SEWER AUTHORITY MID-COASTSIDE

FINANCIAL STATEMENTS
AND INDEPENDENT AUDITOR'S REPORT

FOR THE YEARS ENDED
JUNE 30, 2012 AND 2011

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SEWER AUTHORITY MID-COASTSIDE

FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT FOR THE FISCAL YEARS ENDED JUNE 30, 2012 AND 2011

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C. G. UHLENBERG LLP
CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of the
Sewer Authority Mid-Coastside

Half Moon Bay, California

We have audited the accompanying basic financial statements of the Sewer Authority Mid-Coastside (the "Authority") as of and for the years ended June 30, 2012 and 2011, as listed in the table of contents. These financial statements are the responsibility the Authority's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Authority, as of June 30, 2012 and 2011, and the respective changes in financial position, and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 26, 2012, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 9 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the

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United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

C. G. Uhlenberg LLP

September 26, 2012
Redwood City, California

MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited)

This section of Sewer Authority Mid-Coastside's (Authority) Comprehensive Annual Financial Report presents our analysis of the Authority's financial performance during the Fiscal Years ended on June 30, 2012 and 2011. Please read it in conjunction with the financial statements, which are presented on pages 10 through 12.

FINANCIAL HIGHLIGHTS

- The Authority's net assets at June 30, 2012 decreased by $1,078,837 (5.6%) as compared to a decrease of $1,153,073 (5.7%) at June 30, 2011.
- During Fiscal Year 2012, the Authority's operating revenues increased by $93,086 (2.4%) and expenses decreased by $87,457 (1.6%). The corresponding changes in Fiscal Year 2011 were decreased operating revenues of $96,286 (2.4%) and decreased expenses of $129,726 (2.3%).

BASIC FINANCIAL STATEMENTS

The financial statements of the Authority report information about the Authority using accounting methods similar to those used by private sector companies. These statements offer short-term and long-term financial information about its activities. The Statement of Net Assets includes all of the Authority's assets and liabilities, and provides information about the nature and amounts of investments in resources (assets) and the obligations to the Authority's creditors (liabilities). It also provides the basis for evaluating the capital structure of the Authority, and assessing the liquidity and financial flexibility of the Authority.

All of the current year's revenues and expenses are accounted for in the Statement of Revenues, Expenses, and Changes in Net Assets. This statement measures the success of the Authority's operations over the past year and can be used to determine the Authority's credit worthiness and whether the Authority has successfully recovered all its costs through its user fees and other charges.

The final required financial statement is the Statement of Cash Flows. The primary purpose of this statement is to provide information about the Authority's cash receipts and cash payments during the reporting period. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations and investments. It also provides answers to such questions as: "Where did cash come from?", "What was cash used for?", and "What was the change in cash balance during the reporting period?"

FINANCIAL ANALYSIS OF THE AUTHORITY

Our analysis of the Authority begins on page 4 of the Management's Discussion and Analysis. One of the most important questions asked about the Authority's finances is: "Is the Authority, as a whole, better off or worse off as a result of the year's activities?" The Statement of Net Assets and the Statement of Revenues, Expenses, and Changes in Net Assets report information about the Authority's activities in a way that will help answer this question. These two statements report the net assets of the Authority and changes in them. You can think of the Authority's net assets (the difference between assets and liabilities) as one way to measure financial health or financial position. Over time, increases or decreases in the Authority's net assets are one indicator of whether its financial health is improving or deteriorating. However, you will need to consider other non-financial factors, such as changes in economic conditions, population growth, zoning, and new or changed government legislation.

NET ASSETS

To begin our analysis, a summary of the Authority's Statements of Net Assets is presented in Tables 1 and 1.1.

Table 1
Condensed Statements of Net Assets (In thousands of dollars)

	FY 2012	FY 2011	Variance	Total Percent Change
Capital Assets	$ 13,210	$ 14,453	$ (1,243)	-8.6%
Other Assets	5,519	5,174	345	6.7%
Total Assets	18,729	19,627	(898)	-4.6%
Current Liabilities	516	371	145	39.1%
Noncurrent Liabilities	139	103	36	35.0%
Total Liabilities	655	474	181	38.2%
Net Assets:				
Investment in Capital Assets	13,210	14,453	(1,243)	-8.6%
Restricted for Capital Projects	3,581	3,410	171	5.0%
Unrestricted	1,283	1,290	(7)	-0.5%
Total Net Assets	$ 18,074	$ 19,153	$ (1,079)	-5.6%

Table 1.1
Condensed Statements of Net Assets (In thousands of dollars)

	FY 2011	FY 2010	Variance	Total Percent Change
Capital Assets	$ 14,453	$ 15,773	$ (1,320)	-8.4%
Other Assets	5,174	4,939	235	4.8%
Total Assets	19,627	20,712	(1,085)	-5.2%
Current Liabilities	371	359	12	3.3%
Noncurrent Liabilities	103	47	56	0.0%
Total Liabilities	474	406	68	16.7%
Net Assets:				
Investment in Capital Assets	14,453	15,773	(1,320)	-8.4%
Restricted for Capital Projects	3,410	3,155	255	8.1%
Unrestricted	1,290	1,378	(88)	-6.4%
Total Net Assets	$ 19,153	$ 20,306	$ (1,153)	-5.7%

As can be seen from the tables above, net assets at June 30, 2012 and 2011 decreased by $1,078,837 and $1,153,073, respectively, from its immediately preceding year. This decrease is the result of the following:

• Investment in Capital Assets decreased by $1,242,740 and $1,320,182 in Fiscal Year 2012 and 2011, respectively, mainly due to the annual depreciation expenses
• Restricted Net Assets at June 30, 2012 and 2011 increased by $171,031 and $254,788, respectively, due to capital contributions less project expenditures.
• Unrestricted Net Assets (those that can be used to finance day-to-day operations) decreased by $7,128 in Fiscal Year 2012 and decreased by $87,679 in 2011. The decrease in 2012 and 2011 was due to receiving less revenue when compared to expenses.

REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

While the Statement of Net Assets shows the change in financial position of net assets, the Statement of Revenues, Expenses, and Changes in Net Assets provides answers as to the nature and source of these changes. As can be seen in Tables 2 and 2.1, the loss of $1,078,837 is the source of the decrease in net assets in Fiscal Year 2012. The decrease in net assets in Fiscal Year 2011 is due to the loss of $1,153,073.

Table 2
Condensed Statements of Revenues, Expenses and Changes in Net Assets
(In thousands of dollars)

	FY 2012	FY 2011	Variance	Total Percent Change
Operation & maintenance	$ 2,841	$ 2,732	$ 109	4.0%
Collection assessments	810	779	31	4.0%
Service fees	237	317	(80)	-25.2%
Other income	41	8	33	412.5%
Operating Revenue	3,929	3,836	93	2.4%
Depreciation expense	1,651	1,665	(14)	-0.8%
Treatment	1,831	1,925	(94)	-4.9%
Collection system	815	766	49	6.4%
Industrial waste	32	31	1	3.2%
Administration	1,072	1,101	(29)	-2.6%
Total Expenses	5,401	5,488	(87)	-1.6%
Net non-operating revenue	41	49	(8)	-16.3%
Capital contributions	352	520	(168)	-32.3%
Capital distributions	-	(70)	70	-100.0%
Change in Net Assets	(1,079)	(1,153)	74	-6.4%
Beginning Net Assets	19,153	20,306	(1,153)	-5.7%
Ending Net Assets	$ 18,074	$ 19,153	$ (1,079)	-5.6%

Table 2.1
Condensed Statements of Revenues, Expenses and Changes in Net Assets
(In thousands of dollars)

	FY 2011	FY 2010	Variance	Total Percent Change
Operation & maintenance	$ 2,732	$ 2,852	$ (120)	-4.2%
Collection assessments	779	784	(5)	-0.6%
Service fees	317	258	59	22.9%
Grant revenue	-	37	(37)	-100.0%
Other income	8	1	7	700.0%
Operating Revenue	3,836	3,932	(96)	-2.4%
Depreciation expense	1,665	1,689	(24)	-1.4%
Treatment	1,925	1,937	(12)	-0.6%
Collection system	766	797	(31)	-3.9%
Industrial waste	31	18	13	72.2%
Administration	1,101	1,177	(76)	-6.5%
Total Expenses	5,488	5,618	(130)	-2.3%
Net non-operating revenue	49	18	31	172.2%
Capital contributions	520	1,151	(631)	-54.8%
Capital distributions	(70)	-	(70)	-
Change in Net Assets	(1,153)	(517)	(636)	123.0%
Beginning Net Assets	20,306	21,011	(705)	-3.4%
Prior period adjustment	-	(188)	188	-100.0%
Net Assets - Restated Beginning	20,306	20,823	(517)	-2.5%
Ending Net Assets	$ 19,153	$ 20,306	$ (1,153)	-5.7%

A closer examination of the source of changes in net assets reveals that the Authority's operating revenues increased by $93,086 in Fiscal Year 2012 due to higher operation & maintenance assessments and collection assessments as compared to a decrease of $96,286 in Fiscal Year 2011. Non-operating revenues increased by $31,256 in Fiscal Year 2012 due to not having a loss on the disposal of fixed assets. Non-operating revenue increased by $31,256 in Fiscal Year 2011 due to not having a loss on the disposal of fixed assets.

Total expenses in Fiscal Year 2012 decreased by $87,457 and decreased in 2011 by $129,726, respectively, due mainly to a combination of the following:

• An increase in collection system expenses of $48,596 in Fiscal Year 2012, and a decrease of $30,605 in Fiscal Year 2011, due primarily to increased payroll costs and vehicle expense in 2012, and decreased payroll costs and professional fees in 2011.
• A decrease in administration expenses of $28,707 in Fiscal Year 2012, and a decrease of $75,987 in Fiscal Year 2011, due primarily to decreased legal services and temporary employee fees in 2012, and due to an increase in payroll costs, temporary employee, and engineering fees in 2011.
• A decrease in treatment expenses of $93,255 in Fiscal Year 2012, and a decrease of $12,766 in Fiscal Year 2011, due primarily to decreased utility, pump station, and plant equipment expenses in 2012, and due to decreased payroll costs in 2011.
• A decrease in depreciation expenses of $15,053 in 2012 and a decrease in depreciation expenses of $23,428 in 2011.

CAPITAL ASSETS

At the end of Fiscal Year 2012, the Authority had invested approximately $13.2 million in capital assets as shown in Table 3.

Table 3
Capital Assets (In thousands of dollars)

	FY 2012	FY 2011	Variance	Total Percent Change
Non-depreciable Assets	$ 1,003	$ 1,001	$ 2	0.2%
Depreciable Assets	42,111	41,706	405	1.0%
Subtotal	43,114	42,707	407	1.0%
Less Accumulated Depreciation	(29,904)	(28,254)	(1,650)	5.8%
Net Capital Assets	$ 13,210	$ 14,453	$ (1,243)	-8.6%

Table 3.1
Capital Assets (In thousands of dollars)

	FY 2011	FY 2010	Variance	Total Percent Change
Non-depreciable Assets	$ 1,001	$ 944	$ 57	6.0%
Depreciable Assets	41,706	41,463	243	0.6%
Subtotal	42,707	42,407	300	0.7%
Less Accumulated Depreciation	(28,254)	(26,634)	(1,620)	6.1%
Net Capital Assets	$ 14,453	$ 15,773	$ (1,320)	-8.4%

More information about the Authority's capital assets is presented in the Notes to the Financial Statements on page 20.

ECONOMIC FACTORS AND NEXT YEAR'S OUTLOOK

The Authority's Board of Directors and management considered many factors when setting the Fiscal Year 2013 budget and user rate charges. The approved Fiscal Year 2013 budget is driven by the "services" provided to the three member agencies - the City of Half Moon Bay, the Montara Water and Sanitary District and the Granada Sanitary District - within our service area. It also reflects the commitment to providing, maintaining and operating a facility for the collection, transmission, treatment and disposal of wastewater for the benefit of inhabitants in these service areas at rates that are stable and reasonable.

The Authority's revenues are from three major sources: 1) operational and maintenance assessments, 2) collections assessments, and 3) service fees.

Operating revenues available for recovering operating costs are projected to be $4.00 million, an increase of $120,000 due to higher assessments and fees in Fiscal Year 2013.

Operating expenses are expected to increase by $68,000 due to the increase in treatment, administration and collection expenses.

These indicators were taken into consideration when adopting the Authority's budget for Fiscal Year 2013.

CONTACTING THE AUTHORITY

This financial report is designed to provide our citizens, customers, investors, and creditors with a general overview of the Authority's finances and to demonstrate the Authority's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Sewer Authority Mid-Coastside at 1000 N. Cabrillo Highway, Half Moon Bay, CA 94019 or call (650) 726-0124.

SEWER AUTHORITY MID-COASTSIDE
STATEMENTS OF NET ASSETS
JUNE 30, 2012 AND 2011

	2012	2011
Assets		
Current Assets		
Cash and investment	$ 5,296,156	$ 5,035,590
Accounts and interest receivable	198,270	90,968
Prepaids and other assets	24,496	47,701
Total Current Assets	5,518,922	5,174,259
Noncurrent Assets		
Nondepreciable capital assets	1,003,515	1,000,498
Depreciable capital assets, net	12,206,768	13,452,525
Total Noncurrent Assets	13,210,283	14,453,023
Total Assets	$ 18,729,205	$ 19,627,282
Liabilities		
Current Liabilities		
Accounts payable and accrued liabilities	$ 229,047	$ 151,899
Due to member agencies	179,650	111,100
Accrued payroll liability	30,197	32,905
Compensated absences - current	77,139	75,481
Total Current Liabilities	516,033	371,385
Noncurrent Liabilities		
Compensated absences - noncurrent	52,593	44,536
Post employment benefits	86,469	58,414
Total Noncurrent Liabilities	139,062	102,950
Total Liabilities	$ 655,095	$ 474,335
Net Assets		
Invested in capital assets	$ 13,210,283	$ 14,453,023
Restricted for capital projects	3,581,097	3,410,066
Unrestricted	1,282,730	1,289,858
Total Net Assets	$ 18,074,110	$ 19,152,947

The notes to the financial statements are an integral part of this statement

SEWER AUTHORITY MID-COASTSIDE
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2012 AND 2011

	2012	2011
Operating Revenues		
Operation and maintenance assessments	$ 2,840,997	$ 2,731,498
Collection assessments	810,029	779,100
Service fees	237,170	316,940
Other income	41,047	8,619
Total Operating Revenues	3,929,243	3,836,157
Operating Expenses		
Treatment	1,831,550	1,924,805
Collection system	814,710	766,114
Industrial waste	31,979	31,017
Administration	1,072,080	1,100,787
Depreciation	1,650,707	1,665,760
Total Operating Expenses	5,401,026	5,488,483
Operating Loss	(1,471,783)	(1,652,326)
Nonoperating Income (Expenses):		
Interest and dividend income	40,678	49,307
Total Nonoperating Income	40,678	49,307
Loss Before Capital Contributions	(1,431,105)	(1,603,019)
Capital Contributions	352,268	519,996
Capital Distributions	-	(70,050)
Changes in Net Assets	(1,078,837)	(1,153,073)
Net Assets - Beginning	19,152,947	20,306,020
Net Assets - Ending	$ 18,074,110	$ 19,152,947

The notes to the financial statements are an integral part of this statement

SEWER AUTHORITY MID-COASTSIDE
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2012 AND 2011

	2012	2011
Cash Flows from Operating Activities		
Receipts from users	$ 3,890,491	$ 3,941,695
Payments to suppliers for goods and services	(1,740,768)	(2,056,141)
Payments to employees	(1,874,136)	(1,816,932)
Net Cash Provided (Used) by Operating Activities	275,587	68,622
Cash Flows from Capital and Related Financing Activities:		
Acquisition of capital assets	(407,967)	(345,578)
Capital assessments received	352,268	519,996
Net Cash Provided by Capital and Related Financing Activities	(55,699)	174,418
Cash Flows from Investing Activities:		
Investment income received	40,678	49,405
Net Change in Cash and Cash Equivalents	260,566	292,445
Cash and Cash Equivalents - Beginning	5,035,590	4,743,145
Cash and Cash Equivalents - Ending	$ 5,296,156	$ 5,035,590
Reconciliation of Operating Loss to		
Net Cash Provided by Operating Activities		
Operating loss	$ (1,471,783)	$ (1,652,326)
Adjustments to reconcile operating loss to		
net cash provided by operating activities		
Depreciation	1,650,707	1,665,760
(Increase) in accounts receivable	(107,302)	64,488
(Increase) decrease in prepaids and other assets	23,205	(7,431)
Increase (decrease) in accounts payable and accruals liabilities	77,148	(46,779)
Increase in due to member agencies	68,550	41,050
Increase in accrued payroll liabilities	(2,708)	(31,306)
Increase (decrease) in compensated absences	9,715	5,959
Increase in post employment benefits	28,055	29,207
Net Cash Provided (Used) by Operating Activities	$ 275,587	$ 68,622
Supplemental disclosure of noncash Capital and Related Financing Activities:		
Capital Contribution increase (decrease) due to changes in		
due to member agencies	$ -	$ (70,050)

The notes to the financial statements are an integral part of this statement

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Description of the Organization

Sewer Authority Mid-Coastside (the Authority) is a public entity created on February 3, 1976 by a Joint Exercise of Powers Agreement between the City of Half Moon Bay, the Montara Water and Sanitary District and the Granada Sanitary District (collectively the "Member Agencies"). The Authority was formed pursuant to the provisions of Title 1, Division 7, and Chapter 5 of the California Government Code. Under this agreement, the Authority has the power to construct, maintain and operate facilities for the collection, transmission, treatment and disposal of wastewater for the benefit of the land and its inhabitants within member agencies' respective boundaries. Authority revenue is mainly derived from assessments for operations, maintenance and collections made on the member agencies.

B. Description of the Financial Reporting Entity

In evaluating how to define the government for financial reporting purposes, management has considered all potential component units. Criteria used in evaluating the inclusion of a potential component unit includes, but is not limited to, financial interdependency, oversight responsibility, ability to significantly influence operations, scope of public service, and the existence of special financing relationships. Based upon the application of these criteria, no potential component units were identified that would be required to be included in the financial statements of the Authority.

C. Basis of Accounting

As defined by the Governmental Accounting Standards Board (GASB), the Authority is a proprietary fund and is accounted for on a cost of service measurement focus using the accrual basis of accounting in accordance with generally accepted accounting principles as promulgated by the GASB. In addition, the Authority applies all applicable Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The Authority has elected not to apply private sector standards issued after November 30, 1989.

Cash Equivalents - For purposes of the statement of cash flows, the Authority considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Investments are reported at fair value. The value is determined based upon market closing prices. The fair value of mutual funds is stated at share value.

Capital Assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Contributed capital assets are valued at their estimated fair market value on the date contributed. The Authority utilized a capitalization threshold of $5,000 for all capital assets. Capital assets are recorded at historical cost. Depreciation is computed using the straight-line method over the estimated useful lives as follows:

Sewage treatment facilities	3-50 years
General plant facility	3-25 years
Collection system	3-10 years

Operating Income and Expense – Operating income and operating expense are defined as activities that result directly from the Authority's operations as a sewer service provider to its member agencies. Non-operating income and expense are defined as ancillary activities such as interest income on funds invested, and other costs not directly attributable to operating activities.

Compensated Absences - Employees may accumulate up to, but not more than, twice their yearly allowance of vacation time. Vacation which has been earned but not used by employees is accrued, and is included in accrued compensation and benefits. No liability is recorded for non-vesting accumulating rights to receive sick pay benefits.

Net Assets - The financial statements utilize a net assets presentation. Net assets are categorized as invested in capital assets, restricted and unrestricted.

- *Invested in capital assets* groups all capital assets into one component and the accumulated depreciation of these assets reduce the balance in this category.
- *Restricted net assets for capital projects* reflect net assets that are subject to constraints externally imposed by its member agencies. The Authority's capital project budget requires funding and project approval from each participating member agency governing body.
- *Unrestricted net assets* represent net assets of the Authority that are not restricted for any project or purpose.

The Authority applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

Use of Estimates - The preparation of basic 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. Actual results could differ from those estimates.

Reclassifications - Certain accounts in the prior-year financial statements have been reclassified for comparative purposes to conform with the presentation in the current-year financial statements.

D. Upcoming Accounting and Reporting Changes

The Authority is currently analyzing its accounting practices to determine the potential impact on the financial statements for the following GASB Statements:

In November 2011, the Governmental Accounting Standards Board ("GASB") issued Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which is effective for financial periods beginning after December 15, 2011. This pronouncement provides accounting guidance for service concession arrangements in which a transferor and an operator in which the transferor conveys to an operator the right and the related obligation to provide services through the use of infrastructure or another public asset in exchange for significant consideration and the operator collects and is compensated by fees from third parties. To date the Authority has not entered into any service concession arrangements covered under this statement.

In December 2011, the GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which is effective for financial statements for periods beginning after December 15, 2011. The objective of this statement is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in certain FASB and AICPA pronouncements issued on or before November 30, 1989, which does not conflict or contradict GASB pronouncements.

In June 2011, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which is effective for financial statements for periods beginning after December 15, 2011. This statement provides guidance for deferred outflows of resources and deferred inflows of resources; previous financial reporting standards did not include guidance for reporting those financial statement elements, which are distinct from assets and liabilities.

In March 2012, the GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which is effective for financial statements for periods beginning after December 15, 2012. This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities.

In March 2012, the GASB issued Statement No. 66, *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62,* which is effective for financial statements for periods beginning after December 15, 2012. The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.*

In June 2012, the GASB issued Statement No. 67, *Financial Reporting for Pension Plans—an amendment of GASB Statement No. 25,* which is effective for financial statements for periods beginning after June 15, 2013. The objective of this Statement is to improve financial reporting by state and local governmental pension plans. This Statement replaces the requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans,* and No. 50, *Pension Disclosures,* as they relate to pension plans that are administered through trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements 25 and 50 remain applicable to pension plans that are not administered through trusts covered by the scope of this Statement and to defined contribution plans that provide postemployment benefits other than pensions.

In June 2012, the GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27,* which is effective for financial statements for periods beginning after June 15, 2014. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities.

2. CASH AND INVESTMENTS

Cash and investments as of June 30, 2012 and 2011 consisted of the following:

	2012	2011
Petty cash	$ 500	$ 500
Demand deposits	889,972	645,259
Investments	4,405,684	4,389,831
Total cash and investments	$ 5,296,156	$ 5,035,590

Investments Authorized by the Authority's Investment Policy

The Authority's investment policy permits investments pursuant to the California Government Code Section 53600 et seq. and 53630 et seq. and includes the following:

A. United States Treasury Securities (Bills, Notes and Bonds).
B. Obligations of United States Government Agencies such as Federal Home Loan Banks, Federal National Mortgage Association, and Federal Farm Credit Banks.
C. Local Agency Investment Fund (LAIF).
D. Certificate of Deposit (in any of the 50 largest F.D.I.C. Insured U.S. banks with which the Authority may have a credit or other business relationship).
E. Passbook savings account demand deposits.

F. Bankers' Acceptances of the U.S. Banks as defined in D. above.
G. Negotiable Certificates of Deposit of the U.S. banks as defined in D. above.
H. Repurchase Agreements executed against U.S. Government or Agency securities. Current market value of the collateral must be greater than or equal to the principal amount invested.

D, E, F, G and H above shall be insured or collateralized at the levels required by the Government Code.

External Investment Pool

The Authority invests in the California State Treasurer's Local Agency Investment Fund (LAIF). LAIF, established in 1977, is regulated by California Government Code Section 16429 and under the day to day administration of the State Treasurer. As of June 30, 2012 and June 30, 2011, LAIF had approximately $22 billion and $23 billion in investments, respectively. The Pool is not registered with the SEC.

LAIF determines fair value on its investment portfolio based on market quotations for those securities where market quotations are readily available, and on amortized cost of best estimate for those securities where market value is not readily available. The Authority's investments with LAIF at June 30, 2012 and June 30, 2011, included a portion of the pooled funds invested in structured notes and asset-backed securities. These investments are described as follows.

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

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

As of June 30, 2012 the Authority had $4,405,684 invested in LAIF, which had invested 3.47% of the pool investments funds in Structured Notes and Asset-Backed Securities. The Authority valued its investments with LAIF by multiplying its account balance with a fair value factor determined by LAIF. This factor is the result of dividing all LAIF participants' total aggregate fair value $60,588,263,603.42 by total aggregate amortized cost $60,514,457,550.95 resulting in a factor of 1.001219643.

As of June 30, 2011 the Authority had $4,389,831 invested in LAIF, which had invested 5.01% of the pool investments funds in Structured Notes and Asset-Backed Securities. The Authority valued its investments with LAIF by multiplying its account balance with a fair value factor determined by LAIF. This factor is the result of dividing all LAIF participants' total aggregate fair value $66,489,270,507.63 by total aggregate amortized cost $66,384,617,119.40 resulting in a factor of 1.001576470.

Investment Risks

Investments are subject to certain types of risks, including interest rate risk, custodial credit risk, credit quality risk, and concentration of credit risk. The following describes those risks.

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. The Authority does not have a formal policy regarding interest rate risk. However, the Authority's practice to manage 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 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.

Custodial Credit Risk - is the risk that the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Authority does not have a formal policy regarding custodial credit risk. The California Government Code and the Authority's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or 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 Authority deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits. With respect to investments, custodial credit risk does not apply to a local government's indirect investment in securities through the use of mutual funds or government investment pools such as LAIF.

As of June 30, 2012, the carrying amount of the Authority's cash deposits was $889,972 while the bank balance was $1,004,486. The bank balance and the carrying amount differed due to deposits in transit and outstanding checks. The FDIC insured the bank balances up to $250,000 per depositor, per insured depository institution, for each account ownership category, except for non-interest bearing transaction accounts at institutions participating in FDIC's Temporary Liquidity Guarantee Program, which are provided with unlimited deposit guarantee. The FDIC's Transactional Account Guarantee program (the "TAG Program") insures amounts above $250,000 by guaranteeing payment to account holders in the event that the financial institution fails to make any required payments. The Authority is insured at First National Bank of Northern California, for the aggregation of deposits owned in different rights and capacities. Should the FDIC Act lower the limits of its insurance coverage or should the TAG program become unavailable, First National Bank agrees to provide collateral coverage for any such shortfall.

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. The Authority does not have a formal policy regarding credit risk. LAIF does not receive a rating from a nationally recognized statistical rating organization.

Concentration of Credit Risk - The investment policy of the Authority contains no limitations on the amount that can be invested in any one issue beyond that stipulated by the California Government Code.

Marking Investments to Fair Value

The Authority adopted Governmental Accounting Standards Board (GASB) Statement 31, which requires that the Authority's investments be carried at fair value instead of cost. Under GASB 31, the Authority must adjust the carrying value of its investments to reflect their fair value at each fiscal year end, and it must include the effects of these adjustments in income for that fiscal year.

3. CHANGE IN ACCOUNTING ESTIMATE

During the fiscal year ended June 30, 2010, the Authority determined the due to member agencies amount of $518,153 as of June 30, 2009 was overestimated. The Authority reversed a portion of the payable and recorded a capital contribution of $221,068 during the year ended June 30, 2011.

4. RELATED PARTY TRANSACTIONS

Name of related parties	Relationship
City of Half Moon Bay (HMB)	Member agency
Granada Sanitary District (GSD)	Member agency
Montara Water and Sanitary District (MWSD)	Member agency

Related party transactions for the years ended June 30, 2012 and 2011 are summarized as follows:

	2012			
	Operation and Maintenance Assessments	Collection Assessments	Capital Assessments	Service Revenue
HMB	$ 1,308,859	$ 272,079	$ -	61,373
GSD	948,149	225,561	211,361	5,016
MWSD	583,989	312,389	140,907	69,433
	$ 2,840,997	$ 810,029	$ 352,268	$ 135,822

	2011			
	Operation and Maintenance Assessments	Collection Assessments	Capital Assessments	Service Revenue
HMB	$ 1,324,247	$ 273,621	$ -	73,706
GSD	832,717	215,768	312,000	6,413
MWSD	574,534	289,711	207,996	159,271
	$ 2,731,498	$ 779,100	$ 519,996	$ 239,390

Related party transactions as of June 30, 2012 and 2011 are summarized as follows:

	2012		2011	
	Receivable	Payable	Receivable	Payable
HMB	$ 35,568	$ -	$ 12,435	$ -
GSD	104,225	-	$ 1,050	-
MWSD	21,974	111	27,106	267
	$ 161,767	$ 111	$ 40,591	$ 267

5. CAPITAL ASSETS

Changes in capital assets for the year ended June 30, 2012 were as follows:

Nondepreciable Assets:	Balance June 30, 2011	Additions	Retirements	Transfers	Balance June 30, 2012
Easement	$ 24,950	$ -	$ -	$ -	$ 24,950
Land	569,740	-	-	-	569,740
Construction in progress	405,808	125,687	-	(122,671)	408,824
Total Nondepreciable Assets	1,000,498	125,687	-	(122,671)	1,003,514
Depreciable Assets:					
Sewage treatment facilities	41,017,489	248,810	-	122,671	41,388,970
General plant facility	313,851	-	-	-	313,851
Collection system	374,735	33,470	-	-	408,205
Total Depreciable Assets	41,706,075	282,280	-	122,671	42,111,026
Less: Accumulated Depreciation					
Sewage treatment facilities	(27,701,758)	(1,629,242)	-	-	(29,331,000)
General plant facility	(184,134)	(15,807)	-	-	(199,941)
Collection system	(367,658)	(5,658)	-	-	(373,316)
Total Accumulated Depreciation	(28,253,550)	(1,650,707)	-	-	(29,904,257)
Total Depreciable Assets, net	13,452,525	(1,368,427)	-	122,671	12,206,769
Total Capital Assets, net	$ 14,453,023	$ (1,242,740)	$ -	$ -	$ 13,210,283

Changes in capital assets for the year ended June 30, 2011 were as follows:

Nondepreciable Assets:	Balance June 30, 2010	Additions	Retirements	Transfers	Balance June 30, 2011
Easement	$ 24,950	$ -	$ -	$ -	$ 24,950
Land	569,740	-	-	-	569,740
Construction in progress	349,602	56,206	-	-	405,808
Total Nondepreciable Assets	944,292	56,206	-	-	1,000,498
Depreciable Assets:					
Sewage treatment facilities	40,774,301	289,372	(46,184)	-	41,017,489
General plant facility	313,851	-	-	-	313,851
Collection system	374,735	-	-	-	374,735
Total Depreciable Assets	41,462,887	289,372	(46,184)	-	41,706,075
Less: Accumulated Depreciation					
Sewage treatment facilities	(26,125,625)	(1,622,317)	46,184	-	(27,701,758)
General plant facility	(167,638)	(16,496)	-	-	(184,134)
Collection system	(340,711)	(26,947)	-	-	(367,658)
Total Accumulated Depreciation	(26,633,974)	(1,665,760)	46,184	-	(28,253,550)
Total Depreciable Assets, net	14,828,913	(1,376,388)	-	-	13,452,525
Total Capital Assets, net	$ 15,773,205	$ (1,320,182)	$ -	$ -	$ 14,453,023

6. OPERATING LEASES

The Authority leased equipment for treatment purpose on a short and defined term. As of June 30, 2012, SAM had no operating leases that have initial or remaining noncancelable lease terms in excess of one year.

Equipment lease expense for the year ended June 30, 2012 and 2011 totaled $79,598 and $69,903, respectively.

7. RISK MANAGEMENT

The Authority mitigates its risk of liability, workers' compensation and property losses by being a member of the California Sanitation Risk Management Authority (CSRMA) and participating in their risk sharing and insurance purchasing pools. The CSRMA pool programs operate to reduce costs by sharing risk among the members. Members of the pool are assessed a yearly premium which is based on member exposure data. In addition, there is retrospective rating process, the result of which is applied to the member's renewal invoice. Participation in CSRMA insurance purchasing pools provide the Authority General Liability Insurance, including excess coverage , to $25.5 million; workers' compensation insurance to statutory limits and property insurance coverage for covered locations to $42.3 million in insurable values.

8. EMPLOYEES' RETIREMENT PLAN

Plan Description

The Authority's defined benefit pension plan, (the "Plan"), provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. The Plan is part of the Public Agency portion of the California Public Employees Retirement System (PERS), a cost sharing multiple-employer plan administered by PERS, which acts as a common investment and administrative agent for participating public employers within the State of California. A menu of benefit provisions as well as other requirements is established by State statutes within the Public Employees' Retirement Law.

The Authority selects optional benefit provisions from the benefit menu by contract with PERS and adopts those benefits through Board Action. PERS issues a separate annual financial report. Copies of the PERS' annual financial report may be obtained from the PERS Executive Office - 400 P Street - Sacramento, California 95814.

Funding Policy

Active plan members in the Plan are required to contribute 7% of their annual covered salary. The Authority is required to contribute the actuarially determined remaining amounts necessary to fund the benefits for its members. Under the current memorandum of understanding (MOU), the Authority pays the employee and employer's portion for retirement. The actuarial methods and assumptions used are those adopted by the PERS Board of Administration.

The required employer contribution rate for the fiscal years ended June 30, 2012 and 2011 was 13.526% and 12.557%, respectively. The contribution requirements of the plan members are established by State statute and the employer contribution rate is established and may be amended by PERS.

Annual Pension Cost

For fiscal years ended June 30, 2012 and 2011, the Authority's annual pension cost was $179,611 and $160,073, respectively, which was equal to the Authority's required and actual contribution. The required contribution was determined as part of the June 30, 2008 actuarial valuation using the entry age normal actuarial cost method. The actuarial assumptions included: (a) 7.75% investment rate of return (net of administrative expenses); (b) projected annual salary increases that vary by age, duration of service, and type of employment; (c) 3.0% inflation; (d) 3.25% payroll growth; and (e) individual salary growth based on a merit scale varying by duration of employment coupled with an assumed annual inflation of 3.0%

and an annual production growth of 0.25%. The actuarial value of PERS assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a 15-year period (smoothed market value) depending on the size of investment gains and/or losses.

Three Year Trend Information of PERS

Fiscal Year Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
6/30/2010	140,208	100%	-
6/30/2011	160,073	100%	-
6/30/2012	179,611	100%	-

9. OTHER EMPLOYMENT BENEFITS

A. Other Postemployment Healthcare Benefits

In adopting the requirements of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* (GASB 45) during the year ended June 30, 2010, the Authority recognizes the cost of postemployment healthcare in the year when employee services are received, reports the accumulated liability from prior years, and provides information useful in assessing potential demands on the Authority's future cash flows. Because the Authority adopted the requirements of GASB Statement No. 45 prospectively, recognition of the liability accumulated from prior years will be phased in over fifteen years, commencing with the 2010 liability.

Plan Description

The Authority administers a single-employer defined benefit healthcare plan ("the Retiree Health Plan") with PERS to provide postemployment healthcare benefit to eligible retirees through the Authority's group health insurance plan which covers both active and retired members. Benefit provisions are established through negotiations between the Authority and the union representing employees and are renegotiated each three-year bargaining period. The Retiree Health Plan does not issue a publicly available financial report.

Funding Policy

Contribution requirements also are negotiated between the Authority and union representatives. Currently the Authority pays the PERS minimum on behalf of each eligible retired employee or eligible survivor of a retired employee and the person receives benefit pays any additional premium based on the coverage selected. The Authority contributed $3,624 and $2,472, respectively, to the plan in each of the years ended June 30, 2012 and 2011.

Annual OPEB Cost and Net OPEB Obligation

The Authority's annual other postemployment benefit (OPEB) cost is calculated based on the annual required contribution (ARC) of the employer. The Authority has elected to calculate the ARC and related information using the alternative measurement method permitted by GASB Statement No. 45 for employers with plans that have fewer than 100 total members. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The following shows the components of the Authority's annual OPEB cost, the amount actually contributed, and changes in the Authority's net OPEB obligation to the Retiree Health Plan for the years ended June 30, 2012 and 2011.

Net OPEB Obligation as of June 30, 2011	$ 58,414
Annual OPEB Cost:	
Normal Cost	30,171
Interest	1,508
Benefit payments made	(3,624)
Net OPEB Obligation as of June 30, 2012	$ 86,469

Net OPEB Obligation as of June 30, 2010	$ 29,207
Annual OPEB Cost:	
Normal Cost	30,171
Interest	1,508
Benefit payments made	(2,472)
Net OPEB Obligation as of June 30, 2011	$ 58,414

Trend Information

The table below presents three year trend information:

Year	Annual OPEB Cost	Actual Employer Contribution	Percentage Contributed	Net OPEB Obligation
2010	$ 31,679	$ 2,472	8%	$ 29,207
2011	$ 31,679	$ 2,472	8%	$ 58,414
2012	$ 31,679	$ 3,624	11%	$ 86,469

Funded Status and Funding Progress

As of June 30, 2010, the most recent actuarial valuation date, the actuarial accrued liability (AAL) for benefits was $199,692, all of which was unfunded. The covered payroll (annual payroll of active employees covered by the plan) was $1,261,060 and the ratio of unfunded actuarial accrued liability (UAAL) to the covered payroll was 15.8%.

The projection of future benefit payments for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Required Supplementary Information – Schedule of Funding Progress for the Retiree Health Plan

Valuation Date	AAL - Simplified Entry Age	Actuairal Value of Assets	UAAL	Funded Ratio	Annual Covered Payroll	UAAL as a Percentage of Covered Payroll
6/30/10	$ 199,692	$ -	$ 199,692	0.0%	$ 1,261,060	15.8%

The aggregate actuarial cost method is used for funding purposes. However, because the aggregate actuarial cost method does not identify or separately amortize unfunded actuarial liabilities, the entry age actuarial cost method has been used to provide required information about funded status and funding progress as a surrogate. The information presented in this schedule is intended to approximate the funding progress of the plan based on the use of the aggregate actuarial cost method.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the June 30, 2010 actuarial valuation, the aggregate cost method was used. The actuarial assumptions used in the valuation are as follows:

Retirement age for active employees – Based on the historical average retirement age for the covered group, active plan members were assumed to retire at age 67.

Marital status – Marital status of members at the calculation date was assumed to continue throughout retirement.

Mortality – Life expectancies were based on mortality tables from the National Center for Health Statistics.

Turnover – Non-group-specific age-based turnover data from GASB Statement 45 were used as the basis for assigning active members a probability of remaining employed until the assumed retirement age and for developing an expected future working lifetime assumption for purposes of allocating to periods the present value of total benefits to be paid.

Healthcare cost trend rate – The expected rate of increase in healthcare insurance premiums was based on projections of the Office of the Actuary at the Centers for Medicare & Medicaid Services. A rate of 5.7% initially, reduced to an ultimate rate of 6.6% after ten years, was used.

Health insurance premiums – 2010 health insurance premiums for retirees were used as the basis for calculation of the present value of total benefits to be paid.

Inflation rate – The expected long-term inflation assumption of 3% was used.

Payroll growth rate – The expected long-term payroll growth rate was assumed to equal the rate of inflation.

Based on the historical and expected returns of the Authority's short-term investment portfolio, a discount rate of 5% was used. The unfunded actuarial accrued liability is being amortized as a level dollar of projected payroll on an open basis. The remaining amortization period as of June 30, 2012 was 13 years.

B. Deferred Compensation Plans

The Authority maintains two deferred compensation plans, qualified under Section 457 of the Internal Revenue Code, in which substantially all employees may participate. Generally, deferred compensation is payable upon retirement, termination of employment, disability or death. The Authority made contributions to the deferred compensation plans of $8,000 and $9,000 for the years ending June 30, 2012 and 2011, respectively. The plan assets are held in trust for the exclusive benefit of the participants and are not included in the Authority's financial statements.

Compensated Absences

Accrued compensated absences for the years ended June 30, 2012 and 2011 were as follows:

	2012	2011
Beginning	$ 120,017	$ 114,058
Additions	86,854	81,440
Reductions	(77,139)	(75,481)
End of year	$ 129,732	$ 120,017
Due within one year	$ 77,139	$ 75,481

C. G. UHLENBERG LLP
CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

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

To the Board of Directors of the
Sewer Authority Mid-Coastside
Half Moon Bay, California

We have audited the accompanying basic financial statements of the Sewer Authority Mid-Coastside (the "Authority") as of and for the years ended June 30, 2011 and 2012 and have issued our report thereon dated September 26, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of the Authority is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations,

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contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, the Board of Directors, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.

C. G. Uhlenberg LLP

September 26, 2012

Redwood City, California