

**PALMDALE RECYCLED WATER AUTHORITY
PALMDALE, CALIFORNIA**

**BASIC FINANCIAL STATEMENTS
WITH INDEPENDENT AUDITOR'S REPORT
AND REQUIRED SUPPLEMENTARY INFORMATION**

FOR THE YEAR ENDED DECEMBER 31, 2016

PALMDALE RECYCLED WATER AUTHORITY
BASIC FINANCIAL STATEMENTS
WITH INDEPENDENT AUDITOR'S REPORT
AND REQUIRED SUPPLEMENTARY INFORMATION
DECEMBER 31, 2016

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Palmdale Recycled Water Authority
Palmdale, California

Report on the Financial Statements

We have audited the accompanying financial statements of the Palmdale Recycled Water Authority (Authority), as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the Authority'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 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 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 opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of December 31, 2016, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 5 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated May 1, 2017, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.

Vavrinick, Trine, Day & Co. LLP

Rancho Cucamonga, California

May 1, 2017

**PALMDALE RECYCLED WATER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2016**

The following is a brief discussion of the Palmdale Recycled Water Authority (Authority) activities and financial performance for the year ended December 31, 2016. Please read in conjunction with the Authority's basic financial statements and accompanying notes which follow this section.

FINANCIAL HIGHLIGHTS

- The Authority's net position at December 31, 2016 was \$641,359, an increase of \$181,512 from the prior year. The increase is due to the continuous member contributions and water sales.
- The Authority's total liabilities at December 31, 2016 were \$79,600.
- The Authority's operating revenues decreased by \$2,941 primarily as the result of lower usage on recycled water sales to the City of Palmdale and vendors (contractors) for construction use.
- The Authority's operating expenses increased by \$21,400 during 2016. Engineering costs increased during the year as the Authority continued working on the design of Recycled Water Facilities Plan.

MEASUREMENT FOCUS AND BASIS OF ACCOUNTING

Measurement focus is a term used to describe which transactions are recorded within the various financial statements. Basis of accounting refers to when transactions are recorded regardless of the measurement focus applied. The accompanying financial statements are reported using the economic resources measurement focus and the accrual basis of accounting.

Under the economic resources measurement focus all assets and liabilities (whether current or noncurrent) associated with these activities are included on the Statement of Net Position. The Statement of Revenues, Expenses and Changes in Net Position present increases (revenues) and decreases (expenses) in total net position. Under the accrual basis of accounting, revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

OVERVIEW OF THE BASIC FINANCIAL STATEMENTS

The Authority's financial statements, prepared in accordance with generally accepted accounting principles (GAAP), offer key, high-level financial information about Authority's activities during the reporting period. The financial statements of the Authority consist of three interrelated statements designed to provide the reader with relevant information on the Authority's financial condition and operating results. These statements offer short-term and long-term financial information about the Authority's activities utilizing the full accrual basis of accounting.

The *Balance Sheet* includes all the Authority's assets, less liabilities, and provides information about the nature and amounts of investments in resources (assets) and the obligations to the Authority's creditors (liabilities), with the difference being reported as net position. It also provides the basis for computing rate of return, evaluating the capital structure of the Authority, and assessing the liquidity and financial flexibility of the Authority.

All the current year's revenues and expenses are accounted for in the *Statement of Revenues, Expenses, and Changes in Net Position*. This statement measures the Authority's operations over the past year and can be used to determine whether the Authority has successfully recovered all its projected costs through its member contributions.

**PALMDALE RECYCLED WATER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2016**

The final required financial statement is the *Statement of Cash Flows* which presents information about the Authority's cash receipts and cash payments during the reporting period classified as cash receipts, cash payments, and net changes in cash resulting from operations, investing, and non-capital financing and capital and related financing activities.

FINANCIAL ANALYSIS OF THE AUTHORITY

Our analysis of the Authority begins on page 3 of the Management's Discussion and Analysis. One of the most important questions asked about the Authority's finances is: "Is the Authority, as a whole, better off or worse off as a result of the year's activities?" The Statement of Net Position and the Statement of Revenues, Expenses, and Changes in Net Position and Statement of Cash Flows report information about the Authority's activities in a way that will help answer this question. These two statements report the net position of the Authority and changes in them. You can think of the Authority's net position as the difference between assets and liabilities as one way to measure financial health or financial position. Over time, increases or decreases in the Authority's net position is one indicator of whether its financial health is improving or deteriorating. However, you will need to consider other non-financial factors such as changes in economic conditions, population growth, changes in rates and charges and new or changed government legislation or accounting standards.

STATEMENT OF NET POSITION

The Statement of Net Position is the difference between assets and liabilities, and may serve over time as a useful indicator of a government's financial position. The following is a summary of the Authority's Balance Sheet as of December 31.

Condensed Statement of Net Position

	2016	2015
Cash and Cash Equivalents	\$ 717,540	\$ 490,783
Accounts Receivable	3,419	32,938
Prepaid Expenses	-	2,552
Total Assets	<u>720,959</u>	<u>526,273</u>
 Total Liabilities	 79,600	 66,426
Unrestricted Net Position	<u>641,359</u>	<u>459,847</u>
Total Liabilities and Net Position	<u>\$ 720,959</u>	<u>\$ 526,273</u>

As can be seen from the financial statement summary above the Authority's assets exceed liabilities by \$641,359, as of December 31, 2016. The Authority's Net Position increased by \$181,512 or 39.5 percent, primarily as the result of annual contributions received from the Authority's members, receiving grant funds and water usage and meter revenues invoiced of \$91,359 while operating expenses increased by \$21,400 compared to 2015.

**PALMDALE RECYCLED WATER AUTHORITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED DECEMBER 31, 2016**

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

While the Balance Sheet shows the net position, the Statement of Revenues, Expenses, and Changes in Net Position provides information as to the nature and source of these changes. The Authority reported an increase in net position of \$181,512 for the year ended December 31, 2016 as compared to the prior year. The following is a summary of the change in the Authority's net position for the year ended December 31.

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

	<u>2016</u>	<u>2015</u>
Operating Revenues:		
Membership Contributions	\$ 200,000	\$ 200,000
Grant Funds	19,418	0
Water and Meter Sales	91,247	113,010
Miscellaneous	112	708
	<u>310,777</u>	<u>313,718</u>
Non-operating Revenue		
Interest Revenue	1,051	469
Total Revenues	<u>311,828</u>	<u>314,187</u>
Expenses:		
Operating Expenses	130,316	108,916
Change in Net Position	181,512	205,271
Net Position - January 1	<u>459,847</u>	<u>254,576</u>
Net Position - December 31	<u>\$ 641,359</u>	<u>\$ 459,847</u>

The changes in net position, is directly related to the Authority's member support to offset operating cost. The Authority received grant funds from a planning grant awarded by the State Water Resources Control Board. Also, during 2016 the Authority continued to provided water and billed vendors for construction activities. The Authority installed meters for various construction companies to utilize recycled water instead of using potable water for construction activities. This allowed the members of the Authority to further utilize recycled water and freeing up potable water usage.

CONTACTING THE AUTHORITY'S FINANICAL MANAGEMENT

This financial report is intended to provide the Board of Directors, customers, taxpayers, creditors, and other interested parties with general overview of the Authority's financial operations and condition at the year ended December 31, 2016, and to demonstrate the Authority's accountability for the funds it receives. If you have any questions about this report or need additional information, you may contact Palmdale Water District, Finance Department, at 2029 E Avenue Q, Palmdale, CA 93550. (661) 947-4111. <http://www.cityofpalmdale.org/Your-City-Hall/Boards-and-Commissions/PRWA>

PALMDALE RECYCLED WATER AUTHORITY

Balance Sheet
December 31, 2016

ASSETS

Current Assets:

Cash and Cash Equivalents	\$ 717,540
Accounts Receivable	<u>3,419</u>
Total Assets	<u>\$ 720,959</u>

LIABILITIES

Current Liabilities:

Customer Deposits	\$ 9,500
Accounts payable	<u>70,100</u>
Total Liabilities	<u>79,600</u>

NET POSITION

Unrestricted	<u>641,359</u>
Total Liabilities and Net Position	<u>\$ 720,959</u>

See accompanying notes to the financial statements

PALMDALE RECYCLED WATER AUTHORITY
Statement of Revenues, Expenses and Changes in Net Position
For the Year Ended December 31, 2016

OPERATING REVENUES

Member Agency Contributions	\$ 200,000
Grant Funds	19,418
Water Sales	59,472
Meter Sales	31,775
Miscellaneous	112
Total Operating Revenues	310,777

OPERATING EXPENSES

Contract Services-Engineering Services	90,891
Contract Services-Auditing Services	10,000
Membership and Dues	2,552
Travel and Meetings	750
Payroll Taxes	58
Marketing and Outreach	5,922
Utilities-Water	20,143
Total Operating Expenses	130,316
Operating Income	180,461

NON-OPERATING REVENUE

Investment Income	1,051
Total Non-Operating Revenue	1,051
Change in Net Position	181,512
Net Position-Beginning of Year	459,847
Net Position-End of Year	\$ 641,359

See accompanying notes to the financial statements

PALMDALE RECYCLED WATER AUTHORITY

Statement of Cash Flows

For the Year Ended December 31, 2016

Cash Flows from Operating Activities:

Cash Received from Member Agencies	\$ 200,000
Cash Received from Grant Funds	19,418
Cash Received from Water Sales	107,388
Cash Payments to Suppliers	<u>(101,100)</u>

Net Cash Provided by Operating Activities	<u>225,706</u>
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Cash Flows from Investing Activities:

Investment Income	<u>1,051</u>
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Net increase in cash and cash equivalents	226,757
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Cash and cash equivalents at the beginning of the year	<u>490,783</u>
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Cash and cash equivalents at the end of the year	<u><u>\$ 717,540</u></u>
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Reconciliation of operating income to net cash provided by operating activities:

Operating Income	\$ 180,461
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Change in accounts receivable:

Decrease in accounts receivable	29,518
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Change in prepaid expenses:

Decrease in prepaid memberships	2,552
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Change in liabilities:

Decrease in water sales deposits	(3,000)
Increase in accounts payable	<u>16,175</u>

Net cash provided by operating activities	<u><u>\$ 225,706</u></u>
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See accompanying notes to the financial statements

PALMDALE RECYCLED WATER AUTHORITY

Notes to the Basic Financial Statements
For the Year Ended December 31, 2016

Note 1- Organization and Summary of Significant Accounting Policies

A. Reporting Entity

The Palmdale Recycled Water Authority (Authority) was formed under a Joint Exercise of Powers Authority on September 26, 2012, pursuant to Sections 6506 and 6507 of the Exercise of Powers Act, codified at California Government Code sections 6500, authorizes public agencies by agreement to exercise jointly any power common to the contracting parties. The Authority was formed between the City of Palmdale, a California Charter City (City) and the Palmdale Water District, an Irrigation District under Division 11 of the California Water Code (PWD). The Authority is an independent public agency separate from the Members.

The purpose of the Authority is to establish an independent public agency to study, promote, develop, distribute, construct, install, finance, use and manage recycled water resources created by the Los Angeles County Sanitation District Nos. 14 and 20 for any and all reasonable and beneficial uses, including irrigation and recharge, and to finance the acquisition and construction or installation of recycled water facilities, recharge facilities and irrigation systems.

B. Basic Financial Statements

The Authority's basic financial statements consist of the Statement of Net Position, the Statement of Revenues, Expenses and Changes in Net Position, the Statement of Cash Flows, and the Notes to the Basic Financial Statements.

C. Basis of Presentation

The Authority accounts for its activities as an enterprise fund. An enterprise fund is a proprietary type fund 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. The Authority's basic financial statements are reported using the economic resources measurement focus and the full accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place.

The accounting policies of the Authority are in conformity with generally accepted accounting principles applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing accounting and financial reporting principles.

PALMDALE RECYCLED WATER AUTHORITY

Notes to the Basic Financial Statements For the Year Ended December 31, 2016

D. Net Position

In the Balance Sheet, net position is classified in the following categories:

- Unrestricted net position – This amount is the net amount of the assets and liabilities that are not included in the determination of net investment in capital assets or the restricted component of net position.

When both restricted and unrestricted resources are available, it is the Authority's policy to use restricted resources first and then unrestricted resources as they are needed.

E. Operating and Non-Operating Revenues and Expenses

Operating revenues consist of charges for water sales to customers for recycled water and member contributions to defray the cost of the Authority's operation. Operating expenses include the cost of sales and services, maintenance of capital assets and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

F. Cash and Cash Equivalents

Cash and cash equivalents include demand deposits. For the purpose of the Statement of Cash Flows, cash and cash equivalents are defined as short-term deposits with original maturities of three months or less from the date of acquisition.

G. Use of 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 assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

H. Implemented Accounting Pronouncements

During 2016, the Authority adopted GASB Statement No. 72, *Fair Value Measurement and Application*. This Statement requires disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques. These disclosures should be organized by type of asset or liability reported at fair value. It also requires additional disclosures regarding investments in certain entities that calculate net asset value per share (or its equivalent). The requirements of this Statement are effective for financial statements for periods beginning after June 15, 2015. The implementation did not have any impact on the Authority's financial statements.

PALMDALE RECYCLED WATER AUTHORITY

Notes to the Basic Financial Statements For the Year Ended December 31, 2016

During 2016, the Authority adopted GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. The provisions in Statement 73 are effective for fiscal years beginning after June 15, 2015—except those provisions that address employers and governmental non-employer contributing entities for pensions that are not within the scope of Statement 68, which are effective for fiscal years beginning after June 15, 2016. The implementation did not have any impact on the Authority's financial statements.

During 2016, the Authority adopted GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to identify—in the context of the current governmental financial reporting environment—the hierarchy of Generally Accepted Accounting Principles (GAAP). This Statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The implementation did not have any impact on the Authority's financial statements.

During 2016, the Authority adopted GASB Statement No. 78, *Pensions Provided through Certain Multiple-Employer Defined Pension Plans*. This statement is intended to assist governments that participate in certain multiple-employer defined benefit pension plans to meet the reporting requirements of GASB 68, *Accounting and Financial Reporting for Pension*. The implementation did not have any impact on the Authority's financial statements.

During 2016, the Authority adopted GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*. This statement permits qualifying external investment pools to measure pool investments at amortized cost for financial reporting purposes. The Statement provides guidance that will allow many pools to continue to qualify for amortized cost accounting. The implementation did not have any impact on the Authority's financial statements.

During 2016, the Authority adopted GASB Statement No. 80, *Blending Requirements for Certain Component Units – an Amendment of GASB Statement No. 14*. This Statement amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of Statement No. 39, *Determining Whether Certain Organizations Are Component Units*. The implementation did not have any impact on the Authority's financial statements.

PALMDALE RECYCLED WATER AUTHORITY

Notes to the Basic Financial Statements For the Year Ended December 31, 2016

I. New Future Accounting Pronouncements

GASB Statement No. 74 – In June 2015, GASB issued Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. Statement No. 74 replaces Statements No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, as amended*, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*. It also includes requirements for defined contribution OPEB plans that replace the requirements for those OPEB plans in Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans, as amended*, Statement 43, and Statement No. 50, *Pension Disclosures*. The provisions in Statement 74 are effective for fiscal years beginning after June 15, 2016. The Authority has not determined its effect on the financial statements.

GASB Statement No. 75 - In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Statement 75 establishes new accounting and financial reporting requirements for governments whose employees are provided with OPEB, as well as for certain non-employer governments that have a legal obligation to provide financial support for OPEB provided to the employees of other entities. The provisions in Statement 75 are effective for fiscal years beginning after June 15, 2017. The Authority has not determined its effect on the financial statements.

GASB Statement No. 77 – In August 2015, GASB issued Statement No. 77, *Tax Abatement Disclosures*. The objective of this Statement is to provide financial statement users with essential information about the nature and magnitude of the reduction in tax revenues through tax abatement programs. This statement is not effective until the fiscal year ending June 30, 2017. The Authority has not determined the effect of this statement.

GASB Statement No. 81 – In March 2016, GASB issued Statement No. 81, *Irrevocable Split-Interest Agreements*. This Statement addresses accounting and financial reporting for certain external investment pools and pool participants. Specifically, it establishes criteria for an external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes. If an external investment pool does not meet the criteria established by this Statement, that pool should apply the provisions in paragraph 16 of Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, as amended. This Statement is effective after June 15, 2015. The Authority has not determined the effect on the financial statements.

PALMDALE RECYCLED WATER AUTHORITY

Notes to the Basic Financial Statements For the Year Ended December 31, 2016

GASB Statement No. 82 – In March 2016, GASB issued Statement No. 82, *Pension Issues—an amendment of GASB Statements No. 67, No. 68, and No. 73*. The objective of this Statement is to address certain issues that have been raised with respect to Statements No. 67, Financial Reporting for Pension Plans, No. 68, Accounting and Financial Reporting for Pensions, and No. 73, Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68. This Statement is effective after June 15, 2016. The Authority has not determined the effect on the financial statements.

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 assets should recognize a liability based on the guidance in this Statement. This Statement is effective after June 15, 2018 and earlier application is encourage. The Authority has not determined the effect on the financial statements.

GASB Statement No. 84 – In January 2017, GASB issued Statement No. 84, *Fiduciary Activities*. This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. This Statement is effective periods beginning after December 15, 2018 and earlier application is encourage. The Authority has not determined the effect on the financial statements.

GASB Statement No. 85 – In March 2017, GASB issued Statement No. 85, *Omnibus 2017*. The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]).. The requirements of this Statement are effective for reporting periods beginning after June 15, 2017 and earlier application is encourage. The Authority has not determined the effect on the financial statements.

PALMDALE RECYCLED WATER AUTHORITY

Notes to the Basic Financial Statements For the Year Ended December 31, 2016

Note 2- Cash and Investments

Cash and investments at December 31, 2016 are classified in the accompanying financial statements as follows:

Statement of net position:

Cash and Cash Equivalents	<u>\$717,540</u>
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Cash and investments as of December 31, 2016 consist of the following:

Deposits with financial institutions	<u>\$717,540</u>
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A. Investment Policy and Authorized Investments

The Authority is authorized under California Code to make direct investments in local agency bonds, notes, or warrants within the State; U.S. Treasury instruments; registered State warrants or treasury notes; securities of the U.S. Government, or its agencies; bankers acceptances; commercial paper; certificates of deposit placed with commercial banks and/or savings and loan companies; repurchase of reverse repurchase agreements; medium term corporate notes; shares of beneficial interest issued by diversified management companies, certificates of participation, obligations with first priority security; and collateralized mortgage obligations as specified in Section 5366. The Authority does not have a formal policy for investments that is more restrictive than the noted Government Code.

B. Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the Authority 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 Authority does not have a policy of custodial credit risk for deposits. 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 government units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the government 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 deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

PALMDALE RECYCLED WATER AUTHORITY

Notes to the Basic Financial Statements For the Year Ended December 31, 2016

Note 3- Contributions from Member Agencies

Section 5.2 of the Joint Exercise of Powers Agreement creating the Palmdale Recycled Water Authority provides that any member may make contributions of money or assets to the Authority; make or advance payments of public funds to defray the cost of Authority's operation; and contribute personnel, equipment or property instead of or in addition to other contributions or advances. Such contributions shall be paid to and disbursed by the Authority as set out in separate agreements between the Authority and the member and approved by the Board and the governing body of the member. During 2016, each member agency contributed \$100,000.

Note 4- Related Party Transactions

The Board of the Authority has assigned staff from the Palmdale Water District and the City of Palmdale to serve in various administrative duties of the Authority. All payroll cost related to staff time while serving the Palmdale Recycled Water Authority is incurred by the respective agencies and none of the payroll costs are incurred by the Authority nor are they charged to the Authority for such services.

During 2016, the City of Palmdale and various developers purchased recycled water from the Authority in the amount of \$91,359.



**INDEPENDENT AUDITOR'S 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
Palmdale Recycled Water Authority
Palmdale, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Palmdale Recycled Water Authority (Authority), as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements and have issued our report thereon dated May 1, 2017.

Internal Control over Financial Reporting

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

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority'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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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.

Vavrinik, Trine, Day & Co. LLP

Rancho Cucamonga, California

May 1, 2017