

*Semitropic Water Storage District*

*Combined Financial Statements*

*December 31, 2017 and 2016*

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### **Independent Auditors' Report**

Board of Directors  
Semitropic Water Storage District  
Wasco, California

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

We have audited the accompanying combined financial statements of Semitropic Water Storage District as of and for the years ended December 31, 2017 and 2016, and the related notes to the combined financial statements, which collectively comprise the District's basic combined financial statements as listed in the table of contents.

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

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

#### **Auditors' Responsibility**

Our responsibility is to express opinions on these combined financial statements based on our audits. We conducted our audits 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 audits to obtain reasonable assurance about whether the combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the combined 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 combined 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 combined financial statements.

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

#### **Opinions**

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of Semitropic Water Storage District as of December 31, 2017 and 2016, and the changes in financial position and cash flows for the years 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 information on pages 3 through 11 be presented to supplement the combined financial statements. Such information, although not a part of the combined financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the combined 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 combined financial statements, and other knowledge we obtained during our audits of the combined financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

### *Other Information*

Our audits were conducted for the purpose of forming opinions on the combined financial statements that collectively comprise the District's combined financial statements. The combined schedules of operating expenses are presented for purposes of additional analysis and are not a required part of the basic combined financial statements. The schedules are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the combined financial statements. Such information has been subjected to the auditing procedures applied in the audits of the combined financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the combined financial statements or to the combined financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combined schedules of operating expenses are fairly stated in all material respects in relation to the basic combined financial statements as a whole.

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

In accordance with *Government Auditing Standards*, we have also issued our report dated June 19, 2018, on our consideration of Semitropic Water Storage District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is 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 Semitropic Water Storage District's internal control over financial reporting and compliance.

**BARBICH HOOPER KING  
DILL HOFFMAN  
Accountancy Corporation**



Bakersfield, California  
June 19, 2018

## *Semitropic Water Storage District*

### *Management's Discussion and Analysis*

The following discussion and analysis of Semitropic Water Storage District financial performance provides an overview of the financial activities for the fiscal years ended December 31, 2017 and 2016. This information is presented in conjunction with the basic audited financial statements and accompanying notes, which follow this section.

#### ***Financial Highlights***

The District's total net position increased \$16.2 million or 9% over the course of the year's operations.

The District's total revenues experienced a net increase of \$2.1 million or 3% during the year ended December 31, 2017. The primary reason for the net increase in total revenues was a net between the increase in water revenues, the decrease in groundwater banking revenue and decrease in prior year income. 2017 was considered a water delivery year, which means that there was more water available for purchase by the District's landowners and also more water available for groundwater banking partners to bank within the District.

The District's total expenses decreased \$0.9 million, or 1%.

The District's gross capital assets increased \$28.2 million, or 7%, during the year ended December 31, 2017 due to the purchase of land for development of a new water supply project.

#### ***Overview of the Combined Financial Statements***

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

#### ***Required Financial Statements***

The combined financial statements of the District report information of the District using accounting methods similar to those used by private sector companies. The combined financial statements conform to accounting principles which are generally accepted in the United States of America and utilize the accrual basis of accounting.

The combined statements of net position includes all of the District's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to District creditors (liabilities), with the difference between the two reported as net position. This statement will indicate which assets are restricted due to contractual, Board action, or other commitments. This statement also provides the basis for assessing the liquidity, capital structure and financial flexibility of the District.

Revenues and expenses for each of the last two fiscal years are accounted for in the combined statements of revenues and expenses and changes in net position. These statements measure the success of the District's operations and can be used to determine profitability, credit worthiness and whether the District has successfully recovered all its costs through user fees and other charges.

*Semitropic Water Storage District*

*Management's Discussion and Analysis*

The combined statement of cash flows reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. From this statement, information related to sources and uses of cash, and the change in cash balances can be compared for each of the last two fiscal years.

*Financial Analysis of the District*

The required combined financial statements, discussed above, assist the reader in making an assessment of whether its financial health is improving or deteriorating. However, one will need to consider other non-financial factors such as changes in economic conditions, hydrology, population growth, and new or changed government legislation.

*Semitropic Water Storage District*

*Management's Discussion and Analysis*

To begin our analysis, a summary of the District's combined statements of net position is presented in Table A.

**Table A**  
**Condensed Combined Statements of Net Position**  
**December 31, 2017 and 2016**  
**(in millions)**

	<u>2017</u>	<u>2016</u>	<u>Dollar Change</u>	<u>Percentage Change</u>
Current assets	\$ 46.8	\$ 40.0	\$ 6.8	17%
Capital assets	297.3	275.8	21.5	8%
Noncurrent other assets	58.5	79.4	(20.9)	-26%
Total assets	<u>402.6</u>	<u>395.2</u>	<u>7.4</u>	2%
Deferred outflows of resources	<u>23.7</u>	<u>24.5</u>	<u>(0.8)</u>	-3%
	<u>\$ 426.3</u>	<u>\$ 419.7</u>	<u>\$ 6.6</u>	2%
Current liabilities	\$ 13.0	\$ 34.0	\$ (21.0)	-62%
Long-term liabilities	214.4	203.0	11.4	6%
Total liabilities	<u>227.4</u>	<u>237.0</u>	<u>(9.6)</u>	-4%
Invested in capital assets, net of related debt	112.9	83.0	29.9	36%
Restricted	9.0	33.3	(24.3)	-73%
Unrestricted	77.0	66.4	10.6	16%
Total net position	<u>198.9</u>	<u>182.7</u>	<u>16.2</u>	9%
	<u>\$ 426.3</u>	<u>\$ 419.7</u>	<u>\$ 6.6</u>	2%

As the statement of net position table above indicates, total assets increased by \$7.4 million to \$402.6 million at December 31, 2017, from \$395.2 million at December 31, 2016. The increase in the total assets of the District was primarily due to an increase in capital assets of \$21.5 million offset by a decrease in cash and investments of \$18.4 million.

Total liabilities decreased by \$9.6 million to \$227.4 million at December 31, 2017, from \$237 million at December 31, 2016. The decrease is mostly due to the net of the current year principal debt payments, and increase in trade accounts payable.

*Semitropic Water Storage District*

*Management's Discussion and Analysis*

**Table B**  
**Condensed Combined Statements of Revenues and Expenses and Changes in Net Position**  
**For the Years Ended December 31, 2017 and 2016**  
*(in millions)*

	<u>2017</u>	<u>2016</u>	<u>Dollar Change</u>	<u>Percentage Change</u>
Operating revenues:				
Contract water	\$ 13.2	\$ 11.0	\$ 2.2	20%
Noncontract water	13.9	5.2	8.7	167%
Groundwater banking	13.2	16.0	(2.8)	-18%
Electrical transfer & hookup	1.1	2.5	(1.4)	-56%
Other charges	1.3	2.7	(1.4)	-52%
	<u>42.7</u>	<u>37.4</u>	<u>5.3</u>	14%
Nonoperating income:				
Interest income	1.3	1.3	-	0%
GA & GP service charges	19.2	18.8	0.4	2%
Prior year income, net	1.7	5.1	(3.4)	-67%
Change in FMV of interest rate swap	1.5	1.7	(0.2)	-12%
	<u>23.7</u>	<u>26.9</u>	<u>(3.2)</u>	-12%
Total revenues	<u>66.4</u>	<u>64.3</u>	<u>2.1</u>	3%
Operating expenses:				
Transmission & distribution	15.8	14.9	0.9	6%
Source of supply	12.8	12.4	0.4	3%
General and administrative	3.1	4.0	(0.9)	-23%
Depreciation and amortization	6.9	6.5	0.4	6%
	<u>38.6</u>	<u>37.8</u>	<u>0.8</u>	2%
Nonoperating expenses:				
Interest expense	10.4	10.5	(0.1)	-1%
Other expenses	1.2	2.8	(1.6)	-57%
	<u>11.6</u>	<u>13.3</u>	<u>(1.7)</u>	-13%
Total expenses	<u>50.2</u>	<u>51.1</u>	<u>(0.9)</u>	-2%
Change in net position	16.2	13.2	3.0	23%
Net position, beginning of year	<u>182.7</u>	<u>169.5</u>	<u>13.2</u>	8%
Net position, end of year	<u>\$ 198.9</u>	<u>\$ 182.7</u>	<u>\$ 16.2</u>	9%



## *Semitropic Water Storage District*

### *Management's Discussion and Analysis*

While the Statement of Net Position shows the change in financial position of the District, the Statements of Revenues and Expenses and Changes in Net Position provides answers as to the nature and source of these changes.

The District's total revenues increased by \$2.1 million to \$66.4 million during the year ended December 31, 2017, from \$64.3 million during the year ended December 31, 2016. The year 2017 was a water delivery, or wet year. A wet year means there is water available other than the District's allocation from the State Water Project (SWP). It also means that our groundwater banking partners may also have additional water that may need to be stored, or banked within the District. In 2017, the allocation from the State Water Project (SWP) increased to 85%, from 60% in 2016. Due to the 85% water allocation, the District's banking partners requested a net recharge to their stored water accounts of 229,054 acre-feet, compared to the net recharge of 12,806 acre-feet in 2016. Water banking revenues includes the recovery/recharge fee charged per acre-foot of water recovered/recharged, the energy cost for returning the water requested and water treatment costs, if necessary. The net increase in total revenues in 2017 was \$2.1 million, which was due to an increase in contract/noncontract water sales of \$10.9 million and the decrease in prior year income of \$3.4 million mostly from the reconciliation of energy/treatment costs for recovery of water for banking partners and net decrease in groundwater banking revenues of \$2.8 million.

Total expenses decreased \$0.9 million to \$50.2 million during the year ended December 31, 2017 from \$51.1 million during the year ended December 31, 2016. This decrease was primarily due to the decrease in other expenses of \$1.7 million from 2016 as a result of a one-time charge of \$2.2 million. The offset against the decrease in other expenses was the increase in transmission and distribution expenses (increase of \$.9 million from 2016) due to the increase in costs incurred to bank the District's water with the Kern Water Bank Authority, Pioneer Project, North Kern Water Storage District, and Cawelo Water District.

*Semitropic Water Storage District*

*Management's Discussion and Analysis*

As of December 31, 2017, the District had invested \$408.7 million in capital assets as shown in Table C.

**Table C**  
**Capital Assets**  
**December 31, 2017 and 2016**  
**(in millions)**

	<u>2017</u>	<u>2016</u>	<u>Dollar Change</u>	<u>Percentage Change</u>
Land	\$ 94.1	\$ 74.1	\$ 20.0	27%
Transmission and distribution	261.4	260.3	1.1	0%
Communication equipment	0.01	0.01	-	0%
Autos and trucks	1.7	1.4	0.3	21%
Office equipment	0.6	0.6	-	0%
Field and miscellaneous equipment	1.1	1.1	-	0%
Well drilling equipment	3.0	3.0	-	0%
Wells	13.8	9.1	4.7	52%
General plant and equipment	3.1	3.1	-	0%
Capacity rights	4.5	4.5	-	0%
Construction in progress	<u>25.4</u>	<u>23.3</u>	<u>2.1</u>	9%
 Total capital assets	 408.7	 380.5	 28.2	 7%
 Less accumulated depreciation	 <u>111.4</u>	 <u>104.7</u>	 <u>6.7</u>	 6%
 Total net capital assets	 <u>\$ 297.3</u>	 <u>\$ 275.8</u>	 <u>\$ 21.5</u>	 8%

As can be seen from the table above, total capital assets increased \$28.2 million to \$408.7 million at December 31, 2017, from \$380.5 million at December 31, 2016. The increase is mainly due to the purchase of land easement for development of a new water supply project (\$20 million).

*Semitropic Water Storage District*

*Management's Discussion and Analysis*

**Table D**  
**Debt**  
**December 31, 2017 and 2016**  
**(in millions)**

	<u>2017</u>	<u>2016</u>	<u>Dollar Change</u>	<u>Percentage Change</u>
Revenue bonds	\$ 185.2	\$ 171.9	\$ 13.3	8%
Warrants	-	23.0	(23.0)	-100%
Swap	14.1	15.6	(1.5)	-10%
State loans	<u>7.0</u>	<u>7.8</u>	<u>(0.8)</u>	-10%
Total debt	<u>\$ 206.3</u>	<u>\$ 218.3</u>	<u>\$ (12.0)</u>	-5%

Revenue bonds are legally secured by a portion of the District's water banking revenues and/or the District's general administrative and general project service charges. If the revenue streams pledged to specific revenue bonds are not sufficient to repay the debt, for only the 2007 and 2009 bonds, the District is not legally obligated to appropriate other funds for debt service payments.

Other debt represents District obligations paid out of its general operating revenues. The District has no general obligation bonds at this time.

Total debt decreased \$12 million to \$206.3 million during the year ended December 31, 2017 from \$218.3 million during the year ended December 31, 2016. The decrease is due to the current year debt principal payments made, as well as the refunding of the 2016 warrants and 2009 Bonds.

The District received an affirmed AA-/Stable rating by Fitch Ratings for both the 2012A and 2012B water banking revenue refunding bonds issued to replace variable debt.

The District received an A+/Stable rating by Standard & Poor's for both the 2012A and 2012B water banking revenue refunding bonds issued to replace variable debt.

The District received an A+/Stable rating by Standard & Poor's for the 2014A revenue bonds issued for land acquisitions and capital projects.

The District received an A+/Stable rating by Standard & Poor's for the 2015A revenue bonds issued for capital projects and a partial refunding of prior bonds.

The District received an A+/Stable rating by Standard & Poor's for the 2017A revenue bonds issued for refunding of prior bonds and warrants.

*Semitropic Water Storage District*

*Management's Discussion and Analysis*

***Budgetary Comparison***

The following table is a comparison of the Board approved budget for 2017 against actual.

***Table E***  
***Budget vs. Actual Comparison***  
***For the Year Ended December 31, 2017***  
***(in millions)***

	<u><i>Actual</i></u>	<u><i>Budget</i></u>	<u><i>Change</i></u>	<u><i>Percentage Change</i></u>
Operating revenues:				
Contract water	\$ 13.2	\$ 13.4	\$ (0.2)	-1%
Noncontract water	13.9	14.7	(0.8)	-5%
Groundwater banking	13.2	12.9	0.3	2%
Electrical transfer & hookup	1.1	0.8	0.3	38%
Other charges	1.3	3.7	(2.4)	-65%
	<u>42.7</u>	<u>45.5</u>	<u>(2.8)</u>	<u>-6%</u>
Nonoperating income:				
Interest income	1.3	0.3	1.0	333%
GA & GP service charges	19.2	18.4	0.8	4%
Prior year income, net	1.7	0.5	1.2	240%
Change in FMV of interest rate swap	1.5	-	1.5	100%
	<u>23.7</u>	<u>19.2</u>	<u>4.5</u>	<u>23%</u>
Total revenues	<u>66.4</u>	<u>64.7</u>	<u>1.7</u>	<u>3%</u>
Operating expenses:				
Transmission & distribution	15.8	10.4	5.4	52%
Source of supply	12.8	21.4	(8.6)	-40%
General and administrative	3.1	10.6	(7.5)	-71%
Depreciation and amortization	6.9	6.5	0.4	6%
	<u>38.6</u>	<u>48.9</u>	<u>(10.3)</u>	<u>-21%</u>
Nonoperating expenses:				
Interest expense	10.4	10.6	(0.2)	-2%
Other expenses	1.2	-	1.2	100%
	<u>11.6</u>	<u>10.6</u>	<u>1.0</u>	<u>9%</u>
Total expenses	<u>50.2</u>	<u>59.5</u>	<u>(9.3)</u>	<u>-16%</u>
Change in net position	<u>\$ 16.2</u>	<u>\$ 5.2</u>	<u>\$ 11.0</u>	<u>212%</u>

*Semitropic Water Storage District*

*Management's Discussion and Analysis*

Total revenue was above budgeted revenues for 2017 mainly due to the increased amount of net prior year income, mostly from the reconciliation of energy/treatment costs for recovery of water for banking partners.

Total expenses came out under budgeted expenses by \$10.3 million. This was mainly due to the lower amount of source of supply expense and the increased amount in transmission and distribution expense. Source of supply was lower due to the District's banking of available excess water, thereby lowering the amount of expense for the year. Transmission and distribution expenses increased due to the amount of fees associated with banking excess water.

The annual budget is presented and approved by the District's Board of Directors each October. An updated budget is presented and approved in June, if necessary.

***Contacting the District Management***

This financial report is designed to provide our customers and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District at P.O. Box 8043, Wasco, CA 93280.

*Semitropic Water Storage District*

*Combined Statements of Net Position  
December 31, 2017 and 2016*

<b>ASSETS AND DEFERRED OUTFLOWS OF RESOURCES</b>	<b>2017</b>	<b>2016</b>
<b><i>Current Assets</i></b>		
Cash and cash equivalents	\$ 30,343,077	\$ 24,509,822
Receivables		
Accounts receivable, trade	5,145,521	4,850,197
General administrative and general project service charges receivable	9,552,459	9,088,048
Current portion of notes receivable	1,270,431	1,079,667
Other prepaid expenses and deposits	456,277	474,462
Total current assets	46,767,765	40,002,196
<b><i>Noncurrent Assets</i></b>		
Restricted assets		
Cash and cash equivalents	1,153,122	22,514,842
Investments	7,892,401	10,761,471
Total restricted assets	9,045,523	33,276,313
Capital assets, net of accumulated depreciation	297,252,130	275,806,911
Other noncurrent assets		
Notes receivable, less current portion	13,451,617	14,721,986
Banked water inventory	14,139,478	8,670,136
Investment in Southern California Water Bank Authority	18,124,430	19,396,431
Investment in Kern Water Bank Authority	3,740,727	3,263,935
Total other noncurrent assets	49,456,252	46,052,488
Total noncurrent assets	355,753,905	355,135,712
<b><i>Total Assets</i></b>	<b>402,521,670</b>	<b>395,137,908</b>
<b><i>Deferred Outflows of Resources</i></b>		
Deferred outflow of interest rate swap	-	3,472
Deferred outflow of advance refunding of bonds	23,712,438	24,526,959
Total deferred outflows of resources	23,712,438	24,530,431
	<b>\$ 426,234,108</b>	<b>\$ 419,668,339</b>

*See Notes to Combined Financial Statements.*

<b>LIABILITIES AND NET POSITION</b>	<b>2017</b>	<b>2016</b>
<b><i>Current Liabilities</i></b>		
Current maturities of long-term debt	\$ 7,711,827	\$ 29,909,330
Trade accounts payable	2,817,342	1,473,462
Customer deposits	548,640	595,411
Accrued liabilities	1,178,456	1,253,980
Deferred revenue	735,550	739,719
Total current liabilities	<u>12,991,815</u>	<u>33,971,902</u>
<b><i>Long-Term Liabilities</i></b>		
Long-term debt, less current maturities	200,324,171	187,405,187
Obligations under interest rate swap	14,064,861	15,557,034
	<u>214,389,032</u>	<u>202,962,221</u>
<b><i>Total Liabilities</i></b>	<u>227,380,847</u>	<u>236,934,123</u>
<b><i>Net Position</i></b>		
Invested in capital assets, net of related debt	112,928,570	83,019,353
Restricted for:		
Debt service	8,997,929	33,239,283
Cafeteria plan	47,594	37,030
Unrestricted	<u>76,879,168</u>	<u>66,438,550</u>
	<u>198,853,261</u>	<u>182,734,216</u>
	<u>\$ 426,234,108</u>	<u>\$ 419,668,339</u>

*Semitropic Water Storage District*

***Combined Statements of Revenues and Expenses  
For the Years Ended December 31, 2017 and 2016***

	<b>2017</b>	<b>2016</b>
<b><i>Operating revenues:</i></b>		
Contract water	\$ 13,202,827	\$ 11,011,522
Noncontract water	13,922,867	5,176,768
Groundwater banking	13,159,186	15,977,217
Electrical transfer and hookup charges	1,052,509	2,522,903
Other charges	1,339,898	2,719,699
	42,677,287	37,408,109
<b><i>Operating expenses:</i></b>		
Transmission and distribution	15,808,724	14,937,456
Source of supply	12,844,111	12,382,347
General and administrative	3,108,218	3,945,175
Depreciation and amortization expense	6,905,347	6,498,874
	38,666,400	37,763,852
Operating income (loss)	4,010,887	(355,743)
<b><i>Nonoperating income (expense):</i></b>		
Interest income	1,305,345	1,261,889
General administrative service charges	251,357	248,820
General project service charges	18,976,822	18,568,016
Interest expense	(10,416,752)	(10,526,642)
Equity in income (loss) from investments	(422,299)	328,685
Other expense, net	(584,512)	(2,725,975)
Prior year income, net	1,719,072	5,093,945
Loss on disposal of assets	(209,576)	(330,915)
Change in fair value of interest rate swap	1,488,701	1,693,049
	12,108,158	13,610,872
Change in net position	\$ 16,119,045	\$ 13,255,129

*See Notes to Combined Financial Statements.*



*Semitropic Water Storage District*

*Combined Statements of Changes in Net Position  
For the Years Ended December 31, 2017 and 2016*

<i>Balance, December 31, 2015</i>	\$ 169,479,087
Change in net position	<u>13,255,129</u>
<i>Balance, December 31, 2016</i>	182,734,216
Change in net position	<u>16,119,045</u>
<i>Balance, December 31, 2017</i>	<u><u>\$ 198,853,261</u></u>

*See Notes to Combined Financial Statements.*

*Semitropic Water Storage District*

*Combined Statements of Cash Flows  
For the Years Ended December 31, 2017 and 2016*

	<u>2017</u>	<u>2016</u>
<b><i>Cash flows from operating activities:</i></b>		
Receipts from customers	\$ 62,229,351	\$ 62,299,048
Payments to suppliers for goods and services	(32,268,840)	(35,089,935)
Payments to employees for services	(3,589,028)	(3,589,028)
Net cash provided by operating activities	<u>26,371,483</u>	<u>23,620,085</u>
<b><i>Cash flows from capital and related financing activities:</i></b>		
Payment for acquisition and construction of capital assets	(28,562,892)	(6,056,936)
Proceeds from sale of capital assets	2,750	-
Payments for interest on bonds and construction loans	(10,314,032)	(10,244,669)
Proceeds from issuance of long term debt	-	3,000,000
Payments on long-term debt	(8,652,704)	(7,039,815)
Net cash used in capital and related financing activities	<u>(47,526,878)</u>	<u>(20,341,420)</u>
<b><i>Cash flows from investing activities:</i></b>		
Net sales (purchases) of investments	2,869,070	(48,258)
Proceeds from receipts on note receivable	1,079,605	936,085
Distributions received from investment	372,910	208,087
Interest income	1,305,345	1,517,166
Net cash provided by investing activities	<u>5,626,930</u>	<u>2,613,080</u>
<b><i>Net increase (decrease) in cash and cash equivalents</i></b>	(15,528,465)	5,891,745
<b><i>Cash and cash equivalents at beginning of the year</i></b>	<u>47,024,664</u>	<u>41,132,919</u>
<b><i>Cash and cash equivalents at the end of the year</i></b>	<u>\$ 31,496,199</u>	<u>\$ 47,024,664</u>
<b><i>Reconciliation of cash and cash equivalents</i></b>		
Cash and cash equivalents	\$ 30,343,077	\$ 24,509,822
Restricted cash and cash equivalents	1,153,122	22,514,842
	<u>\$ 31,496,199</u>	<u>\$ 47,024,664</u>

*See Notes to Combined Financial Statements.*

	<u>2017</u>	<u>2016</u>
<b><i>Reconciliation of operating income (loss) to net cash provided by operating activities:</i></b>		
Operating income (loss)	\$ 4,010,887	\$ (355,743)
<b><i>Adjustments to reconcile operating income (loss) to net cash provided by operating activities:</i></b>		
Depreciation and amortization	6,905,346	6,498,875
General administrative and general project service charges	19,228,179	18,816,836
Prior year income, net	1,719,072	5,093,945
Other expense, net	(584,512)	(2,725,975)
<b><i>Changes in operating assets and liabilities:</i></b>		
Receivables and general administrative and general project service charges receivable	(759,735)	14,500,037
Other prepaid expenses and deposits	18,185	87,068
Banked water inventory	(5,469,342)	(1,386,148)
Accounts payable and accrued liabilities	1,307,572	(8,207,101)
Deferred revenue	(4,169)	(8,701,709)
	<u>\$ 26,371,483</u>	<u>\$ 23,620,085</u>
<b><i>Noncash investing and financing activities:</i></b>		
Change in fair value of interest rate swap obligation	<u>\$ 1,492,173</u>	<u>\$ 1,713,125</u>
Equity in income (loss) from investments	<u>\$ (422,299)</u>	<u>\$ 328,685</u>
Purchase of capital assets in exchange of warrants	<u>\$ -</u>	<u>\$ 20,000,000</u>
Amortization of deferred outflow of advanced refundings included in interest expense	<u>\$ 1,286,511</u>	<u>\$ 1,277,230</u>
Payoff of 2016 warrants through 2017 bond issuance	<u>\$ 23,000,000</u>	<u>\$ -</u>
Advanced refunding of 2009 bonds through 2017 bond issuance	<u>\$ 34,215,000</u>	<u>\$ -</u>

*Semitropic Water Storage District*

*Notes to Combined Financial Statements*

***Note 1. Nature of Activities and Summary of Significant Accounting Policies***

***Principles of combination:***

The combined financial statements include the accounts of Semitropic Water Storage District, Buttonwillow Improvement District of the Semitropic Water Storage District, Pond-Poso Improvement District of the Semitropic Water Storage District, Semitropic Wildlife Improvement District of the Semitropic Water Storage District and Semitropic Improvement District of the Semitropic Water Storage District. Inter-district accounts have been eliminated.

***Nature of District's activities:***

Semitropic Water Storage District (the District) was formed on August 27, 1958. It began as an irrigation district for the purpose of securing State Water Project supplies to reduce groundwater overdraft. The District, a special district of the State of California, is one of eight water storage districts in California and is the largest in Kern County. The District is governed by a Board of Directors consisting of seven members who are elected by rate payers to serve four-year terms. Semitropic Improvement District has been appointed as agent to administer contracts on behalf of Buttonwillow Improvement District, Pond-Poso Improvement District, Semitropic Wildlife Improvement District and Semitropic Water Storage District.

The District's service area is comprised of approximately 221,000 acres or 345 square miles in the northwestern portion of Kern County. Since its inception, Buttonwillow Improvement District, Pond-Poso Improvement District, Semitropic Improvement District and Semitropic Wildlife Improvement District were created to help administer and manage the course of action and policies of Semitropic Water Storage District.

Although Buttonwillow Improvement District, Pond-Poso Improvement District, Semitropic Improvement District and Semitropic Wildlife Improvement District are a part of the Semitropic Water Storage District, they are operated and reported on as Semitropic Improvement District. As such, Semitropic Water Storage District is generally not liable for any contracts entered into or commitments made by them.

***Significant accounting policies are as follows:***

***Basis of accounting and financial reporting:***

The accompanying combined financial statements have been prepared on the accrual basis of accounting, in conformity with the uniform system of accounts prescribed for water districts by the Controller of the State of California. Under the accrual basis, revenues are recognized when earned and expenses are recognized when incurred regardless of the timing of cash payments or receipts.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as nonoperating.

## *Notes to Combined Financial Statements*

When the District has both unrestricted and restricted resources available for District purposes, it is the District's practice to first expend restricted resources, subsequently utilizing unrestricted resources as needed.

The District utilizes a net position presentation in accordance with GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB No. 63, *Financial Reporting of Deferred Outflows or Resources, Deferred Inflows of Resources, and Net Position*. Net position is categorized as invested in capital assets, net of related debt, restricted components of net position and unrestricted components of net position. These categories are defined as follows.

*Invested in capital assets, net of related debt* - This component of net position consists of capital assets, including restricted capital assets, net of accumulated depreciation and the deferred outflow of advanced refunding of bonds, reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net position component as the unspent proceeds.

*Restricted components of net position* - This component of net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Generally, a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported.

*Unrestricted components of net position* - This component of net position is the net amount of assets, deferred outflows of resources, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

### ***Deferred outflows of resources:***

The District reports increases in net assets that relate to future periods as deferred outflows of resources in a separate section of the combined statements of net position. Deferred outflow of resources reported in this year's combined financial statements are due to the deferred amount arising from the refunding of bonds in previous years as well as the deferred amount arising from the change in fair value of an interest rate swap. The deferred refunding amounts are being amortized over the remaining life of the refunding bonds as part of interest expense.

### ***Fund accounting:***

The District utilizes accounting for enterprise entities that 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 revenue earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

## *Notes to Combined Financial Statements*

### ***Use of estimates:***

The preparation of combined financial statements in conformity with accounting principles generally accepted in the United States of America 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 combined financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### ***Revenue recognition:***

The District has three primary sources of revenue. From its inception, the District has recognized revenue from the sale of surface irrigation water to water users located within the District for the purpose of halting the groundwater overdraft. Effective February 10, 2016, after certifying the results of a Proposition 218 majority protest hearing, the District established a State Water Project (“SWP”) water charge and additional water use charge for Contract water users. The SWP water charge will be set each year based on a percentage of the fixed portion of costs to the District to import supplies through the District’s contract with the KCWA. The Additional Water Use charge will be charged based on the acre-feet delivered to each Contract water user. The amount of SWP and Additional Water Use charges for December 31, 2017 were \$8,022,715 and \$5,180,112, respectively. The District’s water rates are supported by an annual applied water cost analysis and are approved by the District’s board on an annual basis. Water rates are not subject to regulation by the California Public Utilities Commission or by any other local, state or federal agency. Revenue from these sales is recognized on the accrual basis as water is delivered.

Beginning in 1995, the District entered into several groundwater banking agreements with its Banking Partners, some of which are other water districts in California. Under these agreements, the Banking Partners use available space within the District’s groundwater basin to store water during wet years (years when there is abundant rainfall and surplus water available) and recover water during dry years (years with little rainfall and no surplus water). The District primarily stores Banking Partners’ water using in-lieu recharge, which stores water by utilizing surface water “in-lieu” of pumping groundwater, thereby storing an equal amount in the groundwater basin. The District is paid an annual fee for operating and maintaining the groundwater banking program and earns revenue on a per acre-foot basis at the time water is stored and when water is returned to the respective Banking Partner. The District also receives revenue toward energy and water treatment reimbursements when water is returned. Revenue for groundwater banking is recognized in the period when annual fees are billed and when water is stored or returned for each respective Banking Partner. At December 31, 2017 and 2016, the District held 885,462 and 656,408 acre-feet (AF), respectively, of water in storage for future delivery to banking partners.

Lastly, the District receives revenue from general administrative and general project service charges for landowners receiving benefit from District services. These charges are established by the Board of Directors for the period January through December of each year and are levied to landowners within the District on their county property tax statements based on uniform rates per acre. For the years ended December 31, 2017 and 2016, \$19,228,179 and \$18,816,836, respectively, was earned by the District for general administrative and general project service charges. If available from District funds, the Board may authorize an end of the year discretionary payment in proportion to the general project service charge to the same District landowners. For the years ended December 31, 2017 and 2016, there was no end of

## *Notes to Combined Financial Statements*

the year discretionary payment authorized by the District. The net of these items is reported as nonoperating revenue to the District for the same January through December period.

Other sources of revenue include interest income and miscellaneous revenue which is comprised of water wheeling income, materials sales and electrical services.

### ***Allowance for delinquency provision:***

In prior years, the allowance for delinquency provision for general administrative and general project service charges has been based on a percentage of assessments levied. The percentage is determined by collections from previous years. As of December 31, 2017 and 2016, the District's management decided an allowance for delinquency provision for general administrative and general project service charges was not necessary.

### ***Accounts receivable, trade:***

Trade accounts receivable are stated at the amount management expects to collect from balances outstanding at year end. Based on management's assessment of the credit history with customers having outstanding balances and current relationships with them, it has concluded that realization of losses on balances outstanding at year end will be immaterial; accordingly, no allowance for doubtful accounts is required.

### ***Concentration of credit risk:***

Credit is extended, in the form of accounts receivable, to landowners who are located in the District's service area and groundwater banking partners.

### ***Capital assets:***

The District's capital assets are recorded at cost. Assets are capitalized when the cost is greater than \$5,000 and the asset has a useful life greater than two years. Depreciation is computed using the straight-line method over the following estimated useful lives:

	<u><i>Years</i></u>
Transmission and distribution	15-60
Communication equipment	5-10
Autos and trucks	5-10
Office equipment	3-10
Field and miscellaneous equipment	5-10
Well drilling equipment	5-20
Wells	15-25
General plant and equipment	15-60
Capacity rights	25

Maintenance and repairs of capital assets are charged to operations and major improvements are capitalized. Upon retirement, sale or other disposition of capital assets, the cost and accumulated depreciation are eliminated from the accounts and the gain or loss is included in operations.

## *Notes to Combined Financial Statements*

### ***Cash and cash equivalents:***

The District considers cash equivalents to be all highly liquid debt instruments purchased with a maturity of three months or less. At December 31, 2017 and 2016, cash and cash equivalents include cash on hand and amounts deposited with banks, the County of Kern Treasurer and the State Treasurer's office.

The District invests any excess funds not needed for immediate needs into State of California managed Local Agency Investment Fund (LAIF), which is a permitted investment by both State law and the District's investment policy. Created by state statute, the LAIF is a component of a pooled money program that is administered by the State Treasurer's Office. The fund has regulatory oversight from the Local Investment Advisory Board, which is comprised of the State Treasurer as chair, the State Controller, and the Director of Finance. As the LAIF does not make share-value adjustments due to immaterial differences between fair value and cost, the District's cost basis in the fund is reflected in cash and cash equivalents on the combined statements of net position as of December 31, 2017 and 2016.

### ***Custodial credit risk:***

Custodial credit risk of deposits is the risk that in the event of a bank failure, the District's deposits may not be returned. The California Government Code and the District's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits and investments, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure District deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits. At December 31, 2017, the District had no risk associated with custodial assets.

### ***Deposits with financial institutions:***

Cash funds deposited with the State Treasurer's office are in a pooled money fund. Funds are pooled with other agencies throughout California. Investments are made in accordance with Government Code Sections 16430 and 16480. Cash funds are also deposited with the County of Kern and are appropriately collateralized by cash, investments and securities.

Pooled funds may be invested in: (1) direct obligations of the United States government, the payment of which the full faith and credit of the United States government is pledged, (2) certificates of deposit at savings and loan associations and federally insured banks when secured by acceptable collateral and, (3) savings accounts at savings and loan associations and banks, to the extent fully insured.

As a government agency, the California Government Code dictates guidelines toward the District's investments in addition to the District's investment policy, which has been approved by the Board of Directors. This policy provides the District's treasurer with investment authority, summarizes authorized investments, and describes the District's procedures and other limitations. The objective of the District's investment policy is to maximize the yield of



## *Notes to Combined Financial Statements*

invested funds while assuring that investments are safe from loss, utilizing the “prudent person” policy of safety, legality and yield.

Below is a summary of the District’s cash and investment policies, credit risk and description of the District’s cash and investments. Separate internal accounts or funds have been created by the District to provide for specific events in accordance with bond covenants, trust agreements or certain regulations. These “restricted” accounts may have minimum balance requirements. The primary restrictions for these accounts are due to construction of capital assets and reserves for principal and interest on outstanding debt. All remaining cash and investments are unrestricted.

Cash and investments as of December 31, 2017 and 2016 are classified in the accompanying combined financial statements as follows:

	<i>2017</i>	<i>2016</i>
Current assets - cash and cash equivalents	\$ 30,343,077	\$ 24,509,822
Noncurrent assets - restricted cash	1,153,122	22,514,842
Noncurrent assets - restricted investments	7,892,401	10,761,471
	\$ 39,388,600	\$ 57,786,135

Cash and investments as of December 31, 2017 and 2016 consisted of the following:

	<i>2017</i>	<i>2016</i>
Cash deposits with financial institutions	\$ 14,114,126	\$ 34,796,864
Deposits with Kern County	579,036	572,363
Deposits with LAIF	16,803,037	11,655,437
Investments with financial institutions	7,892,401	10,761,471
	\$ 39,388,600	\$ 57,786,135

### ***Investments:***

The District is permitted by both Board policy and State law to invest in various authorized investments, subject to a variety of limits and controls, including State of California bonds, U.S. Government Agency securities (Treasury and other federal agencies) and other securities (bankers’ acceptances, negotiable certificates of deposit, etc.). The District investment portfolio is primarily comprised of holdings in certificates of deposits, corporate and municipal bonds, and commercial paper.

### ***Disclosures relating to interest rate risk and credit risk:***

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the District manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion

**Notes to Combined Financial Statements**

of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the minimum rating required by the California Government Code and the actual rating as of year end for each investment type.

	<u>Total</u>	<u>Minimum legal rating</u>	<u>AAA-AA</u>	<u>A</u>	<u>Baa-BBB</u>	<u>Unrated</u>
Corporate & Municipal Bonds	\$ 2,591,350	A	\$ 247,620	\$ 1,519,218	\$ 771,481	\$ 53,031
Commercial Paper	\$ 2,304,816	A	\$ -	\$ 2,304,816	\$ -	\$ -

There is no minimum legal rating for U.S. Government Agency Securities and certificates of deposit.

As of December 31, 2017, the District had the following investments and maturities:

	<u>Fair Value</u>	<u>Investment maturities</u>		
		<u>Less Than 1 Year</u>	<u>1 Year to 5 Years</u>	<u>6 Years to 25 Years</u>
Certificates of Deposit	\$ 2,996,235	\$ 2,029,852	\$ 966,383	\$ -
Corporate & Municipal Bonds	2,591,350	2,240,787	350,563	-
Commercial Paper	2,304,816	2,304,816	-	-
	<u>\$ 7,892,401</u>	<u>\$ 6,575,455</u>	<u>\$ 1,316,946</u>	<u>\$ -</u>

As of December 31, 2016, the District had the following investments and maturities:

	<u>Fair Value</u>	<u>Investment maturities</u>		
		<u>Less Than 1 Year</u>	<u>1 Year to 5 Years</u>	<u>6 Years to 25 Years</u>
Certificates of Deposit	\$ 5,271,023	\$ 2,206,280	\$ 3,064,743	\$ -
Corporate & Municipal Bonds	5,490,448	2,772,855	2,627,722	89,871
	<u>\$ 10,761,471</u>	<u>\$ 4,979,135</u>	<u>\$ 5,692,465</u>	<u>\$ 89,871</u>

**Cash flows:**

GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, states for purposes of preparing the statements of cash flows, all transactions that are not classified as capital and related financing activities, noncapital financing activities or investing activities are classified as operating activities. The adjustments to reconcile operating income to net cash provided by

*Notes to Combined Financial Statements*

operating activities includes other income which consists primarily of general administrative and general project service charges and water contract income from prior years.

**Note 2. *Water Received and Delivered***

Detailed below is the water received and delivered by the District. This information does not include water that is solely pumped and utilized by farmers. Rather, water information provided below represents water that is utilized by the District.

<i><b>Water Received</b></i>	<i><b>2017</b></i> <i><b>(acre-feet)</b></i>	<i><b>2016</b></i> <i><b>(acre-feet)</b></i>
<u>Purchased from Kern County Water Agency</u>		
Entitlement		
Current year allocation (85% and 60%)	131,750	93,000
Add borrowing (carryover) to next year	(17,207)	(6,201)
Add borrowing (carryover) from prior year	6,201	4,170
Subtotal	<u>120,744</u>	<u>90,969</u>
Other	30,779	1,580
Total water received - Kern County Water Agency	<u>151,523</u>	<u>92,549</u>
Total water received from Banking Partners	<u>254,496</u>	<u>33,906</u>
Total other water received	<u>24,423</u>	<u>-</u>
Total water received from other water agencies	<u>83,551</u>	<u>3,496</u>
<u>In-District Ground Water Extraction</u>		
District wells pumped	-	46,669
Pumping agreement with landowners	-	2,705
	<u>-</u>	<u>49,374</u>
<u>Out of District Ground Water</u>		
Kern Water Bank	-	1,708
Pioneer Project	-	916
	<u>-</u>	<u>2,624</u>
<i><b>Total Water Received</b></i>	<u><u>513,993</u></u>	<u><u>181,949</u></u>

*Notes to Combined Financial Statements*

	<u>2017</u> <u>(acre-feet)</u>	<u>2016</u> <u>(acre-feet)</u>
<b><i>Water Delivered</i></b>		
<u>Delivered In-District</u>		
Contract	117,748	81,670
Noncontract	203,410	50,523
In-District spreading and overdraft correction	52,422	-
Supplemental Ag water	-	6,199
Other	28,216	31
Total Water Delivered - In-District	<u>401,796</u>	<u>138,423</u>
Banked with other Agencies	<u>104,264</u>	<u>140</u>
Returned to other water agencies	<u>5,374</u>	<u>11,654</u>
Returned to Landowners	-	2,177
Returned to Banking Partners	-	19,282
Returned to Banking Partners exchange	-	-
	<u>-</u>	<u>21,459</u>
Losses	<u>2,559</u>	<u>10,273</u>
<b><i>Total Water Delivered</i></b>	<u><u>513,993</u></u>	<u><u>181,949</u></u>

**Note 3. Restricted Assets**

***Reserve funds:***

The District maintains several reserve funds under provisions of loan contracts and bond issuances and other restrictions. The amounts required for each fund are as follows:

	<u>2017</u>		<u>2016</u>	
	<u>Amount</u> <u>Required</u>	<u>Amount on</u> <u>Deposit</u>	<u>Amount</u> <u>Required</u>	<u>Amount on</u> <u>Deposit</u>
Bond and loan reserve fund	\$ 8,997,929	\$ 8,997,929	\$ 33,239,283	\$ 33,239,283
Cafeteria plan	47,594	47,594	37,030	37,030
	<u>\$ 9,045,523</u>	<u>\$ 9,045,523</u>	<u>\$ 33,276,313</u>	<u>\$ 33,276,313</u>

The provisions of the various loan contracts and reserve funds are as follows:

***Bond and loan reserve fund:***

The provisions of the District's various bond issuances and loans from the State of California, Department of Water Resources require the District to maintain reserves until the bonds have been redeemed, certain loan requirements are satisfied or until bond proceeds are exhausted.

## *Notes to Combined Financial Statements*

### ***Cafeteria plan:***

The District has a cafeteria plan whereby employees may elect to defer a portion of their current salary to be reimbursed for future medical expenses.

### ***Note 4. Investments***

#### ***Investment in Kern Water Bank Authority:***

Upon adoption of the Monterey Agreement in 1997, the District obtained a 6.67% interest in Kern Water Bank Authority (KWBA) by reducing the District's annual entitlement water from 158,000 acre-feet to 155,000 acre-feet. The District is able to store water at the KWBA in wet years and draw water in dry years. The District's investment in Kern Water Bank Authority is accounted for using the equity method. Under this method, the District recognizes its share of KWBA's accrual basis income or loss. The District's equity in income from this investment for the years ended December 31, 2017 and 2016 was \$476,792 and \$129,531, respectively. The earnings from this investment are included in equity in income (loss) from investments on the combined statements of revenues and expenses.

#### ***Investment in Southern California Water Bank Authority:***

On July 28, 2008, the District entered into a Joint Powers Agreement with Valley Mutual Water Company, LLC and Rosamond Community Service District to create Semitropic-Rosamond Water Bank Authority. During 2017, the name of the Authority was changed to Southern California Water Bank Authority ("SCWBA").

Initially, SCWBA was to consist of a "First Priority Right" to the following interests in the District's Stored Water Recovery Unit (SWRU) banking project that will provide: (1) 33,333 AF/year of SWRU Delivery Capacity, (2) 300,000 AF of SWRU Storage Capacity, and (3) 100,000 AF/year of SWRU Recovery and Return Capacity, together with rights to certain unused capacities in the SWRU and other elements of the Semitropic Water Bank, and the following rights in the Antelope Valley Water Bank (AVWB): (1) 100,000 AF/year of AVWB Delivery Capacity, (2) 500,000 AF of AVWB Storage Capacity, and (3) 100,000 AF/year of AVWB Recovery and Return Capacity. As part of the agreement, the District recorded an investment in the amount of \$20,000,000, which represented the District's equity ownership in SCWBA.

In 2012, the SCWBA joint powers agreement was amended which essentially bifurcated the two water bank operations and defined which assets and liabilities of SCWBA were owned and to be maintained by each member. In addition, beginning in 2013, all revenues and expenses would be allocated to each member on an agreed upon methodology in lieu of allocating the change in net position based on the membership interest.

The District's investment in SCWBA is accounted for using the equity method. Under this method, the District recognizes its share of SRWBA's accrual basis income or loss. The District's equity in income (loss) from this investment for the years ended December 31, 2017 and 2016 was \$(899,091) and \$199,154 respectively. The earnings from this investment are included in equity in income (loss) from investments on the combined statements of revenue and expenses.

*Notes to Combined Financial Statements*

**Note 5. Notes Receivable**

Notes receivable consists of the following at December 31, 2017 and 2016:

	<i>2017</i>	<i>2016</i>
Note receivable, Poso Creek Water Company, LLC, 5.19%, secured by letter of credit in favor of the District for 18% of outstanding balance and 20,000 AF of water in storage, semi-annual principal and interest payments of \$728,523, due December 2026	\$ 10,371,967	\$ 11,256,229
Note receivable, Homer, LLC, 5.5%, secured by letter of credit in favor of the District for 30% of outstanding balance, \$2,000,000 due in 2013 with graduated principal and interest payments due annually beginning January 1, 2014, due January 2023	4,350,081	4,545,424
	14,722,048	15,801,653
Less current portion	(1,270,431)	(1,079,667)
	\$ 13,451,617	\$ 14,721,986

*Notes to Combined Financial Statements*

**Note 6. Capital Assets**

The following is a summary of changes in the District's capital assets for the years ended December 31, 2017 and 2016:

	<i>Assets-At Cost</i>				
	<u>Balance 12/31/16</u>	<u>Acquisitions</u>	<u>Retirements</u>	<u>Reclass/ Transfers</u>	
<b>Capital Assets not being depreciated:</b>					
Land	\$ 74,085,879	\$ 20,006,750	\$ -	\$ -	\$ 94,092,629
Construction in progress	23,354,070	7,592,230	(210,604)	(5,372,540)	25,363,156
<b>Capital Assets being depreciated:</b>					
Transmission and distribution equipment	260,241,269	403,595	-	738,015	261,382,879
Autos and trucks	1,420,502	390,311	(133,456)	-	1,677,357
Office equipment	555,199	42,997	(21,649)	-	576,547
Field and misc. equip.	1,075,181	117,939	-	(110,461)	1,082,659
Well drilling equip.	2,991,282	-	(807)	-	2,990,475
Wells	9,090,205	9,070	-	4,744,986	13,844,261
General plant and equipment	3,132,999	-	-	-	3,132,999
Capacity rights	4,503,542	-	-	-	4,503,542
	<u>\$ 380,464,877</u>	<u>\$ 28,562,892</u>	<u>\$ (366,516)</u>	<u>\$ -</u>	<u>\$ 408,661,253</u>
<b>Accumulated Depreciation</b>					
	<u>Balance 12/31/16</u>	<u>Depreciation Expense</u>	<u>Retirements</u>	<u>Reclass/ Transfers</u>	<u>Balance 12/31/17</u>
Transmission and distribution equipment	\$ 97,532,154	\$ 5,938,852	\$ -	\$ -	\$ 103,471,006
Autos and trucks	1,319,529	71,301	(132,587)	-	1,258,243
Office equipment	461,409	36,483	(21,288)	-	476,604
Field and misc. equip.	629,713	86,084	-	-	715,797
Well drilling equip.	1,692,042	128,527	(314)	-	1,820,255
Wells	732,492	366,810	-	-	1,099,302
General plant and equipment	1,308,701	80,012	-	-	1,388,713
Capacity rights	975,350	195,952	-	-	1,171,302
	<u>\$ 104,657,966</u>	<u>\$ 6,905,346</u>	<u>\$ (154,189)</u>	<u>\$ -</u>	<u>\$ 111,409,123</u>

*Notes to Combined Financial Statements*

	<i>Assets-At Cost</i>				
	<i>Balance</i> <i>12/31/15</i>	<i>Acquisitions</i>	<i>Retirements</i>	<i>Reclass/ Transfers</i>	<i>Balance</i> <i>12/31/16</i>
<b>Capital Assets not being depreciated:</b>					
Land	\$ 54,085,879	\$ 20,000,000	\$ -	\$ -	\$ 74,085,879
Construction in progress	33,094,527	5,969,200	(330,915)	(15,378,742)	23,354,070
<b>Capital Assets being depreciated:</b>					
Transmission and distribution equipment	248,918,552	-	-	11,322,717	260,241,269
Autos and trucks	1,509,728	-	(89,226)	-	1,420,502
Office equipment	551,284	12,932	(9,017)	-	555,199
Field and misc. equip.	1,041,434	33,747	-	-	1,075,181
Well drilling equip.	2,950,225	41,057	-	-	2,991,282
Wells	5,034,180	-	-	4,056,025	9,090,205
General plant and equipment	3,132,999	-	-	-	3,132,999
Capacity rights	4,503,542	-	-	-	4,503,542
	<b>\$ 354,837,099</b>	<b>\$ 26,056,936</b>	<b>\$ (429,158)</b>	<b>\$ -</b>	<b>\$ 380,464,877</b>

	<i>Accumulated Depreciation</i>				
	<i>Balance</i> <i>12/31/15</i>	<i>Depreciation</i> <i>Expense</i>	<i>Retirements</i>	<i>Reclass/ Transfers</i>	<i>Balance</i> <i>12/31/16</i>
Transmission and distribution equipment	\$ 91,842,259	\$ 5,689,895	\$ -	\$ -	\$ 97,532,154
Autos and trucks	1,360,940	47,815	(89,226)	-	1,319,529
Office equipment	433,728	36,698	(9,017)	-	461,409
Field and misc. equip.	513,450	116,263	-	-	629,713
Well drilling equip.	1,565,631	126,411	-	-	1,692,042
Wells	527,990	204,502	-	-	732,492
General plant and equipment	1,228,688	80,013	-	-	1,308,701
Capacity rights	779,397	195,953	-	-	975,350
	<b>\$ 98,257,334</b>	<b>\$ 6,498,875</b>	<b>\$ (98,243)</b>	<b>\$ -</b>	<b>\$ 104,657,966</b>



*Notes to Combined Financial Statements*

**Note 7. Long-Term Debt**

Long-term debt at December 31, 2017 and 2016 was as follows:

	<i>2017</i>	<i>2016</i>
Contract payable, State of California, 2.4%, unsecured, payable \$135,321 semiannually including interest, due May 2023 (proceeds were used for construction of groundwater recharge project)	\$ 1,504,182	\$ 1,734,635
Contract payable, State of California, 2.6%, unsecured, payable \$55,052 semiannually including interest, due August 15, 2023 (proceeds were used for construction of groundwater recharge project)	608,112	700,625
Contract payable, State of California, 2.6%, unsecured, payable \$161,076 semiannually including interest, due December 31, 2025 (proceeds were used for construction of a water distribution system)	2,197,331	2,459,489
Contract payable, State of California, 2.4%, unsecured, payable \$159,792 semiannually including interest, due April 1, 2025 (proceeds were used for construction of a water distribution system)	2,665,530	2,916,665
2007 Revenue Bonds, 3.586%, collateralized by rights to deposits in investment accounts, principal payable semiannually, interest payable monthly, paid in full (proceeds used for District's share of construction costs of CVC project)	-	273,334
2009A Refunding Revenue Bonds, interest rates vary over life of bonds between 2.5% -5.25%, collateralized by the District's general project service charges, principal payable annually, interest payable semi-annually, paid in full (proceeds were used to refund 2008 bonds, fund a reserve for the bonds, and pay for cost of issuance of bonds)	-	34,215,000

*Notes to Combined Financial Statements*

<p>2012A Revenue Bonds, interest rates vary over life of bonds between 2% - 5%, collateralized by future groundwater banking revenue, principal payable annually, interest payable semi-annually, due December 1, 2035 (proceeds were used to refund 2004 and 2006 bonds, refund 2011 warrants, fund a reserve for the bonds, and pay for cost of issuance of bonds)</p>	73,710,000	74,450,000
<p>2012B Revenue Bonds, 2.8%, collateralized by future groundwater banking revenue, principal payable annually, interest payable semi-annually, due December 1, 2022 (proceeds were used to refund 2004 and 2006 bonds, refund 2011 warrants, fund a reserve for the bonds, and pay for cost of issuance of bonds)</p>	6,715,000	7,550,000
<p>2013A Revenue Bonds, interest rates vary over life of bonds between 3% - 5%, collateralized by the District's general project service charges, principal payable annually, interest payable semi-annually, due December 1, 2023 (proceeds used to finance miscellaneous construction projects )</p>	6,205,001	7,110,001
<p>2014A Revenue Bonds, interest rates vary over life of bonds between 3% - 5%, collateralized by the District's general project service charges, principal payable annually, interest payable semi-annually, due December 1, 2024 (proceeds used to purchase land and finance certain construction projects)</p>	14,790,000	16,565,000
<p>2015A Revenue Bonds, interest rates vary over life of bonds between 3% - 5%, collateralized by the District's general project service charges, principal payable annually, interest payable semi-annually, due December 1, 2045 (proceeds used to refund a portion of the 2009 bonds and was used to purchase land)</p>	31,420,000	31,800,000

*Notes to Combined Financial Statements*

2017A Revenue Bonds, interest rates vary over life of bonds between 3% - 5%, collateralized by the District's general project service charges, principal payable annually, interest payable semi-annually, due December 1, 2037 (proceeds used to refund a portion of the 2009 bonds and 2016 warrants )	52,375,000	-
2016 Warrants, 2.48%, collateralized by a second lien on the District's general project service charges, interest payable semi-annually, paid in full (proceeds used to purchase land for a future project)	-	23,000,000
	192,190,156	202,774,749
2005 Interest Rate Swap, at cost (See Note 9)	2,218,000	2,550,700
Plus premiums, net of accumulated amortization 2017, \$1,955,622; 2016, \$1,454,498	13,627,842	11,989,068
Less current maturities	(7,711,827)	(29,909,330)
Long term debt, plus premiums and less current maturities	\$ 200,324,171	\$ 187,405,187

**Notes to Combined Financial Statements**

The following is a summary of the long-term debt transactions for the years ended December 31, 2017 and 2016:

	<u><b>Payable</b></u> <u><b>12/31/16</b></u>	<u><b>Additions</b></u>	<u><b>Deletions</b></u>	<u><b>Payable</b></u> <u><b>12/31/17</b></u>	<u><b>Due within</b></u> <u><b>One Year</b></u>
Bond principal	\$ 171,963,335	\$ 52,375,000	\$ (39,123,334)	\$ 185,215,001	\$ 6,855,000
Warrants	23,000,000	-	(23,000,000)	-	-
Loans, State of California	7,811,414	-	(836,259)	6,975,155	856,827
	<u>202,774,749</u>	<u>52,375,000</u>	<u>(62,959,593)</u>	<u>192,190,156</u>	<u>\$ 7,711,827</u>
Fair Value of interest rate swap	15,557,034	-	(1,492,173)	14,064,861	
	<u>\$ 218,331,783</u>	<u>\$ 52,375,000</u>	<u>\$ (64,451,766)</u>	<u>\$ 206,255,017</u>	
	<u><b>Payable</b></u> <u><b>12/31/15</b></u>	<u><b>Additions</b></u>	<u><b>Deletions</b></u>	<u><b>Payable</b></u> <u><b>12/31/16</b></u>	<u><b>Due within</b></u> <u><b>One Year</b></u>
Bond principal	\$ 177,859,886	\$ -	\$ (5,896,551)	\$ 171,963,335	\$ 6,073,334
Warrants	-	23,000,000	-	23,000,000	23,000,000
Loans, State of California	8,954,678	-	(1,143,264)	7,811,414	835,996
	<u>186,814,564</u>	<u>23,000,000</u>	<u>(7,039,815)</u>	<u>202,774,749</u>	<u>\$ 29,909,330</u>
Fair Value of interest rate swap	17,270,159	(1,713,125)	-	15,557,034	
	<u>\$ 204,084,723</u>	<u>\$ 21,286,875</u>	<u>\$ (7,039,815)</u>	<u>\$ 218,331,783</u>	

The annual requirements to amortize all debt outstanding as of December 31, 2017 are as follows:

<u><b>Years Ending</b></u> <u><b>December 31,</b></u>	<u><b>Principal</b></u>	<u><b>Interest</b></u>	<u><b>Interest Rate</b></u> <u><b>Swaps, net</b></u>	<u><b>Total</b></u> <u><b>Debt Service</b></u>
2018	\$ 7,711,827	\$ 8,230,133	\$ 1,660,302	\$ 17,602,262
2019	8,178,269	7,950,440	1,612,282	17,740,991
2020	8,825,179	7,645,931	1,560,419	18,031,529
2021	9,307,831	7,285,580	1,504,518	18,097,929
2022	9,855,880	6,894,579	1,444,569	18,195,028
2023-2027	43,061,170	28,040,295	6,158,730	77,260,195
2028-2032	47,410,000	18,461,702	3,874,040	69,745,742
2033-2037	45,880,000	7,523,488	875,706	54,279,194
2038-2042	8,115,000	1,891,600	-	10,006,600
2043-2045	3,845,000	390,750	-	4,235,750
	<u>\$ 192,190,156</u>	<u>\$ 94,314,498</u>	<u>\$ 18,690,566</u>	<u>\$ 305,195,220</u>

*Notes to Combined Financial Statements*

**Note 8. Fair Value Measurement**

The District categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The hierarchy is based on the valuation inputs used to measure the fair value of the assets. Level 1 inputs are quoted prices in active markets for identical assets or liabilities; Level 2 inputs are quoted market prices for similar assets or liabilities, quoted market prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data of substantially the full term of the assets or liabilities; Level 3 inputs are significant unobservable inputs for assets or liabilities. The District's recurring fair value measurements as of December 31, 2017 and 2016 are as follows:

<i>December 31, 2017</i>				
<i>Fair Value Measurements Using:</i>				
<i>Fair Value</i>	<u><i>Level 1</i></u>	<u><i>Level 2</i></u>	<u><i>Level 3</i></u>	
<b><i>Investments:</i></b>				
Certificates of Deposit	\$ 2,996,235	\$ 2,996,235	\$ -	\$ -
Corporate & Municipal Bonds	2,591,350	2,591,350	-	-
Commercial Paper	2,304,816	2,304,816		
	<u>\$ 7,892,401</u>	<u>\$ 7,892,401</u>	<u>\$ -</u>	<u>\$ -</u>
<b><i>Obligations under interest rate swap:</i></b>				
Sun Trust Swap	\$ (14,064,861)	\$ -	\$ (14,064,861)	\$ -
	<u>\$ (14,064,861)</u>	<u>\$ -</u>	<u>\$ (14,064,861)</u>	<u>\$ -</u>
 <i>December 31, 2016</i>				
<i>Fair Value Measurements Using:</i>				
<i>Fair Value</i>	<u><i>Level 1</i></u>	<u><i>Level 2</i></u>	<u><i>Level 3</i></u>	
<b><i>Investments:</i></b>				
Certificates of Deposit	\$ 5,271,023	\$ 5,271,023	\$ -	\$ -
Corporate & Municipal Bonds	5,490,448	5,490,448	-	-
	<u>\$ 10,761,471</u>	<u>\$ 10,761,471</u>	<u>\$ -</u>	<u>\$ -</u>
<b><i>Obligations under interest rate swap:</i></b>				
Sun Trust Swap	\$ (15,553,562)	\$ -	\$ (15,553,562)	\$ -
Wells Fargo	(3,472)	-	(3,472)	-
	<u>\$ (15,557,034)</u>	<u>\$ -</u>	<u>\$ (15,557,034)</u>	<u>\$ -</u>

*Notes to Combined Financial Statements*

**Note 9. Derivatives**

The District accounts for derivatives under GASB No. 53, *Accounting and Financial Reporting for Derivative Instruments*. The objectives and terms of the District's hedging derivative instruments outstanding at December 31, 2017 are listed below:

	<u>Type</u>	<u>Objective</u>	<u>Effective Date</u>	<u>Maturity Date</u>	<u>Terms</u>
Sun Trust Swap	Pay-fixed interest rate swap	Hedge of changes in interest rates of future bond issuances	9/1/2014	12/1/2035	Pay 5.12%, receive 69% of LIBOR
Wells Fargo Swap	Pay-fixed interest rate swap	Hedge of changes in interest rates of the 2007 Revenue Bonds	11/15/2007	5/15/2017	Pay 3.586%, receive LIBOR

	<u>Fair Value</u>	<u>Notional Amount</u>	<u>Change in Fair Value</u>	<u>Change in Fair Value</u>
Sun Trust Swap	\$ (14,064,861)	\$40,592,452	Nonoperating income (expense)	\$ 1,488,701
Wells Fargo Swap	<u>-</u> <u>\$ (14,064,861)</u>	\$ -	Deferred outflow of interest rate swap	\$ 3,472

The objectives and terms of the District's hedging derivatives instruments at December 31, 2016 are listed below:

	<u>Fair Value</u>	<u>Notional Amount</u>	<u>Change in Fair Value</u>	<u>Change in Fair Value</u>
Sun Trust Swap	\$ (15,553,562)	\$41,682,515	Nonoperating income (expense)	\$ 1,693,049
Wells Fargo Swap	<u>(3,472)</u> <u>\$ (15,557,034)</u>	\$ 272,338	Deferred outflow of interest rate swap	\$ 20,076

## *Notes to Combined Financial Statements*

On October 27, 2005, the District entered into an off-market forward starting swap (2005 swap). The swap commenced September 1, 2014, and is based on an initial notional amount of \$53,895,000. The pay-fixed, receive-variable swap generated debt service savings in the form of an upfront payment in the amount of \$3,927,850, from the counterparty, SunTrust Bank (SunTrust). This amount is recorded in the combined statements of net position as long-term debt and is not adjusted to the fair value at each reporting date. During the year ended December 31, 2006, \$600,850 of the swap upfront payment was paid back as part of the advance refunding of the 2003 Revenue Bonds of the District, leaving \$3,327,000 to be amortized when the swap agreement commenced. During the year ended December 31, 2012, the District issued the 2012 bonds which advanced refunded the 2004 bonds. In accordance with GASB No. 53, the District elected to include the Sun Trust swap as part of the defeasance of the 2004 bonds. The fair value of the Sun Trust swap of \$17,251,826 at December 31, 2012 was included in the deferred loss of the defeasance of the 2004 and 2006 bonds and is included in the deferred outflow of advance refunding of bonds on the combined statements of net position. This amount will be amortized over the term of the 2012 bonds. Beginning in 2013, changes in fair value of the Sun Trust interest rate swap are recognized in nonoperating income (expense) on the combined statements of revenues and expenses.

On April 24, 2007, the District entered into an off-market swap with Wells Fargo Bank (Wells Fargo) in anticipation of a projected future issuance of variable rate bonds to synthetically advance refund the District's 2007 Bonds. The swap commenced November 15, 2007, and is based on an initial notional amount of \$5,000,000. The swap expired in 2017.

The fair values of the interest rate swaps were estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swaps.

### ***Risks***

*Credit Risk* - Credit risk is the risk that Sun Trust Bank cannot fulfill the terms and obligations specified in the swap agreement. Because the swap had a negative fair value as of December 31, 2017, the District did not have exposure related to credit risk on its swap. However, the District would have exposure related to credit risk in the amount of the swaps' positive fair value if interest rates increased to cause the fair value of the swaps to become positive. The credit rating of Wells Fargo and SunTrust is AA- and BBB+ by Standard & Poors.

*Basis Risk* - The District is exposed to basis risk on its 2005 pay-fixed interest rate swap because the variable rate payments received are equal to 69% of LIBOR, which is currently not hedging any outstanding variable interest debt. Based on the significance and extent of any basis risk exposure, the purpose of the swap to generate debt service savings is not being realized.

*Termination Risk* - Under certain terms of the respective contracts, either the District or SunTrust may terminate the swap from nonperformance from the other party. If the swap is terminated, the projected future issuance of variable rate bonds would no longer be hedged to a fixed rate. If the swap is terminated and the swap has a negative fair value, the District would be liable to SunTrust for a payment equal to the fair value of the swap. The additional termination events in the agreement are limited to credit related events only and the ratings triggers are substantially below the current credit rating of SunTrust and the District.

**Notes to Combined Financial Statements**

*Market Access Risk* – At this time, the District will most likely not issue variable rate debt to coincide with the Sun Trust Swap.

*Rollover Risk* – At this time, the District is not exposed to rollover risk.

*Foreign Currency Risk* - All derivatives are denominated in U.S. dollars and therefore, the District is not exposed to foreign currency risk.

**Note 10. Self-Insurance**

The District is a member of the Association of California Water Agencies, Joint Powers Insurance Authority (JPIA). JPIA is a group of California Water Districts who have pooled funds to provide self-insurance coverage as follows:

<u>Type of Coverage</u>	<u>Limits per Occurrence Self-Insurance</u>	<u>Limits per Occurrence Excess Insurance</u>
General liability/ automobile liability/ public officials liability	\$5,000,000	\$5,000,000-\$55,000,000
Fidelity insurance	\$ 100,000	\$100,000-\$500,000
Property insurance	\$ 100,000	\$100,000-\$150,000,000

The District is in a group with a \$0 retention level (deductible) per occurrence for the general liability, \$5,000 per occurrence for buildings, personal property, fixed equipment and mobile equipment, \$500 per occurrence on licensed vehicles, \$1,000 per occurrence for fidelity claims, and \$25,000 - \$50,000 for machinery. Claims over the retention levels are insured by the group up to the self-insurance limits (see above) and by policies purchased by JPIA from Markel-Evanston Insurance Company, Great American Insurance Co. of New York, Great American Insurance Company, Great American E & S (AMWINS), Allied Public Risk/ Allied World Assurance Co., General Security Indemnity Co of Arizona, XL Insurance America, Inc., Hartford Fire Insurance Co. and Endurance Risk Solutions Assurance Company for the excess.

JPIA bills the District a deposit premium at the beginning of each policy year, which is placed in a reserve fund to cover the self-insurance portion of any claim. Settlements and/or expenses related to claims during the year are charged against the reserve. If the balance of the reserve at the end of the year is deemed too low in relation to the amount of outstanding claims, the District is billed for additional premiums. When the claims are fully settled, any amounts remaining in the reserve are refunded to the District.

**Note 11. Commitments and Contingencies**

***Water Supply Contract with Kern County Water Agency:***

The District obtained its surface water supply in accordance with certain contracts signed between 1969 and 1974 with the Kern County Water Agency (Agency), amended to its current annual amount of 155,000 acre feet of entitlement surface water, through the year 2039. The Agency, in turn, obtained its surface water supply in 1963 when it signed a contract with the State of California, Department of Water Resources (DWR), to purchase annual surface water, currently contracted at 998,731 acre feet, through the State Water Project (SWP) through the year 2035.



## *Notes to Combined Financial Statements*

The District's contract with the Agency provides for various separate charges, all of which are included in "source of supply" in operating expenses of the District's combined statements of revenues and expenses. The "fixed charge" component of the contract is not necessarily reduced by annual water supply deficiencies as the District is obligated to pay 100% of the annual fixed costs billed by the Agency. Under certain circumstances, fixed charges could be reduced by the DWR when the District receives less than its full entitlement in years of low water supply. Source of supply costs attributable to this contract were \$14,543,974 and \$11,878,736 for the years ended December 31, 2017 and 2016, respectively.

On March 13, 2008, Judge Wanger of the Fresno Federal Court, ordered DWR to reduce the amount of SWP water exported by the Delta pumps.

On May 25, 2010, Judge Wanger of the Fresno Federal Court eased pumping restrictions that were set in place on March 13, 2008. The federal court granted a preliminary injunction on the biological opinion for salmon, stating that the federal agencies responsible for drafting the biological opinion must take in account human impacts and also demonstrate why certain water exports restriction were called for in the opinion.

Because of the continuing possibility of state water allocations being maintained at reduced levels for water users due to the 2008 and 2010 decisions, the District has developed several programs to augment the District's available water supply among which are, the utilization of wells, banking programs and the transfer of water from sources outside the District. Additionally, the District continues to work on the financial aspect of the problems in an attempt to reduce charges and increase the reliability of the water supply to water users, wherever possible.

During the years ended December 31, 2017 and 2016, the DWR allocated 85% and 60%, respectively, of entitlement to state water contractors, due to the snow and rain activity during the winter of 2016-17. Due to the continued pumping restrictions, the DWR has issued a 35% allocation for the 2018 water year as of the date of this report.

### ***Uncalled assessments:***

The Improvement Districts have levied assessments in prior years which have not been called. The uncalled assessments in the Improvement Districts serve as security on construction financing for Project Unit One in the Pond-Poso Improvement District and the Project Units One and Two in the Buttonwillow Improvement District. Uncalled assessments at December 31, 2017 and 2016 were \$4,059,411.

As part of the Energy Development Element project approval vote on November 26, 1991, an assessment was authorized in the amount of \$119 per acre on approximately 125,947 acres, for a total adjusted assessment of \$14,987,729. These assessments will collateralize the bonds until paid. It is anticipated these assessments, which were levied in February 1992, will remain uncalled and that bond obligations will be paid from operations.

Although the assessments have been levied, they are uncalled and are not reflected as an asset and related liability in the combined financial statements. These assessments will not be recognized until such time as they are called by the District.

## Notes to Combined Financial Statements

### Legal:

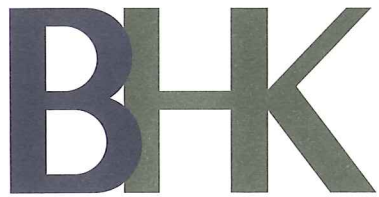
The District is currently a party to various legal proceedings, some of which are covered by insurance. The amount or range of possible loss, if any, is not reasonably subject to estimation. Notwithstanding the uncertainties associated with litigation, management, including general counsel, currently believe that the ultimate outcome of these proceedings, individually and in the aggregate, will not have a material adverse effect on the District's financial position or cash flows.

### Note 12. Retirement Plan

The District contributes to the Semitropic Water Storage District 401(k) Plan, a defined contribution pension plan. The District administers the Plan, which covers all eligible employees, and can amend the Plan or its contributions at any time. The Plan consists of investments in mutual funds with John Hancock, Principal Financial and Invesco. The District contributes an amount equal to 10% of the employees' base salary each month to the employees' pension plan. Employees are required to contribute 4% of base salary each month to receive District contributions, but can contribute up to the statutory IRS limits. To determine the base salary for the plan year, the rates applicable on January 1 are used throughout the plan year and adjusted during the year if a pay increase is given. An employee is eligible for participation in the retirement plan after six months of service. The District's contributions for each employee are 20% vested after two years of employment with vesting increasing 20% for each additional year of employment up to six years. The District's contributions are 100% vested after six years of employment. Unvested contributions and interest forfeited by employees who leave before six years of service are used to reduce the District's current-period contribution requirement or offset plan expenses.

The District's payroll and contributions for the years ended December 31, 2017 and 2016 were as follows:

	<u>2017</u>	<u>2016</u>
Total payroll	<u>\$ 3,405,840</u>	<u>\$ 3,436,971</u>
Base salary for computing contributions	<u>\$ 3,140,921</u>	<u>\$ 3,035,233</u>
District contributions	<u>\$ 312,327</u>	<u>\$ 294,231</u>
Employee contributions	<u>\$ 177,895</u>	<u>\$ 166,911</u>



BARBICH HOOPER KING  
DILL HOFFMAN

ACCOUNTANCY CORPORATION

**Independent Auditors' Report on Internal Control over Financial Reporting  
and on Compliance and Other Matters Based on an Audit of Financial Statements  
Performed in Accordance with Government Auditing Standards**

Board of Directors  
Semitropic Water Storage District  
Wasco, California

We have audited, 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, the combined financial statements of Semitropic Water Storage District as of and for the years ended December 31, 2017 and 2016, and the related notes to the combined financial statements, which collectively comprise Semitropic Water Storage District's basic financial statements, and have issued our report thereon dated June 19, 2018.

**Internal Control over Financial Reporting**

In planning and performing our audits of the combined financial statements, we considered Semitropic Water Storage District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the combined financial statements, but not for the purpose of expressing an opinion on the effectiveness of Semitropic Water Storage District's internal control. Accordingly, we do not express an opinion on the effectiveness of the Semitropic Water Storage District'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 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. However, material weaknesses may exist that have not been identified.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Semitropic Water Storage District's combined 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 audits, 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 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.

**BARBICH HOOPER KING**  
**DILL HOFFMAN**  
Accountancy Corporation



Bakersfield, California  
June 19, 2018

*Semitropic Water Storage District*

*Combined Schedules of Operating Expenses  
For the Years Ended December 31, 2017 and 2016*

	<u>2017</u>	<u>2016</u>	<u>Increase (Decrease)</u>
<b><i>Transmission and distribution:</i></b>			
Power	\$ 7,935,120	\$ 9,514,306	\$ (1,579,186)
Salaries and wages	1,727,074	1,702,872	24,202
Repairs and maintenance	1,079,244	1,423,720	(344,476)
Water banking expenses	3,449,132	939,612	2,509,520
Employee benefits	967,445	886,508	80,937
Fuel and oil	341,424	183,488	157,936
Payroll taxes	165,535	157,551	7,984
Operating supplies	66,673	61,868	4,805
Miscellaneous	8,522	2,778	5,744
Equipment rent	42,710	38,097	4,613
Utilities	19,207	21,120	(1,913)
Licenses and fees	6,372	5,466	906
Equipment maintenance	266	70	196
	<u>\$ 15,808,724</u>	<u>\$ 14,937,456</u>	<u>\$ 871,268</u>
<b><i>Source of supply:</i></b>			
State Water Project table 1 entitlement	\$ 12,572,861	\$ 11,878,736	\$ 694,125
Other	271,250	503,611	(232,361)
	<u>\$ 12,844,111</u>	<u>\$ 12,382,347</u>	<u>\$ 461,764</u>

	<u>2017</u>	<u>2016</u>	<u><i>Increase (Decrease)</i></u>
<b><i>General and administrative:</i></b>			
Salaries and wages	\$ 1,309,235	\$ 1,365,444	\$ (56,209)
Consulting	602,584	923,232	(320,648)
Employee benefits	553,560	574,094	(20,534)
Repairs and maintenance	261,168	389,954	(128,786)
Legal	325,745	179,753	145,992
Insurance	176,291	171,320	4,971
Public relations	10,000	162,500	(152,500)
Engineering	272,198	127,291	144,907
Dues	269,983	155,916	114,067
Payroll taxes	85,929	98,846	(12,917)
Utilities	64,107	61,489	2,618
Office	61,925	52,013	9,912
Accounting and auditing	46,675	46,850	(175)
Travel	47,168	28,032	19,136
Financing and administration	17,507	19,641	(2,134)
Building services	19,702	18,084	1,618
Equipment rent	17,922	16,851	1,071
Bank fees	12,381	11,670	711
Directors' fees and expense	10,290	10,785	(495)
Marketing	6,911	2,734	4,177
Property taxes	2,077	1,962	115
Allocation of G&A costs to capital assets	<u>(1,065,140)</u>	<u>(473,286)</u>	<u>(591,854)</u>
	<u>\$ 3,108,218</u>	<u>\$ 3,945,175</u>	<u>\$ (836,957)</u>
<b><i>Depreciation and amortization expense</i></b>	<u>\$ 6,905,347</u>	<u>\$ 6,498,874</u>	<u>\$ 406,473</u>