

**SANTA CRUZ COUNTY
SANITATION DISTRICT**

**A COMPONENT UNIT OF
THE COUNTY OF SANTA CRUZ**

**BASIC FINANCIAL STATEMENTS AND
INDEPENDENT AUDITOR'S REPORTS**

**FOR THE FISCAL YEAR ENDED
JUNE 30, 2023**

**SANTA CRUZ COUNTY SANITATION DISTRICT
JUNE 30, 2023**

TABLE OF CONTENTS

	<u>Page</u>
<u>FINANCIAL SECTION</u>	
Independent Auditor's Report	1
Management's Discussion and Analysis.....	4
Basic Financial Statements:	
Statement of Net Position	8
Statement of Revenues, Expenses, and Changes in Net Position.....	9
Statement of Cash Flows	10
Notes to the Basic Financial Statements	12
Other Report:	
Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	21
Schedule of Findings and Questioned Costs.....	23

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of the
Santa Cruz County Sanitation District
Santa Cruz, California

Report on the Audit of the Financial Statements

Opinions

We have audited the accompanying basic financial statements of the Santa Cruz County Sanitation District (the District), a component unit of the County of Santa Cruz (the County), as of and for the fiscal year ended June 30, 2023, and the related notes to the basic financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the District as of June 30, 2023, and the respective changes in financial position and cash flows for the fiscal year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinions

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. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the District and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the District's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinions. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 County's internal control relating to the District. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the District's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4-7 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 December 20, 2023, on our consideration of the County's internal control over financial reporting relating to the District and on our tests of the County's 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 County's internal control over financial reporting or on compliance relating to the District. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the County's internal control over financial reporting and compliance relating to the District.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

A handwritten signature in blue ink that reads "Brown Armstrong Accountancy Corporation". The signature is written in a cursive, flowing style.

Bakersfield, California
December 20, 2023

**SANTA CRUZ COUNTY SANITATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2023**

INTRODUCTION

This section of the Santa Cruz County Sanitation District's (the District) annual financial report presents a discussion and analysis of the District's financial performance during the fiscal year that ended June 30, 2023. Please read it in conjunction with the District's basic financial statements following this section.

THE FINANCIAL HIGHLIGHTS

- The assets of the District exceeded liabilities at the close of the 2022/2023 fiscal year by \$146,745,863 (net position). Of this amount, \$15,117,916 (unrestricted) may be used to meet ongoing obligations to citizens and creditors, and \$131,627,947 is the net investment in capital assets.
- The District's total net position increased by \$3,551,916. This is an increase of \$1,340,534 from the prior fiscal year's change in net position. This increase is primarily attributable to a \$2,590,871 increase in charges for services and a \$1,022,864 increase in investment income offset with an increase in expenses of \$2,367,495.

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 comprise two components: (1) Government-wide financial statements, and (2) Notes to the basic financial statements. Fund financial statements are not included in the basic financial statements because all activities of the District are accounted for within a single enterprise fund. Enterprise funds are accounted for using the accrual method of accounting. Required Supplementary Information is included 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 private-sector business.

The *statement of net position* presents information on all District assets and liabilities, with the difference between the two reported as net position. Over time, increases and decreases in net position may serve as a useful indicator of whether or not the financial position of the District is improving or deteriorating.

The *statement of revenues, expenses, and changes in net position* 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 result in cash flows in a future fiscal period.

Both of these government-wide financial statements would distinguish functions of the District that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). However, there are no governmental activities in the District.

Notes to the Basic Financial Statements

The notes to the basic financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide financial statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net position may serve as a useful indicator of a government's financial position. In the case of the District, assets exceeded liabilities by \$146,745,863 at the close of the most recent fiscal year. Further detail is provided in the following table:

Condensed Statements of Net Position

	2023	2022	Increase (Decrease) \$	Increase (Decrease) %
Assets				
Current assets	\$ 18,715,109	\$ 20,172,845	\$ (1,457,736)	-7.2%
Capital assets, net	151,498,053	146,302,682	5,195,371	3.6%
Other noncurrent assets	17,860,273	20,008,924	(2,148,651)	-10.7%
Total Assets	188,073,435	186,484,451	1,588,984	0.9%
Liabilities				
Current liabilities	4,866,296	5,560,836	(694,540)	-12.5%
Noncurrent liabilities	36,461,276	37,729,668	(1,268,392)	-3.4%
Total Liabilities	41,327,572	43,290,504	(1,962,932)	-4.5%
Net Position				
Net investment in capital assets	131,627,947	107,272,683	24,355,264	22.7%
Unrestricted	15,117,916	35,921,264	(20,803,348)	-57.9%
Total Net Position	\$ 146,745,863	\$ 143,193,947	\$ 3,551,916	2.5%

The significant changes in the District's net position are summarized as follows:

- Cash and investments decreased by \$1,457,736 from the prior fiscal year. Further information is presented in the Statement of Cash Flows.
- Capital assets, net increased by \$5,195,371 from the prior fiscal year. Further information is presented under the Capital Assets and Debt Administration section of this Management's Discussion and Analysis.
- Current liabilities decreased by \$694,540 from the prior fiscal year due to the timing of projects.
- Noncurrent liabilities have decreased by \$1,268,392. Further information is presented under the Capital Assets and Debt Administration section of this Management's Discussion and Analysis.

Analysis of Net Position

The largest portion of the District's net position (\$131,627,947) (89.70%) reflects its net investment in capital assets (e.g., pumping stations, transmission systems, mobile equipment, other equipment, sewage treatment plant, and construction in progress), less related debt used to acquire those assets that is still outstanding. The District uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the District's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay these debts must be provided from other sources, since the capital assets themselves cannot be used to liquidate these debts.

The remaining balance of the District's net position (\$15,117,916 (10.30%)) is unrestricted and may be used to meet the District's ongoing obligations to citizens and creditors.

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

	2023	2022	Increase (Decrease) \$	Increase (Decrease) %
Revenues				
Program Revenues				
Charges for services	\$ 31,679,491	\$ 29,088,620	\$ 2,590,871	8.9%
General Revenues				
Aid from other government agencies	189,673	104,436	85,237	81.6%
Investment income	1,101,758	78,894	1,022,864	1296.5%
Gain on sale of capital assets	9,409	-	9,409	100.0%
Total Revenues	32,980,331	29,271,950	3,708,381	12.7%
Expenses				
Sanitation District	29,428,415	27,060,568	2,367,847	8.8%
Total Expenses	29,428,415	27,060,568	2,367,847	8.8%
Change in Net Position	3,551,916	2,211,382	1,340,534	60.6%
Net Position, Beginning	143,193,947	140,982,565	2,211,382	1.6%
Net Position, Ending	\$ 146,745,863	\$ 143,193,947	\$ 3,551,916	2.5%

Analysis of Changes in Net Position

The District's change in net position was \$3,551,916 for the current fiscal year. This is an increase of \$1,340,534 from the prior fiscal year's change in net position. This increase is primarily attributable to a \$2,590,871 increase in charges for services and an increase in investment income of \$1,022,864, offset with an increase in expenses of \$2,367,847.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The District's net capital assets as of June 30, 2023, amounted to \$151,498,053. These net capital assets include pumping stations, transmission systems, mobile equipment, other equipment, sewage treatment plant, and construction in progress.

The net increase in the District's capital assets (net book value) for the current period was \$5,195,371, or 3.6%.

Major capital asset events during the current fiscal year included the following:

- Increase to construction in progress amounted to \$6,202,398.
- Pumping station systems increased by \$470,318, which included construction in progress completions of \$301,622.
- The majority of the remaining changes in capital assets were additions of \$4,697,977 offset by depreciation expense of \$6,175,322.

The District's capital assets are presented below by type to illustrate changes from the prior fiscal year:

	2023	2022	Increase (Decrease) \$	Increase (Decrease) %
Pumping station systems	\$ 62,687,756	\$ 62,217,438	\$ 470,318	0.8%
Transmission systems	149,658,708	146,341,547	3,317,161	2.3%
Sewage treatment plant	35,924,625	35,924,625	-	0.0%
Construction in progress	12,797,564	6,595,166	6,202,398	94.0%
Mobile equipment	5,071,342	4,846,534	224,808	4.6%
Other equipment	3,817,570	2,661,562	1,156,008	43.4%
Total cost	269,957,565	258,586,872	11,370,693	4.4%
Less accumulated depreciation	(118,459,512)	(112,284,190)	6,175,322	5.5%
Capital assets, net	\$ 151,498,053	\$ 146,302,682	\$ 5,195,371	3.6%

Additional information on the District's capital assets can be found in Note 3 on page 18 of this report.

Long-Term Debt

At June 30, 2023, the District had total long-term debt outstanding of \$37,729,698 (including current portion of \$1,268,422) as compared to \$39,029,969 (including current portion of \$1,300,301) at the prior year-end. The decrease is primarily the result of payments of \$1,300,271 on existing debt. Please see Note 4 on page 18 for additional information.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the District's finances for all those with an interest in the District's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Santa Cruz County Auditor-Controller, 701 Ocean Street, Room 100, Santa Cruz, CA 95060.

BASIC FINANCIAL STATEMENTS

**SANTA CRUZ COUNTY SANITATION DISTRICT
STATEMENT OF NET POSITION
JUNE 30, 2023**

	2023
ASSETS	
Current Assets:	
Cash and investments with County Treasurer, unrestricted	\$ 18,715,109
Total Current Assets	18,715,109
Noncurrent Assets:	
Cash and investments with Fiscal Agent, restricted	17,860,273
Capital assets, net	151,498,053
Total Noncurrent Assets	169,358,326
Total Assets	188,073,435
LIABILITIES	
Current Liabilities:	
Accounts payable and accrued liabilities	3,461,530
Accrued bond interest	136,344
Loans payable, current portion	1,268,422
Total Current Liabilities	4,866,296
Noncurrent Liabilities:	
Loans payable, net	36,461,276
Total Noncurrent Liabilities	36,461,276
Total Liabilities	41,327,572
NET POSITION	
Net investment in capital assets	131,627,947
Unrestricted	15,117,916
Total Net Position	\$ 146,745,863

The accompanying notes are an integral part of these basic financial statements.

**SANTA CRUZ COUNTY SANITATION DISTRICT
STATEMENT OF REVENUES, EXPENSES, AND
CHANGES IN NET POSITION
FOR THE FISCAL YEAR ENDED JUNE 30, 2023**

	2023
OPERATING REVENUES	
Charges for services	\$ 31,679,491
OPERATING EXPENSES	
General and administrative	6,894,506
Services and supplies	15,054,640
Depreciation	6,175,322
Total Operating Expenses	28,124,468
Operating Income	3,555,023
NONOPERATING REVENUES (EXPENSES)	
Aid from other government agencies	189,673
Investment income	1,101,758
Bond interest and related fees	(1,303,947)
Gain on sale of capital assets	9,409
Total Nonoperating Revenues (Expenses)	(3,107)
Change in Net Position	3,551,916
Net Position - Beginning	143,193,947
Net Position - Ending	\$ 146,745,863

The accompanying notes are an integral part of these basic financial statements.

**SANTA CRUZ COUNTY SANITATION DISTRICT
STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 2023**

	2023
Cash Flows from Operating Activities:	
Cash receipts from customers	\$ 31,679,491
Cash paid to suppliers for goods and services	(12,655,633)
Cash paid for interfund services used	(9,945,296)
	9,078,562
Cash Flows from Noncapital Financing Activities:	
Subsidy from other government agencies	189,673
	189,673
Cash Flows from Capital and Related Financing Activities:	
Acquisition and construction of capital assets	(11,370,693)
Proceeds from sale of assets	9,409
Issuance of debt	-
Principal paid on capital debt	(1,318,352)
Interest paid on capital debt	(1,296,744)
	(13,976,380)
Cash Flows from Investing Activities:	
Interest and investment income, net	1,101,758
	1,101,758
Net Decrease in Cash and Investments	(3,606,387)
Cash and Investments, Beginning	40,181,769
Cash and Investments, Ending	\$ 36,575,382
Reconciliation of Cash and Cash Investments to the Statement of Net Position	
Cash and investments with County Treasurer, unrestricted	\$ 18,715,109
Cash and investments with Fiscal Agent, restricted	17,860,273
	\$ 36,575,382

The accompanying notes are an integral part of these basic financial statements.

**SANTA CRUZ COUNTY SANITATION DISTRICT
STATEMENT OF CASH FLOWS (Continued)
FOR THE FISCAL YEAR ENDED JUNE 30, 2023**

	2023
Reconciliation of Operating Income to Net Cash	
Provided by Operating Activities:	
Operating income	\$ 3,555,023
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	6,175,322
Changes in assets and liabilities:	
Accounts payable	(651,783)
Net Cash Provided by Operating Activities	\$ 9,078,562

The accompanying notes are an integral part of these basic financial statements.

**SANTA CRUZ COUNTY SANITATION DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2023**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Santa Cruz County Sanitation District (the District) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the District's accounting policies are described below.

A. Description of the Reporting Entity

The District is managed by the Santa Cruz County Department of Public Works (Department) under the direction of the District Board of Directors. Among other assignments, the Department provides management, administration, engineering, maintenance, and construction services for the District. In addition, other Santa Cruz County (County) services provided to the District are:

1. Collection, by the Treasurer-Tax Collector, of sewer charges included on the customers' tax bills.
2. Collection of connection fees by the Planning Department.
3. Providing of investment services by the Treasurer.
4. Providing of legal services by the County Counsel.

The Department recovers its administrative costs from a 3.0% to 10.0% overhead surcharge on all services performed. Other charges related to construction and acquisitions of sewage processing facilities have been capitalized in the accompanying financial statements once the improvements or acquisitions have been completed.

The District's financial statements are presented as an enterprise fund and as a discretely presented component unit in the County's financial statements, pursuant to GASB Statement No. 61.

The District does not have employees. All employees are employees of the Department. The County charges the District a weighted labor rate for work performed on behalf of the District.

B. Measurement Focus, Basis of Accounting, and Basis of Presentation

The basic financial statements include the Statement of Net Position; the Statement of Revenues, Expenses, and Changes in Net Position; and the Statement of Cash Flows.

The basic financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Accordingly, all assets, deferred outflows of resources, liabilities, and deferred inflows of resources (whether current or noncurrent) are included on the Statement of Net Position. The Statement of Revenues, Expenses, and Changes in Net Position presents increases (revenues) and decreases (expenses) in total net position. Under the 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.

The District distinguishes operating revenues and expenses from nonoperating items. Operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the District. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as property taxes and investment income, result from nonexchange transactions or ancillary activities in which the District gives (receives) value without directly receiving (giving) equal value in exchange.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Measurement Focus, Basis of Accounting, and Basis of Presentation (Continued)

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

The District has elected to apply all GASB pronouncements as well as any applicable pronouncements of the Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board (APB) Opinions, and Accounting Research Bulletins (ARB) of the Committee on Accounting Procedure unless they contradict or conflict with GASB Statement No. 61.

The District's accounting records are a part of the County's centralized accounting system.

C. Cash and Investments

The District maintains all of its cash and investments with the County Treasurer in an investment pool. On a monthly basis the County Treasurer allocates interest to participants based upon their average daily balances. Investments in the investment pool are highly liquid, as deposits and withdrawals can be made at anytime without penalty. The County does not impose any maximum investment limit. The fair value of the District's investment in this pool is reported in the accompanying financial statements at amounts based upon the District's pro-rata share of the fair value provided by the County for the entire investment pool. The balance available for withdrawal is based on the accounting records maintained by the County, which are recorded on an amortized cost basis of accounting.

D. Restricted Cash with Fiscal Agents

Restricted cash with fiscal agents is comprised of funds reserved for capital projects and debt service.

E. Inventories

Inventories consist of materials and supplies which are valued using the FIFO method (first-in, first-out).

F. Capital Assets

Capital assets, which include land, construction in progress, buildings and improvements, improvements other than buildings, machinery and equipment, autos and trucks, equipment under capitalized leases, and infrastructure assets (e.g., roads, bridges, traffic signals, and similar items), are reported in the Government-Wide Financial Statements. County policy has set the capitalization threshold for reporting capital assets at \$5,000 for equipment and vehicles and \$25,000 for infrastructure, buildings, and structures. Capital assets are valued at historical cost or estimated historical cost if actual historical cost was not available. Donated assets are valued at their estimated market value on the date donated.

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

Infrastructure	4-65 years
Buildings and structures	10-50 years
Equipment and vehicles	3-15 years

For infrastructure systems, the County elected to use the "Basic Approach" as defined by GASB Statement No. 34 for infrastructure reporting.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

F. Capital Assets (Continued)

The County defines infrastructure as the basic physical assets that allow the County to function. The assets include streets, bridges, sidewalks, drainage systems, etc. Each major infrastructure system can be divided into subsystems. For example, the street system can be subdivided into pavement, curb and gutters, sidewalks, medians, streetlights, landscaping, and land. These subsystems were not delineated in the basic financial statements. The appropriate operating department maintains information regarding the subsystems.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest on construction-related debt incurred during the period of construction is capitalized as a cost of the constructed assets.

Maintenance and repairs are charged to operations when incurred. Betterments and major improvements which significantly increase values, change capacities, or extend useful lives are capitalized. Upon sale or retirement of capital assets, the cost and related accumulated depreciation are removed from the respective accounts and any resulting gain or loss is included in the results of the operations.

G. Net Position

In the Statement of Net Position, net position is classified in the following categories:

Net Investment in Capital Assets – This amount consists of capital assets net of accumulated depreciation and reduced by outstanding debt that is attributed to the acquisition, construction, or improvement of the assets.

Restricted Net Position – This amount is restricted by external creditors, grantors, contributions, or laws or regulations of other governments.

Unrestricted Net Position – This amount consists of all net position that does not meet the definition of “net investment in capital assets” or “restricted net position.”

H. Use of Estimates

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

I. Effect of New Governmental Accounting Standards Board Pronouncements

GASB Statement No. 91 – *Conduit Debt Obligations*. The requirements of this statement are effective for reporting periods beginning after December 15, 2021. There was no impact on the basic financial statements due to the implementation of this statement.

GASB Statement No. 94 – *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*. The requirements of this statement are effective for reporting periods beginning after June 15, 2022. There was no impact on the basic financial statements due to the implementation of this statement.

GASB Statement No. 96 – *Subscription-Based Information Technology Arrangements*. The requirements of this statement are effective for reporting periods beginning after June 15, 2022. There was no impact on the basic financial statements due to the implementation of this statement.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

I. Effect of New Governmental Accounting Standards Board Pronouncements (Continued)

GASB Statement No. 99 – *Omnibus 2022*. The requirements of this statement are effective as follows:

- The requirements related to extension of the use of the London Interbank Offered Rate (LIBOR), accounting for Supplemental Nutrition Assistance Program (SNAP) distributions, disclosures of nonmonetary transactions, pledges of future revenues by pledging governments, clarification of certain provisions in GASB Statement No. 34, as amended, and terminology updates related to GASB Statement No. 53 and GASB Statement No. 63 are effective upon issuance.
- The requirements related to leases, public-private and public-public partnerships (PPPs), and subscription-based information technology arrangements (SBITAs) are effective for fiscal years beginning after June 15, 2022, and all reporting periods thereafter.
- The requirements related to financial guarantees and the classification and reporting of derivative instruments within the scope of GASB Statement No. 53 are effective for fiscal years beginning after June 15, 2023, and all reporting periods thereafter.

There was no impact on the basic financial statements due to the implementation of this statement.

J. Future Governmental Accounting Standards Board Pronouncements

Recently released standards by GASB affecting future fiscal years are as follows:

GASB Statement No. 100 – *Accounting Changes and Error Corrections—an Amendment of GASB Statement No. 62*. For fiscal years beginning after June 15, 2023, and all reporting periods thereafter. The District has not fully judged the effect of the implementation of GASB Statement No. 100 as of the date of the financial statements.

GASB Statement No. 101 – *Compensated Absences*. The requirements of this statement are effective for fiscal years beginning after December 15, 2023, and all reporting periods thereafter. The District has not fully judged the effect of the implementation of GASB Statement No. 101 as of the date of the financial statements.

NOTE 2 – CASH AND INVESTMENTS

A. Cash and Investments

Cash and investments are presented on the Statement of Net Position as follows at June 30, 2023:

Cash and investments with County Treasurer, unrestricted	\$ 18,715,109
Cash and investments with Fiscal Agent, restricted	<u>17,860,273</u>
Total	<u><u>\$ 36,575,382</u></u>

B. Cash Held with the Santa Cruz County Treasurer

The District pools cash from all sources and all funds except “Cash and investments with fiscal agents” with the County Treasurer so that it can be invested at the maximum yield, consistent with safety and liquidity, while individual funds can make expenditures at any time. The Santa Cruz County Treasury Oversight Committee oversees the Treasurer’s investments and policies.

The California Government Code requires California banks and savings and loan associations to secure the County’s cash deposits by pledging securities as collateral. This code states that collateral pledged in this manner shall have the effect of perfecting a security interest in such collateral superior to those of a general creditor. Thus, collateral for cash deposits is considered to be held in the County’s name.

NOTE 2 – CASH AND INVESTMENTS (Continued)

B. Cash Held with the Santa Cruz County Treasurer (Continued)

The market value of pledged securities must equal at least 110% of the County's cash deposits. California law also allows institutions to secure County deposits by pledging first trust deed mortgage notes having a value of 150% of the County's total cash deposits. The County may waive collateral requirements for cash deposits, which are fully insured up to \$250,000 by the Federal Deposit Insurance Corporation. The County, however, has not waived the collateralization requirements.

C. Investments

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

<u>Authorized Investment Types</u>	<u>Maximum Maturity</u>	<u>Maximum Percentage of Portfolio</u>	<u>Maximum Percentage Investment in One Issuer</u>
Local agency bonds	5 Years	0.1	None
U.S. Treasury obligations	5 Years	1	None
U.S. Government Agency obligations	5 Years	1	0.25
Bankers' acceptances	180 Days	0.4	0.1
Commercial paper	270 Days	0.25	0.1
Negotiable certificates of deposit	5 Years	0.3	0.1
Bank deposit	5 Years	0.1	0.1
Repurchase agreements	1 Year	1	0.1
Medium-term notes	5 Years	0.3	0.1
Mutual funds/money market mutual funds	N/A	0.2	0.1
Local Agency Investment Fund (LAIF)	N/A	\$75 million	None
Joint Powers Authority investment fund	None	0.25	0.1
Supranationals	5 Years	0.3	0.1

In accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, investments were stated at fair value. The fair value of investments correlates to changes in interest rates. When interest rates increase, an investment portfolio will see a decrease in fair value, as prior securities were purchased at lower yields. Inversely, when interest rates decrease, an investment portfolio will see an increase in fair value, as prior securities were purchased at higher yields. The prior reporting period saw a significant increase in interest rates, which resulted in a material unrealized decrease of \$32,494,816 in fair value of pool investments at June 30, 2022. During the current reporting period interest rates remained high. The unrealized decrease in the fair value of investment decreased from \$32,494,816 to \$25,566,028 at June 30, 2023, a change of \$6,938,788. The change has been recorded in the financial statements of all funds with equity in pooled cash and investments in the County Treasury. The County has the full intent and ability to hold investments to maturity and does not expect to realize the decrease in fair value.

Investments of debt proceeds held by the bond trustee are governed by provisions of the debt agreements, rather than the general provisions of the California Government Code or the County's investment policy.

D. Interest Rate Risk

The County manages its exposure to declines in fair values by limiting the weighted average maturity of its investment portfolio to five years or less in accordance with its Investment Policy.

NOTE 2 – CASH AND INVESTMENTS (Continued)

E. Concentration of Credit Risk

At June 30, 2023, in accordance with State law and the County's Investment Policy, the County did not have 5% or more of its net investment in commercial paper, corporate bonds, or medium-term notes of a single organization, nor did it have 10% or more of its net investment in any one money market mutual fund. Investments in obligations of the U.S. government, U.S. government agencies, or government-sponsored enterprises are exempt from these limitations.

F. Custodial Credit Risk

For investments and deposits held with fiscal agents, custodial credit risk is the risk that, in the event of the failure of the counterparty, the County will not be able to recover the value of its investments or deposits that are in the possession of an outside party. At fiscal year-end, the County's investment pool and cash with fiscal agents had no securities exposed to custodial credit risk.

G. Local Agency Investment Fund (LAIF)

The County is a participant in LAIF which is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. The County's investments with LAIF at June 30, 2023, included a portion of the pooled funds invested in Structured Notes and Asset-Backed Securities:

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

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

As of June 30, 2023, the County had \$10,348 invested in LAIF, which had invested none of the pool investment funds in Structured Notes and Asset-Backed Securities, just as in the previous fiscal year. LAIF provided a fair value factor of 0.984828499 to calculate the fair value of the investments in LAIF. However, an adjustment was not made to reflect the fair value of LAIF, as the fair value adjustment was considered immaterial.

H. Investment in County Investment Pool

The District is an involuntary participant in the County Investment Pool that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. The fair value of the District's investment in this pool is reported in the accompanying financial statements at amounts based upon the District's pro-rata share of the fair value provided by the County for the entire County portfolio. The balance available for withdrawal is based on the accounting records maintained by the County, which are recorded on a fair market value basis.

The County Treasurer's Investment Pool categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. These principles recognize a three-tiered fair value hierarchy, as follows:

Level 1 – Investments reflect prices quoted in active markets,

Level 2 – Investments reflect prices that are based on a similar observable asset either directly or indirectly, which may include inputs in markets that are not considered to be active, and

Level 3 – Investments reflect prices based upon unobservable sources.

NOTE 3 – CAPITAL ASSETS

Capital asset activity for the fiscal year ended June 30, 2023, is as follows:

	Balance July 1, 2022	Additions	Deletions	Transfers	Balance June 30, 2023
Nondepreciable assets:					
Construction in progress	\$ 6,595,166	\$ 7,366,600	\$ (9,954)	\$ (1,154,248)	\$ 12,797,564
Total nondepreciable assets	6,595,166	7,366,600	(9,954)	(1,154,248)	12,797,564
Depreciable assets:					
Pumping stations	62,217,438	168,696	-	301,622	62,687,756
Transmission systems	146,341,547	2,464,535	-	852,626	149,658,708
Sewage treatment capacity rights	35,924,625	-	-	-	35,924,625
Mobile equipment	4,846,534	224,808	-	-	5,071,342
Other equipment	2,661,562	1,156,008	-	-	3,817,570
Total depreciable assets	251,991,706	4,014,047	-	1,154,248	257,160,001
Accumulated depreciation:					
Pumping stations	(29,303,975)	(1,101,265)	-	(268,322)	(30,673,562)
Transmission systems	(56,235,972)	(3,515,005)	-	(1,011,015)	(60,761,992)
Sewage treatment capacity rights	(21,659,656)	(985,340)	-	1,279,337	(21,365,659)
Mobile equipment	(3,394,178)	(211,709)	-	-	(3,605,887)
Other equipment	(1,690,409)	(362,003)	-	-	(2,052,412)
Total accumulated depreciation	(112,284,190)	(6,175,322)	-	-	(118,459,512)
Depreciable assets, net	139,707,516	(2,161,275)	-	1,154,248	138,700,489
Total capital assets, net	\$ 146,302,682	\$ 5,205,325	\$ (9,954)	\$ -	\$ 151,498,053

The District owns 47% of capacity rights of the City of Santa Cruz (City) Treatment Plant. Operation and maintenance of these treatment and outfall facilities are the responsibility of the City, with the District paying its proportionate share based on actual levels of flow. The District's investment in the City Treatment Plant is included in the District's capital assets.

Depreciation expense for the District for the fiscal year ended June 30, 2023, was \$6,175,322.

NOTE 4 – LONG-TERM DEBT

The following is a summary of long-term liabilities transactions for the fiscal year ended June 30, 2023:

Description	Beginning Balance July 1, 2022	Additions/ Adjustments	Deletions	Ending Balance June 30, 2023	Amounts Due Within One Year	Amounts Due in More Than One Year
Loans Payable:						
State Water Resources Control Board 2009	\$ 6,916,867	\$ -	\$ (617,391)	\$ 6,299,476	\$ 632,826	\$ 5,666,650
State Water Resources Control Board 2020	4,918,745	-	(130,665)	4,788,080	133,017	4,655,063
IBank	6,706,936	-	(154,134)	6,552,802	159,498	6,393,304
Bonds Payable:						
2022 Green Bond	19,945,000	-	(380,000)	19,565,000	325,000	19,240,000
2022 Green Bond Premium	542,421	-	(18,081)	524,340	18,081	506,259
Total Loans and Bonds Payable, Net	\$ 39,029,969	\$ -	\$ (1,300,271)	\$ 37,729,698	\$ 1,268,422	\$ 36,461,276

A. State Water Resources Control Board Loan 2009

During 2009, the District entered into a Project Finance Agreement (Agreement) with the State Water Resources Control Board (SWRCB) to finance the Aptos Transmission Main Relocation Project. Under this Agreement, the SWRCB has agreed to loan the District a total of \$16,725,699. As of June 30, 2023, the District had a balance of \$6,299,476 in loan disbursements pursuant to this Agreement. Pursuant to the Agreement, the interest rate is 2.5% and the District began making payments to repay the loan in the 2013/2014 fiscal year.

NOTE 4 – LONG-TERM DEBT (Continued)

B. State Water Resources Control Board Loan 2020

During 2020, the District entered into a Construction Installment Sale Agreement (Agreement) with the SWRCB to finance the Soquel Pump Station Force Main Replacement Project. Under this Agreement, the SWRCB has agreed to loan the District a total of \$5,000,000. As of June 30, 2023, the District had a balance of \$4,788,080 in loan disbursements pursuant to this Agreement. Pursuant to the Agreement, the interest rate is 1.8% and the District began making payments to repay the loan in the 2022/2023 fiscal year.

C. California Infrastructure and Economic Development Bank (IBank) Loan

In April 2019, the District entered into an Installment Sale Agreement (IBank Loan Agreement) with IBank to reduce the frequency of Sanitary Sewer Overflows (SSO) and, wherever possible, prevent SSO while meeting all applicable regulatory requirements by replacing old and deteriorated sewer lines prior to their failure. Under this IBank Loan Agreement, IBank has agreed to loan the District a total of \$7,000,000. Pursuant to the IBank Loan Agreement, the interest rate is 3.46% with the first principal payment due on August 1, 2020, with a loan maturity date of August 1, 2048. As of June 30, 2023, the District had a balance of \$6,552,082 in loan distributions pursuant to this IBank Loan Agreement.

D. Santa Cruz County Capital Financing Authority Revenue Bonds, Series 2022 (Green Bonds)

On June 1, 2022, the Santa Cruz County Capital Financing Authority issued Green Revenue Bonds for \$19,945,000. The bonds were issued in varying types. There are 14 serial bonds and 6 term bonds issued at a premium (the bonds). Serial bonds mature annually on June 1 between 2023 and 2036. The interest rate on the serial bonds is 5%. There are six term bonds. The first term bond, for \$1,265,000, was issued at an interest rate of 5% and matures on June 1, 2038. The second term bond for \$1,385,000, was issued at an interest rate of 4% and matures on June 1, 2040. The third term bond for \$1,500,000, was issued at an interest rate of 4% and matures on June 1, 2042. The fourth term bond for \$2,485,000, was issued at an interest rate of 4.125% and matures on June 1, 2045. The fifth term bond for \$2,810,000, was issued at an interest rate of 4.125% and matures on June 1, 2048. The sixth term bond for \$4,320,000 was issued at an interest rate of 4.25% and matures on June 1, 2052. The bonds were issued to finance wastewater improvements, specifically 5 separate components that make up the wastewater improvement project. As of June 30, 2023, the District had an outstanding balance of \$19,565,000.

The annual requirements to amortize to maturity all long-term debt outstanding including interest payable are as follows:

Fiscal Year Ended June 30,	Revenue Bonds		Loans Payable		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
2024	\$ 325,000	\$ 870,669	\$ 925,341	\$ 467,640	\$ 1,250,341	\$ 1,338,309
2025	345,000	854,419	949,075	443,810	1,294,075	1,298,229
2026	360,000	837,169	973,439	419,349	1,333,439	1,256,518
2027	380,000	819,169	998,449	394,237	1,378,449	1,213,406
2028	400,000	800,169	1,820,560	1,103,141	2,220,560	1,903,310
2029-2033	2,305,000	3,681,594	4,887,643	1,280,668	7,192,643	4,962,262
2034-2038	2,950,000	3,043,844	2,200,024	803,314	5,150,024	3,847,158
2039-2043	3,680,000	2,304,294	2,531,996	466,929	6,211,996	2,771,223
2044-2048	4,500,000	1,489,931	1,719,205	136,560	6,219,205	1,626,491
2049-2052	4,320,000	468,563	634,626	22,982	4,954,626	491,545
Sub-Total	<u>19,565,000</u>	<u>\$ 15,169,821</u>	<u>\$ 17,640,358</u>	<u>\$ 5,538,630</u>	<u>37,205,358</u>	<u>\$ 20,708,451</u>
Unamortized Premium	<u>524,340</u>			Unamortized Premium	<u>524,340</u>	
Total Revenue Bonds	<u>\$ 20,089,340</u>			Total	<u>\$ 37,729,698</u>	

NOTE 5 – RISK MANAGEMENT

The District is exposed to various risks of loss related to torts, theft or damage to and destruction of assets, errors and omissions, injuries to employees, and natural disasters.

The District is included within the terms of the County's insurance coverage. The County is self-insured for its general and auto liability, workers' compensation, and property coverage. The County has chosen to establish risk-financing internal service funds, where assets are set aside for claim settlements associated with the above risk of loss up to certain limits. Excess coverage is provided by the Public Risk Innovation, Solutions, and Management (PRISM) Program (formerly known as the California State Association of Counties Excess Insurance Authority), a joint powers authority whose purpose is to develop and fund programs of excess insurance for its member counties and public entities.

As of June 30, 2023, the workers' compensation self-insured retention is \$500,000.

The unpaid claims liability included in each of the County's Self-Insurance Internal Service Funds are based on the results of actuarial studies and include amounts for claims incurred but not reported. Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends, including frequency and amount of payouts, and other economic and social factors. It is the County's practice to obtain full actuarial studies bi-annually. Annual premiums are charged by each self-insurance fund using various allocation methods which include actual costs, claims experience, claims exposures, and number of participants.

Management is not aware of any claims pending against the District. There have been no reductions in the District's insurance coverage from the prior year and no settlement amounts have exceeded commercial insurance coverage.

NOTE 6 – COMMITMENTS AND CONTINGENCIES

There are various claims and legal actions pending against the District for which no provision has been made in the accompanying basic financial statements. In the opinion of the District's management, liabilities arising from these claims and legal actions, if any, will not have an adverse material effect on the financial position of the District.

The District has received Federal grants for specific purposes that are subject to review and audit by the Federal government. Although such audits could result in expenditure disallowance under grant terms, the required reimbursements, if any, are not expected to be material.

As of June 30, 2023, in the opinion of District Management, there were no outstanding matters that would have a significant effect on the financial position of the District.

NOTE 7 – SUBSEQUENT EVENTS

Subsequent events have been evaluated through December 20, 2023, which is the day the financial statements were available to be issued. Management did not identify any subsequent financial events.

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

To the Board of Directors of the
Santa Cruz County Sanitation District
Santa Cruz, 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 basic financial statements of the Santa Cruz County Sanitation District (the District), a component unit of the County of Santa Cruz (the County), as of and for the fiscal year ended June 30, 2023, 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 20, 2023.

Report on Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the County's internal control over financial reporting (internal control) relating to the District as a basis for designing 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 the County's internal control relating to the District. Accordingly, we do not express an opinion on the effectiveness of the County's internal control relating to the District.

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 or significant deficiencies may exist that were not identified.

Report on 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 the County's compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. 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 County's internal control or on compliance relating to the District. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the County's internal control and compliance relating to the District. Accordingly, this communication is not suitable for any other purpose.

BROWN ARMSTRONG
ACCOUNTANCY CORPORATION

A handwritten signature in blue ink that reads "Brown Armstrong Accountancy Corporation". The signature is written in a cursive, flowing style.

Bakersfield, California
December 20, 2023

**SANTA CRUZ COUNTY SANITATION DISTRICT
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
JUNE 30, 2023**

CURRENT YEAR SCHEDULE OF FINDINGS AND QUESTIONED COSTS

None noted.

STATUS OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS

None noted.