noted during our review of the internal controls over the journal entry process.

***Effect:***

Journal entries may be posted without secondary review, resulting in an increased risk of error in the account records.

***Cause:***

The District's process does not properly ensure a separate preparer and reviewer for all journal entries.

***Recommendation:***

We recommend that the District review the procedures over journal entries to ensure timely review and posting to the general ledger.

***Views of Responsible Officials and Planned Corrective Actions:***

Staff will prepare and submit a monthly package to the General Manager and Treasurer which will include a list of the Adjusting Journal Entries recorded for the General Manager and Treasurer to review.

**EMERALD BAY SERVICE DISTRICT  
SCHEDULE OF FINDINGS AND RESPONSES, CONTINUED  
FOR THE FISCAL YEAR ENDED JUNE 30, 2018**

*Finding Number 2018-004*

**PUBLIC FUNDS DEPOSITS AND COLLATERALIZATION**

*Criteria:*

The Federal Deposit Insurance Corporation (FDIC) insures deposits up to \$250,000. Further, 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 100 percent of the total amount deposited by the public agencies. California law also allows financial institutions to secure deposits by pledging first trust deed mortgage notes having a value of 150 percent of the secured public deposits.

*Condition:*

The District's Cash Preferred Deposit account totaling \$56,532 as of June 30, 2018 is not FDIC insured. Further, the District's deposit balance of \$158,605 is not held in an account collateralized in accordance with California Government Code.

*Context:*

The condition was noted during our testwork over the District's cash and deposit accounts.

*Effect:*

\$56,532 of District funds are not subject to FDIC insured limits. Also the District's cash balance of \$158,605 is not collateralized in accordance with California Government Code.

*Cause:*

The District did not ensure the deposit accounts were properly collateralized or insured by the FDIC.

*Recommendation:*

We recommend the District consider obtaining the required collateralization required under government code, or close the accounts.

*Views of Responsible Officials and Planned Corrective Actions:*

The District will work with Bank of America to ensure that all deposits are collateralized and the funds that are currently held in with Merrill Lynch will be transferred into either the Bank of America checking account or the District's LAIF Account.

**EMERALD BAY SERVICE DISTRICT  
SCHEDULE OF PRIOR YEAR FINDINGS AND STATUS OF CORRECTIVE ACTION  
FOR THE FISCAL YEAR ENDED JUNE 30, 2018**

**Financial Statement Findings**

None reported.