

**SANTA ANA WATERSHED ASSOCIATION  
FINANCIAL STATEMENTS  
AND  
REQUIRED SUPPLEMENTARY INFORMATION  
WITH  
INDEPENDENT AUDITORS' REPORT  
FOR THE YEAR ENDED  
DECEMBER 31, 2015**

# SANTA ANA WATERSHED ASSOCIATION

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December 31, 2015

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## Independent Auditors' Report

To the Board of Directors  
Santa Ana Watershed Association  
Riverside, California

We have audited the accompanying basic financial statements of Santa Ana Watershed Association ("SAWA") as of and for the year ended December 31, 2015 and the related notes to the financial statements as listed in the table of contents.

### Management's Responsibility for the Financial Statements

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

### Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to SAWA's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of SAWA's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Santa Ana Watershed Association as of December 31, 2015, and the changes in financial position and its cash flows for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

## **Emphasis of Matter**

### *Uncertain Net Position Restrictions*

As discussed in Note 11 to the financial statements, SAWA is undergoing an agreed-upon procedures engagement to determine possible restricted balances pertaining to funds received from the Orange County Water District, a related party. In addition, it is currently reviewing costs allocated to specific projects and contemplating a retroactive change to its cost allocations which would change its expendable restricted net position. These issues have not been resolved and could potentially have significant effects on SAWA's unrestricted net position. Our opinion is not modified with respect to this matter.

## **Report on Summarized Comparative Information**

We have previously audited the Santa Ana Watershed Association's 2014 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated October 29, 2015. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2014 is consistent, in all material respects, with the audited financial statements from which it has been derived.

## **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 to 7 be presented to supplement the basic financial statements. Such information, although not 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 audits 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.

*Ahena Adcock Devlin LLP*

January 25, 2017

**MANAGEMENT'S DISCUSSION AND ANALYSIS - UNAUDITED**

**SANTA ANA WATERSHED ASSOCIATION**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS - UNAUDITED**  
**December 31, 2015**

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As management of the Santa Ana Watershed Association ("SAWA"), we offer readers of SAWA's financial statements this narrative overview and analysis of SAWA's financial activities during the fiscal year ended December 31, 2015. Please read it in conjunction with SAWA's financial statements and accompanying notes to those financial statements.

**Financial Highlights**

- Total net position decreased by \$931,029 or 11.6 percent.
- Capital assets decreased by \$1,733 or 1.2 percent.
- Current assets decreased by \$673,965 or 17.71 percent.

**Overview of the Financial Statements**

This discussion and analysis is intended to serve as an introduction of SAWA's financial statements. SAWA operates as a nonprofit public benefit corporation. SAWA's Board of Directors is composed of, or appointed by, selected officials of local government agencies. Accordingly, SAWA is subject to governmental accounting principles and is accounted for as an enterprise fund, using the full accrual basis of accounting. As an enterprise fund, SAWA's financial statements are comprised of two components: financial statements and notes to the financial statements.

In accordance with GASB Statement No. 34, SAWA's financial statements include a statement of net position, statement of revenues, expenses and changes in net position, and a statement of cash flows.

The statement of net position presents information on all of SAWA's assets and liabilities, with the differences between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of SAWA is improving or deteriorating.

The statement of revenues, expenses, and changes in net position presents information showing how SAWA's net position changed during the year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flow in future fiscal periods.

The statement of cash flows conveys to financial statement users how SAWA managed cash resources during the year. This statement converts the change in net position presented on the statement of revenues, expenses, and changes in net position into actual cash provided by and used for operations. The statement of cash flows also details how SAWA obtains cash through financing and investing activities, and how cash is spent for these purposes.

The notes to the financial statements provide additional information that is essential to a full understanding of the financial statements.

**SANTA ANA WATERSHED ASSOCIATION**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS - UNAUDITED**  
**December 31, 2015**

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**Summary Financial Information and Analysis**

**Table 1**  
**Condensed Statements of Net Position**

	<b>December 31, 2015</b>	<b>December 31, 2014</b>	<b>Change</b>
Current assets	\$3,130,753	\$3,804,718	\$(673,965)
Noncurrent assets			
Restricted assets	3,994,519	4,282,060	(287,541)
Capital assets	<u>146,027</u>	<u>147,760</u>	<u>(1,733)</u>
Total assets	<u>7,271,299</u>	<u>8,234,538</u>	<u>(963,239)</u>
Current liabilities	114,830	140,181	(25,351)
Noncurrent liabilities	<u>40,123</u>	<u>46,982</u>	<u>(6,859)</u>
Total liabilities	<u>154,953</u>	<u>187,163</u>	<u>(32,210)</u>
Net position			
Invested in capital assets	146,027	147,760	(1,733)
Nonexpendable restricted	38,981	38,981	-
Expendable restricted	3,955,538	4,243,079	(287,541)
Unrestricted	<u>2,975,800</u>	<u>3,617,555</u>	<u>(641,755)</u>
Total net position	<u>\$7,116,346</u>	<u>\$8,047,375</u>	<u>\$(931,029)</u>

Net position decreased by \$931,029, as seen in Table 1. The decrease in current assets and restricted assets is due to the outflow of cash exceeding the amounts of cash received in the current year. Some of the cash expended in the current year was for ongoing projects. Revenues related to these ongoing projects were recognized in prior years when the cash was received. The decrease in capital assets relates mostly to the depreciation. The decrease in total liabilities is mostly due to the decrease in amounts due to suppliers/contractors for ongoing projects.

While the Statement of Net Position shows changes in financial position, the Statement of Revenues, Expenses, and Changes in Net Position provides answers as to the nature and source of these changes. As can be seen in Table 2, the decrease in net position of \$931,029 in the current year is the result of excess expenses over revenues.

**SANTA ANA WATERSHED ASSOCIATION**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS - UNAUDITED**  
**December 31, 2015**

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**Table 2**  
**Condensed Statement of Revenues, Expenses, and Changes in Net Position**

	<b>December 31, 2015</b>	<b>December 31, 2014</b>	<b>Change</b>
Operating revenues	\$ 910,263	\$ 1,012,834	\$ (102,571)
Operating expenses	<u>(1,789,831)</u>	<u>(2,140,066)</u>	350,235
Net operating expenses	<u>(879,568)</u>	<u>(1,127,232)</u>	247,664
Nonoperating revenues	25,986	315	25,671
Gain/(loss) on disposal of capital assets	10,405	(38,475)	48,880
Investment income/(loss)	(74,854)	196,415	(271,269)
Nonoperating expenses	<u>(12,998)</u>	<u>(43,621)</u>	30,623
Net nonoperating revenues (expenses)	<u>(51,461)</u>	<u>114,634</u>	<u>(166,095)</u>
Change in net position	(931,029)	(1,012,598)	81,569
Net position, beginning of year	<u>8,047,375</u>	<u>9,059,973</u>	<u>(1,012,598)</u>
Net position, end of year	<u>\$7,116,346</u>	<u>\$ 8,047,375</u>	<u>\$ (931,029)</u>

SAWA's operating revenues less operating expenses net to a loss of \$879,568. This operating loss is attributed to expenses incurred on projects in the current year while the corresponding revenue was recognized in a prior period as mitigation fees from developers and biological monitoring revenue. The net nonoperating loss is attributed mostly to dividends earnings of \$233,946, the unrealized loss on the investment portfolio of \$301,013 and the realized loss on the sale of investments of \$7,787.



**SANTA ANA WATERSHED ASSOCIATION  
MANAGEMENT'S DISCUSSION AND ANALYSIS - UNAUDITED  
December 31, 2015**

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**Capital Assets**

As can be seen in Table 3, as of December 31, 2015, SAWA has \$146,027 invested in capital assets (net of accumulated depreciation).

**Table 3  
Capital Assets**

	<b>December 31, 2015</b>	<b>December 31, 2014</b>	<b>Change</b>
Field equipment	\$ 94,842	\$ 101,904	\$(7,062)
Office equipment	70,891	61,940	8,951
Leasehold improvements	<u>17,281</u>	<u>17,281</u>	-
	183,014	181,125	1,889
Accumulated depreciation	(130,724)	(127,102)	(3,622)
Conservation easement	<u>93,737</u>	<u>93,737</u>	-
Net capital assets	<u>\$ 146,027</u>	<u>\$ 147,760</u>	<u>\$(1,733)</u>

The decrease of \$1,733 can be summarized as follows:

- Current year purchases amounted to \$15,810.
- Current year depreciation expense amounted to \$16,949.
- The disposal of a vehicle netted to a loss of \$594.

**Long-term Debt**

Currently SAWA has no long-term debt obligations, other than compensated absences payable. The long-term portion of compensated absences decreased by \$6,859 from the prior year. This decrease is related to vacation time use.

**SANTA ANA WATERSHED ASSOCIATION  
MANAGEMENT'S DISCUSSION AND ANALYSIS - UNAUDITED  
December 31, 2015**

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**Economic Factors and Next Year's Budget**

SAWA will be entering into the second year of a two-year \$650,000 agreement with U.S. Fish and Wildlife Service to provide Vireo Monitoring and Cowbird Trapping in the Santa Ana Watershed through December 2017. We are in negotiations to make this a longer term agreement. The Riverside County Flood Control and Water Conservation District has approved a \$135,000 contract for Tamarisk and invasive plant removal at Lake Elsinore Outlet Channel and Gunnerson Pond. Work for this project will begin January 2017.

SAWA has budgeted an additional \$155,700 in restoration projects and biological monitoring and reporting with State and local government agencies for 2017.

SAWA also has a one-year \$927,000 biological services contract with the Western Riverside Regional Conservation Authority to support the MSHCP.

Our goal for 2017 is to preserve mitigation funds in the investment pool and to not use them to support the overhead burden of running the Association. Through including an overhead charge in SAWA's billable rates, SAWA will be able to recover most of its overhead in the services performed for third parties.

**Contacting SAWA's Financial Management**

This financial report is designed to provide SAWA's contributors, member agencies, the public, and creditors with a general overview of SAWA's finances and to show SAWA's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact Hugh Wood, Executive Director, Santa Ana Watershed Association, Post Office Box 5407, Riverside, California, 92517.

## **FINANCIAL STATEMENTS**

**SANTA ANA WATERSHED ASSOCIATION**  
**STATEMENTS OF NET POSITION**  
**(With Comparative Totals)**  
**December 31, 2015 and 2014**

	<b>2015</b>	<b>2014</b>
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and investments	\$2,733,795	\$3,219,619
Accounts receivable	17,048	76
Due from governments	341,016	526,533
Dividends receivable	2,686	24,744
Herbicide inventory	15,031	11,927
Prepaid income taxes	-	1,694
Prepaid expenses	<u>21,177</u>	<u>20,125</u>
Total current assets	<u>3,130,753</u>	<u>3,804,718</u>
<b>Noncurrent assets</b>		
Restricted cash and investments	3,994,519	4,282,060
Capital assets not being depreciated	93,737	93,737
Capital assets, net of accumulated depreciation	<u>52,290</u>	<u>54,023</u>
Total noncurrent assets	<u>4,140,546</u>	<u>4,429,820</u>
Total assets	<u>7,271,299</u>	<u>8,234,538</u>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities	32,711	57,481
Accrued compensation and benefits	59,157	50,426
Compensated absences payable	17,195	20,135
Related party payable	<u>5,767</u>	<u>12,139</u>
Total current liabilities	<u>114,830</u>	<u>140,181</u>
<b>Noncurrent liabilities</b>		
Compensated absences payable	<u>40,123</u>	<u>46,982</u>
Total noncurrent liabilities	<u>40,123</u>	<u>46,982</u>
Total liabilities	<u>154,953</u>	<u>187,163</u>
<b>NET POSITION</b>		
Invested in capital assets	146,027	147,760
Nonexpendable restricted net position	38,981	38,981
Expendable restricted net position	3,955,538	4,243,079
Unrestricted	<u>2,975,800</u>	<u>3,617,555</u>
Total net position	<u>\$7,116,346</u>	<u>\$8,047,375</u>

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

**SANTA ANA WATERSHED ASSOCIATION**  
**STATEMENTS OF REVENUES, EXPENSES, AND**  
**CHANGES IN NET POSITION**  
**(With Comparative Totals)**  
**Years Ended December 31, 2015 and 2014**

	<b>2015</b>	<b>2014</b>
<b>Operating revenues</b>		
Mitigation fees	\$ 279,289	\$ 533,564
Grant income	234,960	228,519
Biological monitoring revenue	343,899	211,548
Other revenues	<u>52,115</u>	<u>39,203</u>
Total operating revenues	<u>910,263</u>	<u>1,012,834</u>
<b>Operating expenses</b>		
Personnel services	989,445	1,013,901
Project expenses	356,887	601,621
PAR project	-	76,750
Field testing and supplies	23,250	8,063
Educational supplies	5,769	1,376
Travel, mileage, and conferences	53,721	67,922
Administration and overhead	343,810	340,687
Depreciation	<u>16,949</u>	<u>29,746</u>
Total operating expenses	<u>1,789,831</u>	<u>2,140,066</u>
Operating loss	<u>(879,568)</u>	<u>(1,127,232)</u>
<b>Nonoperating revenues (expenses)</b>		
Contributions to others	(12,998)	-
Contributions received	442	315
Other income (expense)	25,544	(43,621)
Gain/(loss) on disposal of capital assets	10,405	(38,475)
Investment income/(loss)	<u>(74,854)</u>	<u>196,415</u>
Nonoperating income (loss)	<u>(51,461)</u>	<u>114,634</u>
Change in net position	(931,029)	(1,012,598)
<b>Net position</b>		
Beginning of year	<u>8,047,375</u>	<u>9,059,973</u>
End of year	<u>\$7,116,346</u>	<u>\$8,047,375</u>

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

**SANTA ANA WATERSHED ASSOCIATION**  
**STATEMENTS OF CASH FLOWS**  
(With Comparative Totals)  
Years Ended December 31, 2015 and 2014

	<b>2015</b>	<b>2014</b>
<b>Cash flows from operating activities</b>		
Cash received from customers	\$ 741,477	\$ 707,346
Cash received from grants	352,910	595,085
Cash payments to employees	(993,657)	(1,070,416)
Cash payments to suppliers for goods and services	<u>(816,486)</u>	<u>(1,228,443)</u>
Net cash used in operating activities	<u>(715,756)</u>	<u>(996,428)</u>
<b>Cash flows from capital and related financing activities</b>		
Cash paid to acquire capital assets	(15,810)	(2,010)
Cash received from sale of capital assets	<u>10,997</u>	<u>33,000</u>
Net cash provided by (used in) capital and related financing activities	<u>(4,813)</u>	<u>30,990</u>
<b>Cash flows from investing activities</b>		
Sale of investments	712,334	3,666,687
Purchase of investments	(246,116)	(627,485)
Interest and dividends received on investments	<u>256,004</u>	<u>381,041</u>
Net cash provided by investing activities	<u>722,222</u>	<u>3,420,243</u>
Net increase in cash and cash equivalents	1,653	2,454,805
<b>Cash and cash equivalents</b>		
Balance, beginning of year	<u>2,881,997</u>	<u>427,192</u>
Balance, end of year	<u>\$2,883,650</u>	<u>\$ 2,881,997</u>
<b>Reconciliation of cash and cash equivalents to the statement of net position</b>		
Cash and investments, unrestricted	\$ 2,733,795	\$ 3,219,619
Cash and investments, restricted	3,994,519	4,282,060
Less mutual funds	<u>(3,844,664)</u>	<u>(4,619,682)</u>
Total cash and cash equivalents	<u>\$ 2,883,650</u>	<u>\$ 2,881,997</u>

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

**SANTA ANA WATERSHED ASSOCIATION**  
**STATEMENTS OF CASH FLOWS**  
(With Comparative Totals)  
Years Ended December 31, 2015 and 2014

	<u>2015</u>	<u>2014</u>
<b>Reconciliation of operating loss to net cash used in operating activities</b>		
Operating loss	\$(879,568)	\$(1,127,232)
Adjustments to reconcile operating loss to net cash used in operating activities		
Depreciation	16,949	29,746
Contributions to others	(12,998)	-
Contributions received	442	315
Other income (expense)	25,544	(43,621)
Changes in operating assets and liabilities:		
Accounts receivable	(16,972)	20,509
Due from governments	185,517	268,773
Herbicide inventory	(3,104)	(11,927)
Prepaid income taxes	1,694	(1,694)
Prepaid expenses	(1,050)	440
Accounts payable and accrued liabilities	(24,770)	(106,903)
Income taxes payable	-	(1,109)
Accrued compensation and benefits	8,731	2,069
Compensated absences payable	(9,799)	(17,750)
Related party payable	(6,372)	(8,044)
Total adjustments	<u>163,812</u>	<u>130,804</u>
Net cash used in operating activities	<u>\$(715,756)</u>	<u>\$ (996,428)</u>

**Noncash capital, financing, and investing activities**

Noncash investing activities – the Organization’s net unrealized loss at December 31, 2015 totaled \$301,013.

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

**SANTA ANA WATERSHED ASSOCIATION**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**December 31, 2015**

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**NOTE 1 – REPORTING ENTITY**

The Santa Ana Watershed Association (“SAWA”) was founded in 1996 as an unincorporated association known as the Santa Ana Watershed Association of Resource Conservation Districts. SAWA incorporated as a nonprofit public benefit corporation in 2003. SAWA’s purpose is to promote a healthy Santa Ana River Watershed for wildlife and people. SAWA develops, coordinates and implements natural resource programs which support a sustainable ecosystem and social benefits from the San Bernardino Mountains to the Pacific Ocean. SAWA’s Board is comprised of appointed representatives from the following governments: Orange County Water District, Inland Empire Resource Conservation District, San Jacinto Basin Resource Conservation District, Riverside-Corona Resource Conservation District, and Elsinore Murrieta Anza Resource Conservation District.

Although legally established as a nonprofit public benefit corporation, SAWA’s Board is composed of or appointed by selected officials of government agencies. Accordingly, SAWA is subject to governmental accounting principles (as applicable to enterprise funds).

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

Fund Accounting

The accounts of SAWA are organized and operated on the basis of a fund. A fund is an independent fiscal and accounting entity with a self-balancing set of accounts. Fund accounting segregates funds according to their intended purpose and uses them to aid management in demonstrating compliance with finance-related legal and contractual provisions. SAWA’s financial statements include an enterprise fund, which is a proprietary fund type. Enterprise funds are used to account for those operations that are financed and operated in a manner similar to a private business or where the board of directors has decided that the determination of revenues earned, costs incurred and/or net income is necessary for management.

Basis of Accounting

Enterprise funds are reported using the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. SAWA follows the reporting requirements for enterprise funds, in accordance with Governmental Accounting Standards Board (GASB) Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, establishing accounting and financial reporting standards for the financial statements of state and local governments. The standard incorporates into the GASB’s authoritative literature the applicable guidance previously only found in certain Financial Accounting Standards Board (FASB) and American Institute of Certified Public Accountants (AICPA) pronouncements issued before November 30, 1989.

An enterprise fund distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with SAWA’s principal ongoing operations. The principal operating revenues of SAWA are from mitigations, in-lieu mitigation fees, and biological monitoring services associated with the Santa Ana River Watershed. The principal operating expenses of SAWA are for invasive weed removal projects, specifically the removal of *Arundo Donax*, also known as giant reed or giant cane, from the Santa Ana River Watershed.



**SANTA ANA WATERSHED ASSOCIATION**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**December 31, 2015**

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**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

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

Use of Estimates

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

Comparative Data

Prior year data has been included where practical for comparison purposes only. The prior year data does not represent a complete presentation in accordance with accounting principles generally accepted in the United States of America. Certain minor reclassifications of prior year data have been made in order to enhance their comparability with current year figures.

Cash and Cash Equivalents

For purposes of the statement of cash flows, SAWA considers cash and cash equivalents to be cash on hand, demand deposits, and money market funds from which funds can be effectively deposited or withdrawn at any time without prior notice or penalty.

Investments

Investments are reported in the accompanying statement of net position at fair value. Changes in fair value that occur during a fiscal year are recognized as investment income reported for that fiscal year. Investment income includes interest earnings, changes in fair value, and any gains or losses realized upon the liquidation, maturity or sale of investments.

Receivables

SAWA considers receivables to be fully collectible at period end. Accordingly, accounts receivable are not shown net of an allowance for uncollectible accounts based on management's estimate. Actual collected amounts could differ.

Inventory

Inventory consists of herbicides carried at the lower of cost or market, and cost is determined on the first-in, first-out (FIFO) method.

Capital Assets

Capital assets are recorded at cost. Donated capital assets are recorded at fair value on the date of donation plus any ancillary costs. SAWA's policy is to capitalize all property having a value of \$500 or more and a life expectancy of one year or more. Depreciation has been provided for using the straight-line method over estimated useful lives of the related assets. Useful lives for depreciation purposes range from 2 to 10 years depending on the asset being capitalized.

**SANTA ANA WATERSHED ASSOCIATION**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**December 31, 2015**

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**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Compensated Absences

Employees gain a vested right to accumulated unpaid vacation based on years of service but cannot accumulate more than 200 hours of accrued vacation. Employee vacation benefits are recognized as a liability of SAWA. For leased employees, an offsetting receivable is recorded to recognize the leasing agency's obligation to reimburse SAWA for this expense. This amount is included in due from governments on the statement of net position.

Income Taxes

SAWA is a charitable not-for-profit organization and is exempt from federal income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code and Code Section 23701(d) of the California Revenue and Taxation Code. It is no longer subject to United States of America federal or state examinations by tax authorities for the years before 2011 and 2010, respectively.

SAWA evaluated its tax positions and the certainty as to whether those positions will be sustained in the event of an audit by taxing authorities at the federal and state levels. The primary tax positions evaluated are related to its continued qualification as a tax-exempt organization and whether there are unrelated business income activities conducted that would be taxable. Management has determined that all income tax positions are more likely than not of being sustained upon potential audit or examination; therefore, no disclosures of uncertain income tax positions are required.

During the year ended December 31, 2015, SAWA did not recognize any interest or penalties associated with any tax positions.

Revenues (operating and nonoperating)

SAWA receives mitigation fees and in-lieu mitigation fees from developers for SAWA's programs to maintain a healthy Santa Ana River Watershed. Mitigation and in-lieu fee revenues are considered operating revenues. Revenues received from investment earnings and contributions are considered nonoperating revenue.

Implementation of New Pronouncements

In February 2015, the GASB issued Statement No. 72, *Fair Value Measurement and Application*. This statement is intended to improve accounting and financial reporting for state and local governments' investments by enhancing the comparability of financial statements among governments by requiring measurement of certain assets and liabilities at fair value using a consistent and more detailed definition of fair value and accepted valuation techniques. It also requires measurement at acquisition value for donated capital assets, which were previously required to be measured at fair value. The requirements of this statement are effective for financial statements for reporting periods beginning after June 15, 2015. SAWA is in the process of determining the potential impact of this statement on its financial statements.

**SANTA ANA WATERSHED ASSOCIATION**  
**NOTES TO THE FINANCIAL STATEMENTS**  
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**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

In June 2015, GASB issued Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments* (GASB 76). This statement identifies the hierarchy of GAAP used to prepare financial statements of state and local governmental entities. This statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. GASB 76 supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The requirements of this statement are effective for financial statements for reporting periods beginning after June 15, 2015, and should be applied retroactively. SAWA is in the process of determining the potential impact of this statement on its financial statements.

**NOTE 3 – CASH AND INVESTMENTS**

Cash and investments as of December 31, 2015 are classified in the accompanying financial statements as follows:

Statement of net position	
Cash and investments	\$2,733,795
Cash and investments – restricted	<u>3,994,519</u>
Total cash and investments	<u>\$6,728,314</u>

Cash and investments as of December 31, 2015 consist of the following:

Deposits with financial institutions	\$ 168,043
Insured savings account	2,715,609
Mutual funds invested into debt securities	1,710,579
Mutual funds invested into equity securities	1,668,098
Mutual funds invested into alternative securities	<u>465,985</u>
Total cash and investments	<u>\$6,728,314</u>

At December 31, 2015 cash and investments were restricted for the following purposes:

Riparian/wetland habitat along San Timoteo Creek	\$1,239,929
In-lieu fee mitigation program	2,715,609
Mockingbird II Conservation Easement Endowment Fund	<u>38,981</u>
Total restricted cash and investments	<u>\$3,994,519</u>

In order to obtain economies of scale, SAWA manages its investments on a commingled basis. SAWA maintains the necessary sub-accounting of all commingled funds, dividing the portfolio into short-term investments for operating needs and long-term investments as determined by the Board, with consultation from staff. The portfolio of SAWA is diversified using the tenets of modern portfolio theory. The basic approach to optimize risk return utilizes a globally diverse portfolio made up of low correlating assets along with the discipline of regular rebalancing.

**SANTA ANA WATERSHED ASSOCIATION**  
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**NOTE 3 – CASH AND INVESTMENTS (Continued)**

Investments Authorized by SAWA’s Investment Policy

The portfolio is managed in a balanced manner to the Income and Growth asset allocation (45 percent equities, 45 percent fixed income, and 10 percent cash) as economic conditions subject to board approval. Deviation of these allocations can be in a range of within 10 percent +/- depending on the operating needs of SAWA. Investments in any one security may not exceed 10 percent of the portfolio, unless in an exchange traded fund (ETF) or mutual fund. No investments may be made on margin. In addition, no short sales, noninvestment grade securities, futures contracts or leverage are permitted unless held in an ETF or actively managed fund. The investments in these strategies are for risk management and not for speculation.

Disclosures Relating to Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that SAWA manages its exposure to interest rate risks is by investing in mutual funds which can be accessed at any time to provide the cash flow and liquidity needed for operations.

**Disclosures Relating to Credit Risk**

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the minimum rating required by (where applicable) SAWA’s investment policy, and the actual rating as of year-end for each investment type.

Investment Type	Minimum Rating	Standard & Poor Ratings as of Year-end			Not Rated
		AAAm	AAA	aa+	
Mutual funds - debt	\$1,710,579 N/A	-	-	-	\$1,710,579
Total	\$1,710,579	\$ -	\$ -	\$ -	\$1,710,579

**Concentration of Credit Risk**

SAWA’s investment policy states that an investment in any one security may not exceed 10 percent of the entire portfolio. There were no investments in any one issuer (other than mutual funds) that represent 10 percent or more of SAWA’s total portfolio. United States of America generally accepted accounting principles also require disclosure in the notes to the financial statements of any investment in an issuer (other than U.S. Treasury securities and mutual funds) that represents 5 percent or more of SAWA’s total investments. As of December 31, 2015, there were no such concentrations.

**SANTA ANA WATERSHED ASSOCIATION**  
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**NOTE 3 – CASH AND INVESTMENTS (Continued)**

**Custodial Credit Risk**

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, an entity will not be able to recover its deposits. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, an entity will not be able to recover the value of its investment. SAWA's investment policy does not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments.

SAWA maintains its cash and investments at one financial institution. The balance at this financial institution is insured by the Securities Investor Protection Corporation (SIPC) up to \$500,000 per client for securities, inclusive of up to \$250,000 per client for cash. This financial institution has obtained private insurance coverage from a Lloyd's of London syndicate to provide additional protection for very large client accounts. For clients who have received the full SIPC limits, further protection, including up to \$1.9 million for cash, is provided by this policy, subject to an aggregate loss limit of \$1 billion for all customer claims. At December 31, 2015, SAWA's investments held at the financial institution exceeded the SIPC limit by \$3,344,662, which would be protected under the Lloyd's of London syndicate policy subject to its aggregate limit. Additionally, SAWA holds funds, which are insured by the Federal Deposit Insurance Corporation, in an Insured Savings Account through this financial institution. SAWA has no uninsured cash balances at December 31, 2015.

**NOTE 4 – RISK MANAGEMENT**

SAWA purchases various insurances through Nonprofit's Insurance Alliance of California (NIAC). The following table presents the coverages along with the applicable limits:

Type of Insurance	Each Occurrence Limit	Aggregate Limit
Commercial liability	\$1,000,000	\$2,000,000
Automobile liability	\$1,000,000	N/A
Umbrella liability	\$1,000,000	\$1,000,000
Professional liability	\$1,000,000	\$2,000,000

SAWA purchases commercial workers' compensation insurance from the State Compensation Insurance Fund (State Fund). Under this policy, State Fund provides workers' compensation coverage of up to \$1,000,000 per claim.

During the year ended December 31, 2015, SAWA had no settlements exceeding insurance coverage for these categories of risk. For the past three years, settlement or judgment amounts have not exceeded insurance coverage.

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**NOTE 5 – CAPITAL ASSETS**

The following is a summary of changes in capital assets for SAWA at December 31, 2015:

	Balance Beginning of Year	Additions	Deletions	Balance End of Year
Capital assets being depreciated:				
Field equipment	\$ 101,904	\$ 6,859	\$(13,921)	\$ 94,842
Office equipment	61,940	8,951	-	70,891
Leasehold improvements	17,281	-	-	17,281
	<u>181,125</u>	<u>15,810</u>	<u>(13,921)</u>	<u>183,014</u>
Less accumulated depreciation for:				
Field equipment	(57,720)	(12,384)	13,327	(56,777)
Office equipment	(52,101)	(4,565)	-	(56,666)
Leasehold improvements	(17,281)	-	-	(17,281)
	<u>(127,102)</u>	<u>(16,949)</u>	<u>13,327</u>	<u>(130,724)</u>
Net assets being depreciated	<u>54,023</u>	<u>(1,139)</u>	<u>(594)</u>	<u>52,290</u>
Capital assets not depreciated:				
Conservation easement	<u>93,737</u>	-	-	<u>93,737</u>
Net assets not being depreciated	<u>93,737</u>	-	-	<u>93,737</u>
Total capital assets, net	<u>\$ 147,760</u>	<u>\$ (1,139)</u>	<u>\$ (594)</u>	<u>\$ 146,027</u>

Depreciation expense was \$16,949 for the year ended December 31, 2015.

**NOTE 6 – DEFINED CONTRIBUTION PENSION PLAN**

SAWA provides pension benefits for all of its permanent employees through a 403(b) defined contribution plan administered by Lincoln Financial Services. The plan was adopted in July 2004 by the Board of Directors. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings. Employees are required to participate after achieving permanent status. SAWA contributes 6 percent of each eligible employee's compensation up to a maximum annual compensation allowed by law. The plan is a standardized plan which can be amended due to changes in law or by the Board of Directors. Employees voluntarily contribute to the plan. Employee contributions are limited to the maximum allowed by law. SAWA's contributions for each employee and the related allocated investment earnings vest in accordance to the plan document. Employees are fully vested after three years of participation. The employees are vested immediately in their contributions and any related allocated investment earnings. During the fiscal year ended December 31, 2015, SAWA contributed \$87,143 to the plan while SAWA employees contributed \$112,179 to the plan inclusive of amounts reimbursed and withheld for leased employees.

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**NOTE 7 – ADMINISTRATIVE OFFICE LEASE**

In August 2011, SAWA entered into a two-year lease for administrative office space. Under the term of the agreement, SAWA is to pay monthly \$1,808 for the use of the office space plus custodial services. The utilities are invoiced quarterly by the lessor and are a percentage of the actual costs for electrical service, natural gas and refuse collection. If SAWA elects to terminate the lease early, it must pay fifty percent (50 percent) of the total rent due for the balance of the lease term or all rent payable from the date of early termination until a replacement tenant is found. The lease was extended in August 2013 for an additional two years and extended again in June 2015 until July 30, 2016. After July 2016, SAWA continued to rent these facilities on a month-to-month basis until October 2015 (see Note 14). Under the extended terms, rent decreased to \$1,733 per month plus janitorial supplies. For the year ended December 31, 2015, SAWA incurred \$29,168 in costs under the lease agreement.

The following is a schedule of minimum lease payments due excluding utilities and janitorial supplies:

Year ended December 31	Amount
2016	\$ <u>12,128</u>
Total	\$ <u>12,128</u>

**NOTE 8 – RELATED PARTY TRANSACTIONS**

As described in Note 1, SAWA's board is comprised of representatives from Orange County Water District (OCWD), Inland Empire Resource Conservation District (IERCD), San Jacinto Basin Resource Conservation District (SJBRC), Riverside-Corona Resource Conservation District (RCRCD), and Elsinore Murrieta Anza Resource Conservation District (EMARCD). The following related party assets (liabilities) are included in the statement of net position for the year ended December 31, 2015:

	<u>OCWD</u>	<u>IERCD</u>	<u>SJBRC</u>	<u>RCRCD</u>	<u>EMARCD</u>	<u>Total</u>
Due from governments	\$71,044	\$37,812	\$5,608	\$ -	\$10,662	\$125,126
Related party payable	-	(5,767)	-	-	-	(5,767)
	<u>\$71,044</u>	<u>\$32,045</u>	<u>\$5,608</u>	<u>\$ -</u>	<u>\$10,662</u>	<u>\$119,359</u>

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**NOTE 8 – RELATED PARTY TRANSACTIONS (Continued)**

The following related party revenues (expenses) are included in the statement of revenues, expenses, and changes in net position for the year ended December 31, 2015:

	OCWD	IERCD	SJBRC	RCRCD	EMARCD	Total
Mitigation fees	\$ -	\$ -	\$ 34,643	\$ -	\$ -	\$ 34,643
Biological monitoring revenue	166,962	155,273	-	-	10,662	332,897
Other revenues	28,963	-	-	-	-	28,963
Project expenses	(87,783)	(99,744)	-	(12,826)	-	(200,353)
Other expenses	(362)	(6,107)	(22,558)	(16,571)	(22,250)	(67,848)
	<u>\$107,780</u>	<u>\$ 49,422</u>	<u>\$ 12,085</u>	<u>\$(29,397)</u>	<u>\$(11,588)</u>	<u>\$128,302</u>

**NOTE 9 – EXPENDABLE RESTRICTED FUNDS**

*Riparian/Wetland Habitat along San Timoteo Creek*

In October 2004, SAWA received \$1,620,000 from the United States Army Corps of Engineers to be used for riparian and wetland habitat restoration along San Timoteo Creek. These funds are restricted for program use. As of December 31, 2015, \$1,239,929 was reflected on the financial statement as part of restricted cash and investments and as a component of expendable restricted net position.

*In-lieu Fee Mitigation Program*

The United States Army Corps of Engineers has required SAWA to establish a separate restricted cash account that is FDIC insured to hold in-lieu fee mitigation monies received but not placed as of June 30, 2013. This account was established in April 2014 and \$2,715,000 was transferred to the account. At December 31, 2015, \$2,715,609 was reflected on the financial statement as part of restricted cash and investments and as a component of expendable restricted net position.

**NOTE 10 – NONEXPENDABLE RESTRICTED FUNDS**

*Mockingbird II Conservation Easement and Endowment Fund*

The Mockingbird II Conservation Easement Endowment Fund was established in November 2009 when Mockingbird II Conservation Easement and the related endowment fund were transferred to SAWA from The Environmental Trust. The conservation easement is reflected as a capital asset at its estimated fair value plus ancillary costs, totaling \$93,737.



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**NOTE 10 – NONEXPENDABLE RESTRICTED FUNDS (Continued)**

The endowment fund received a total of \$38,981 and is required to be held in perpetuity with only the investment earnings available for use in the maintenance of the conservation easement. This fund is reflected on the statement of net position in restricted cash and investments as a component of nonexpendable restricted net position.

**NOTE 11 – ANTICIPATED CHANGES TO NET POSITION**

*Restricted Balance Clarification Agreement with Orange County Water District*

SAWA and Orange County Water District (“OCWD”), a related party, entered into an agreement on August 8, 2013. Terms of this agreement required an Agreed-Upon Procedures (AUP) engagement to be performed to determine the amount of money SAWA holds that is attributable to OCWD’s projects and contributions. Any remaining OCWD funds held by SAWA would be considered held in trust and would represent restricted balances. The amount of the trust funds resulting from trust fund activities and investment earnings over the period July 1997 through the date of these financial statements is unknown, as the AUP engagement is incomplete as of the date of these financial statements. Work on this engagement is ongoing. As a result, no related cash or net position restrictions are included in SAWA’s financial statements as of December 31, 2015.

*Administrative Cost Reallocation*

SAWA has identified that administrative costs were not properly allocated in the past for the Reach 3B project and is currently negotiating to reallocate prior costs. The effect of these potential reallocations on unrestricted and expendable restricted net position has not been determined.

*In-lieu Fee Mitigation Requirements*

SAWA has also identified that in-lieu fee mitigation requirements may have been satisfied to a greater extent than originally reported. This would result in a reduction in expendable restriction net position for these funds, with an offsetting increase in unrestricted net position, or other expendable restricted funds, or both. Research to determine the extent of the reclassification has not been completed, and changes to net position could not be estimated at this time.

Due to the unresolved nature of the these issues, potential changes to unrestricted and restricted balances were considered by management to be un-estimable as of January 25, 2017, the date these financial statements were available to be issued.

**NOTE 12 - CONCENTRATION**

A significant portion of SAWA’s operating revenue came from four government agencies which represent 84 percent of all operating revenue for the year ended December 31, 2015. As of December 31, 2015, 32 percent of accounts receivable was due from two of these agencies. An additional 48 percent of accounts receivable was due from a fifth government agency, to whom SAWA leases biological staff.

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**NOTE 13 – RISKS AND UNCERTAINTIES**

SAWA invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term. The volatility of the market and credit institutions after December 31, 2015 could have a significant, negative effect on SAWA's investments.

**NOTE 14 – SUBSEQUENT EVENTS**

In September 2016, SAWA entered into a ten-year lease for office space. This agreement is noncancellable for the first five years and cancellable with twelve months written notice thereafter. Monthly rent under this agreement is \$5,652 with a 2.5 percent annual increase for the first five years and a 3.5 percent annual increase thereafter. Payment of SAWA's share of operating expenses is also required. The following is a schedule of minimum payments over the next five years excluding operating expenses:

Year ended December 31	Amount
2016	\$ 16,957
2017	68,253
2018	69,960
2019	71,709
2020	73,501
Thereafter	<u>56,153</u>
Total	<u>\$356,533</u>

In November 2016, SAWA entered into a five-year noncancellable lease for warehouse space. Monthly rent, common area maintenance and parking fees under this agreement total \$1,314 with a 3.0 percent annual increase of rent and common area maintenance. The following is a schedule of minimum payments over the next five years:

Year ended December 31	Amount
2016	\$ 2,014
2017	15,801
2018	16,257
2019	16,727
2020	17,211
Thereafter	<u>16,194</u>
Total	<u>\$84,204</u>

In the preparation of these financial statements, SAWA considered subsequent events through January 25, 2017 which is the date these financial statements were issued.