

**San Rafael Sanitation District
A Component Unit of the City of San Rafael**

**Annual Financial Report
Fiscal Years Ended
June 30, 2017 and 2016**

**With
Independent Auditors' Report**

**SAN RAFAEL SANITATION DISTRICT
YEARS ENDED JUNE 30, 2017 AND 2016**

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INDEPENDENT AUDITORS' REPORT

To the Members of the Board
of the San Rafael Sanitation District
San Rafael, California

Report on the Financial Statements

We have audited the accompanying financial statements of the San Rafael Sanitation District (the District), a component unit of the City of San Rafael, as of and for the years ended June 30, 2017 and 2016 and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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 the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of San Rafael Sanitation District as of June 30, 2017 and 2016, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

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

Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued our report dated September 21, 2017, on our consideration of the District's internal control over financial reporting 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, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

Varrinek, Trine, Day & Co., LLP.
Pleasanton, California
September 21, 2017

SAN RAFAEL SANITATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

The Management's Discussion and Analysis provides an overview of the District's financial activities for the fiscal years ended June 30, 2017 and 2016. Please read it along with the District's financial statements, which begin on page 8.

FINANCIAL HIGHLIGHTS

The District's total net position as of June 30, 2017, was approximately \$67,884,000 which is an increase of approximately \$6,500,000 over the prior year's balance. Net position is comprised of approximately \$48,392,000 of net investment in capital assets and approximately \$19,491,000 of unrestricted net position.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the District's financial statements which include two components: (1) basic financial statements and (2) notes to the basic financial statements.

The District is a single purpose entity that reports as an enterprise fund under governmental accounting standards. The financial statements are designed to provide readers with a broad overview of the District's finances, similar to a private-sector business.

The Statements of Net Position present information on all of the District's assets and liabilities, with the difference between assets and liabilities reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The Statements of Revenues, Expenses and Changes in Net Position present information showing how the District's net position changed during the fiscal year. All changes in net position are recognized as of the date of the underlying event that gives rise to the change, regardless of the timing of the related cash flows.

The Statements of Cash Flows present information about the District's cash receipts, cash payments and net changes in cash resulting from operations, investing, and financing activities. These statements show the sources and uses of cash, as well as the change in the cash balances during the fiscal years.

SAN RAFAEL SANITATION DISTRICT
MANAGEMENT’S DISCUSSION AND ANALYSIS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

The following table is a summary of the District’s assets, liabilities, and net position.

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Current assets	\$ 24,639,912	\$ 24,100,692	\$ 23,022,326
Noncurrent assets	48,392,318	43,425,057	39,191,829
Total assets	<u>73,032,230</u>	<u>67,525,749</u>	<u>62,214,155</u>
Current liabilities	1,341,625	1,944,508	2,113,156
Noncurrent liabilities	3,807,005	4,197,790	3,993,160
Total liabilities	<u>5,148,630</u>	<u>6,142,298</u>	<u>6,106,316</u>
Net position			
Net investment in capital assets	48,392,318	43,425,057	39,191,829
Unrestricted	19,491,282	17,958,394	16,916,010
Total net position	<u>\$ 67,883,600</u>	<u>\$ 61,383,451</u>	<u>\$ 56,107,839</u>

As indicated in the table above, current assets increased each year from 2015 to 2017. This was primarily because SRSD was accumulating resources for planned capital projects. The increase in noncurrent assets was the result of capital improvement projects undertaken each year, partly offset by annual depreciation amount. Expenditures for capital improvement projects often do not coincide with revenue for annual fiscal periods since they are subject to lengthy planning periods, weather considerations and long construction periods. Current liabilities consist primarily of trade payables and a liability to the City of San Rafael for pension and other post-employment benefits. The majority of the trade payables relate to accounts payable on capital projects.

At June 30, 2017, unrestricted net position was approximately \$19.49 million, an increase of 1.532 million over the prior year. Although there are no legal restrictions on this balance, a substantial portion of these funds are held to finance the District’s ongoing capital improvement programs. Details of capital improvements are described in *Capital Assets and Debt Administration*.

SAN RAFAEL SANITATION DISTRICT
MANAGEMENT’S DISCUSSION AND ANALYSIS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

Results of operations are summarized as follows:

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Operating revenues	\$ 16,014,016	\$ 15,414,530	\$ 14,629,758
Nonoperating revenues	1,662,082	1,446,171	1,393,054
Total revenues	<u>17,676,098</u>	<u>16,860,701</u>	<u>16,022,812</u>
Operating expenses	<u>11,255,194</u>	<u>11,654,767</u>	<u>11,375,239</u>
Income before connection fees received and special item	6,420,904	5,205,934	4,647,573
Connection fees received	79,245	69,678	133,692
Special item - contract services	-	-	(4,462,815)
Changes in net position	<u>6,500,149</u>	<u>5,275,612</u>	<u>318,450</u>
Net position at beginning of the year	<u>61,383,451</u>	<u>56,107,839</u>	<u>55,789,389</u>
Net position at end of the year	<u>\$ 67,883,600</u>	<u>\$ 61,383,451</u>	<u>\$ 56,107,839</u>

The fourth of five annual sewer service rate increases was implemented in fiscal year 2016-17. Operating expenses decreased from 2016 to 2017. Included in operating expenses are waste treatment costs incurred as a member of the Central Marin Sanitation Agency. These sewage treatment operating costs include a proportionate share of revenue bonds issued by the Central Marin Sanitation Agency (CMSA).

The financial statements for the year ended June 30, 2015 included the initial recognition of the obligation to the City of San Rafael related to its unfunded obligation for post-retirement benefits for employees serving the District which was presented as a “Special Item” in the statements of revenue, expense and changes in net position. Annual changes to this obligation are recorded in operating expenses for the years ended June 30, 2016 and 2017. For fiscal year 2016, the change in unfunded obligation resulted in an increase in operating expense of approximately \$396,000. For fiscal year 2017, the change in unfunded obligation resulted in a decrease to operating expenses of approximately \$331,000.

SAN RAFAEL SANITATION DISTRICT
MANAGEMENT’S DISCUSSION AND ANALYSIS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital assets, net of accumulated depreciation, were as follows:

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Land & easements	\$ 115,329	\$ 115,329	\$ 115,329
Construction in progress	272,032	3,204,067	591,304
Subsurface lines	23,882,502	17,551,743	15,300,773
Sewage collection facilities	23,566,223	21,867,794	22,397,512
General plant & admin facilities	556,232	686,124	786,911
Net investment in capital assets	<u>\$ 48,392,318</u>	<u>\$ 43,425,057</u>	<u>\$ 39,191,829</u>

In addition to operations and maintenance (O&M) programs, the District also maintains ongoing capital improvement programs. These programs largely influence how the District budgets and sets its rates.

In June 2015, the Board of Directors designated amounts to be provided as reserves for capital improvement projects and adopted a policy requiring transfers, commencing in 2015-16, to separate reserve accounts to provide funding required to pay for planned capital improvement projects. Transfers are based on average annual expenditures projected for the subsequent ten years.

The first program, known as the *80-Year Life-Cycle Program*, is maintained to provide for systematic replacement of all of the District’s gravity sewer lines over a rolling, 80-year cycle. Management plans to replace an average of 1.6 miles of sewer lines per year at an estimated cost of \$4.90 million per year. Approximately \$5.37 million was expended on these projects during the year ended June 30, 2017, leaving a reserve balance of \$7.06 million for this program.

The District also has a *Pump Station and Force Main Capital Improvement Program* to make capital improvements related to its pump stations and force mains. Planned annual expenditures are funded on a pay-as-you-go basis and annual costs are estimated to range between \$1.20 million and \$2.40 million per year. Approximately \$1.14 million was expended on these projects during the year ended June 30, 2017, leaving a reserve balance of \$1.70 million for this program.

The District maintains a program to provide for replacement of vehicles and other equipment, setting aside a portion of the expected replacement cost of each significant equipment item. Approximately \$3,000 was expended on equipment during the year ended June 30, 2017, leaving a reserve balance of \$1.69 million for this program.

SAN RAFAEL SANITATION DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

THE FUTURE OF THE DISTRICT

The District is insulated from general economic conditions, such as increases or declines in property tax values, or other types of revenues that vary with economic conditions, such as sales taxes. Most of the District's revenues are from user fees that are based on rates set by the District at levels sufficient to provide for planned costs of operation, maintenance, debt service and capital improvements. Sewer charges are annual fees charged to all premises connected to the system. In June 2013, the District adopted a new rate schedule with schedule increases for 2013-14 through 2017-18.

Personnel costs, including retirement and health benefits, capital improvement, and operations and maintenance costs are projected to increase. In addition, the cost of sewage treatment will rise significantly due to the rising costs of operation of Central Marin Sanitation District (CMSA) along with an increase in the allocation percentage of CMSA operating costs allocated to the District. The new user rate schedules are expected to be adequate to operate and maintain our system.

REQUESTS FOR INFORMATION

This financial report is designed to provide our residents, taxpayers and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the funds under its stewardship.

Please address any questions about this report or requests for additional financial information to 111 Morphew Street, San Rafael, CA 94901.

Basic Financial Statements

SAN RAFAEL SANITATION DISTRICT

STATEMENTS OF NET POSITION

AS OF JUNE 30, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 24,536,913	\$ 24,011,268
Accounts receivable	18,609	19,294
Prepaid expenses	54,842	54,382
Due from related parties	29,548	15,748
Total current assets	<u>24,639,912</u>	<u>24,100,692</u>
Noncurrent assets		
Nondepreciable assets	387,361	3,319,396
Collection systems and facilities, net	48,004,957	40,105,661
Total noncurrent assets	<u>48,392,318</u>	<u>43,425,057</u>
Total assets	<u>73,032,230</u>	<u>67,525,749</u>
LIABILITIES		
Current liabilities		
Accounts payable	588,674	1,216,053
Payable to related parties	32,120	67,238
Obligation to the City of San Rafael	720,831	661,217
Total current liabilities	<u>1,341,625</u>	<u>1,944,508</u>
Noncurrent liabilities:		
Obligation to the City of San Rafael	<u>3,807,005</u>	<u>4,197,790</u>
Total liabilities	<u>5,148,630</u>	<u>6,142,298</u>
NET POSITION		
Net investment in capital assets	48,392,318	43,425,057
Unrestricted	19,491,282	17,958,394
Total net position	<u>\$ 67,883,600</u>	<u>\$ 61,383,451</u>

SAN RAFAEL SANITATION DISTRICT
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN NET POSITION
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

	2017	2016
OPERATING REVENUES		
Sewer charges	\$ 16,014,016	\$ 15,414,530
OPERATING EXPENSES		
Sewage collection	3,250,465	4,029,163
Sewage treatment	6,155,154	5,934,022
Depreciation and amortization	1,549,499	1,425,741
General and administration	300,076	265,841
Total operating expenses	11,255,194	11,654,767
Operating income	4,758,822	3,759,763
NONOPERATING REVENUES		
Property taxes	1,528,047	1,367,172
Aid from governmental agencies	36,945	32,774
Interest income	97,090	46,225
Total nonoperating revenues	1,662,082	1,446,171
Income before connection fees received	6,420,904	5,205,934
Connection fees received	79,245	69,678
CHANGES IN NET POSITION	6,500,149	5,275,612
Net position at beginning of the year	61,383,451	56,107,839
Net position at end of the year	\$ 67,883,600	\$ 61,383,451

SAN RAFAEL SANITATION DISTRICT
STATEMENTS OF CASH FLOWS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from sewer charges	\$ 15,985,153	\$ 15,400,488
Payments to City of San Rafael for contract personnel	(2,230,632)	(2,274,797)
Payments to joint venture for sewage treatment	(6,155,154)	(5,934,022)
Payments to vendors and suppliers	(1,053,932)	(1,513,651)
Payments to City of San Rafael regarding post-employment benefits for contract personnel	(661,217)	(469,655)
Net cash provided by operating activities	<u>5,884,218</u>	<u>5,208,363</u>
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Receipts from property taxes	1,528,047	1,367,172
Receipts of aid from governmental agencies	36,945	32,774
Net cash provided by non-capital financing activities	<u>1,564,992</u>	<u>1,399,946</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Connection fees collected	79,245	69,678
Payments for capital acquisitions	(7,099,900)	(5,509,954)
Net cash used for capital and related financing activities	<u>(7,020,655)</u>	<u>(5,440,276)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest received from Marin County pooled cash and investments account	97,090	46,225
Net change in cash and cash equivalents	525,645	1,214,258
Cash and cash equivalents at beginning of year	24,011,268	22,797,010
Cash and cash equivalents at end of year	<u>\$ 24,536,913</u>	<u>\$ 24,011,268</u>

SAN RAFAEL SANITATION DISTRICT
STATEMENTS OF CASH FLOWS (CONTINUED)
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

**RECONCILIATION OF OPERATING INCOME
TO NET CASH PROVIDED BY OPERATING ACTIVITIES**

	<u>2017</u>	<u>2016</u>
Operating income	\$ 4,758,822	\$ 3,759,763
Adjustments to reconcile operating income to net cash provided (used) by operating activities:		
Depreciation and amortization	1,549,499	1,425,741
(Increase) decrease in accounts receivable and other current assets	(13,575)	135,892
Increase (decrease) in accounts payable and other current liabilities	(79,357)	(509,225)
Increase (decrease) in Obligation to the City of San Rafael	(331,171)	396,192
Net cash provided from operating activities	<u>\$ 5,884,218</u>	<u>\$ 5,208,363</u>

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

1. NATURE OF THE ORGANIZATION

San Rafael Sanitation District is a *Sanitation District* in the County of Marin formed in 1947 under Section 4700 of the California Health & Safety Code. It serves the southern two-thirds of the City of San Rafael and adjacent unincorporated areas. The District provides wastewater transmission over its entire service area and performs collection system maintenance in the unincorporated areas.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

REPORTING ENTITY

Although the nucleus of a financial reporting entity usually is a primary government, an organization other than a primary government, such as a component unit, may serve as the nucleus for its financial reporting entity when the component unit provides separately issued financial statements. Component units are legally separate organizations for which the elected officials of the primary government are financially accountable. The primary government is financially accountable if it appoints a voting majority of the organization's governing body and is able to impose its will on that organization. The San Rafael Sanitation District is a component unit of the City of San Rafael. The District is governed by a three member Board of Directors serving four-year terms. The City Council of the City of San Rafael appoints two out of the three board members and has the ability to remove the two board members at will. The third member is a representative of the County of Marin.

INTRODUCTION

The District's financial statements are prepared in accordance with generally accepted accounting principles (GAAP). The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements.

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

BASIS OF ACCOUNTING

The District's operations are accounted for as an enterprise fund, and are reported using the economic resources measurement focus and the accrual basis of accounting – similar to business enterprises. Accordingly, revenues are recognized when they are earned and expenses are recognized at the time liabilities are incurred.

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

The District distinguishes between operating revenues and expenses from nonoperating revenues and expenses. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the District's principal ongoing operations. These revenues are primarily charges to customers for services. Operating expenses include the cost of services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

CASH AND CASH EQUIVALENTS

For purposes of the statement of cash flows, the District has defined cash and cash equivalents to include cash on hand, demand deposits, and short-term investments maturing within 90 days.

COLLECTION SYSTEMS AND FACILITIES

Collection systems and facilities purchased or constructed are stated at cost. Assets contributed have been recorded at the fair market value at the date received. Interest is capitalized for assets constructed when applicable. The costs of normal repairs and maintenance that do not add to the value of an asset or materially extend asset lives are not capitalized. Improvements are capitalized and depreciated over the remaining useful lives of the related capital assets, as applicable. Applicable capital assets must be capitalized for amounts \$1,000 or above and may be capitalized for amounts from \$500 to \$1,000 if determined to be sensitive. Depreciation is provided by the straight-line method over the estimated useful lives of capital assets as follows:

Subsurface lines	50-80 years
Sewer collection facilities	5-50 years
General plant & administrative facilities	3-15 years

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

JOINT VENTURES

The District participates in a joint-powers agreement with the Central Marin Sanitation Agency, a regional sewage treatment facility, as further explained in Note 6.

SEWER CHARGES

Sewer charges are billed and collected on behalf of the District by the County of Marin as a special assessment on annual property tax billings. Property taxes are levied on January 1 and are due in two equal installments on November 1 and February 1. In accordance with the Teeter Plan, the County remits to the District all charges which are assessed and the County retains responsibility for collecting past due amounts.

The Teeter Plan provides that the County advance the District its share of the annual gross levy of secured property taxes and special assessments. In consideration, the District gives the County of Marin its rights to penalties and interest on delinquent secured property tax receivables and actual proceeds collected.

PROPERTY TAXES

The County of Marin levies taxes and places liens on real property as of January 1 on behalf of the District. Property taxes are due the following November 1 and February 1 and become delinquent December 10 and April 10, for the first and second installments, respectively. Unsecured property taxes are levied throughout the year.

CONNECTION FEES

Connection fees represent a one-time contribution of resources to the District imposed on contractors and developers for the purpose of financing capital improvements. Connection fees are recognized after non-operating revenues (expenses) in the statement of revenues, expenses and changes in net position. The District utilizes connection fees received on a first-in-first-out basis to finance current year capital projects. Accordingly, if there is a balance of connection fees available at year-end, it is classified as restricted net position.

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

STAFF SALARIES AND BENEFITS AND WORKERS' COMPENSATION

The District has no regular full-time employees. The City of San Rafael provides staff to the District under contract and provides all benefits including workers' compensation insurance.

ESTIMATES

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

RECLASSIFICATIONS

Certain amounts in the prior-year financial statements have been reclassified for comparative purposes to conform to the presentation of the current-year financial statements.

3. CASH AND CASH EQUIVALENTS

The District maintains all of its cash in the County of Marin pooled investment fund for the purpose of increasing interest earnings through pooled investment activities. Interest earned on the investment pool is allocated quarterly to the participating funds using the daily cash balance of each fund. This pool, which is available for use by all funds, is displayed in the financial statements as "Cash and cash equivalents."

The County Pool includes both voluntary and involuntary participation from external entities. The District is a voluntary participant. The State of California statutes require certain special districts and other governmental entities to maintain their cash surplus with the County Treasurer. The District has approved by resolution, the investment policy of the County of Marin which complies with the California Government Code.

The County's investment pool is not registered with the Securities and Exchange Commission as an investment company. The pool has a credit rating of "AAA/V1." Investments made by the Treasurer are regulated by the California Government Code and by the County's investment policy. The objectives of the policy are in order of priority, safety, liquidity, yield, and public trust.

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

3. CASH AND CASH EQUIVALENTS (continued)

The County has established a treasury oversight committee to monitor and review the management of public funds maintained in the investment pool in accordance with Article 6 Section 27131 of the California Government Code. The oversight committee and the Board of Supervisors review and approve the investment policy annually. The County Treasurer prepares and submits a comprehensive investment report to the members of the oversight committee and the investment pool participants every month. The report covers the types of investments in the pool, maturity dates, par value, actual costs and fair value.

FAIR VALUE MEASUREMENT

The District categorized its fair value measurements within the fair value hierarchy established by general accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets, Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. As of June 30, 2017, The District held no individual investments. All funds are invested in the Marin County Investment Pool.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The District's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability. Deposits and withdrawals from the County Pool are made on the basis of \$1 and not fair value. Accordingly, the Districts' proportionate share of investments in the County Pool at June 30, 2017 and 2016 of \$24,537,000 and \$2,4011,000, respectively, were considered uncategorized input not defined as a Level 1, Level 2, or Level 3 input.

The Marin County Investment Pool invests substantially all its funds in U.S. government obligations and registered money market funds rated 'AAAmmf' by Fitch Ratings or equivalent.

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

3. CASH AND CASH EQUIVALENTS (continued)

INTEREST RATE RISK

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Duration is a measure of the price sensitivity of a fixed income portfolio to changes in interest rates. It is calculated as the weighted average time to receive a bond's coupon and principal payments. The longer the duration of a portfolio, the greater is its price sensitivity to changes in interest rates. The District has not adopted a policy to manage interest rate risk.

In accordance with its investment policy, the County manages its exposure to declines in fair values by limiting the weighted average maturity of its investment pool to 540 days, or 1.5 years. At June 30, 2017 and 2016, the County's investment pool had a weighted average maturity of 231 and 204 days, respectively.

For purposes of computing weighted average maturity, the maturity date of variable rate notes is the length of time until the next reset date rather than the stated maturity date.

CREDIT RISK

State law and the County's Investment Policy limits investments in commercial paper, corporate bonds, and medium term notes to the rating of "A" or higher as provided by Moody's Investors Service or Standard & Poor's Corporation. The County's Investment Policy limits investments purchased by Financial Institution Investment Accounts, a type of mutual fund, to United States Treasury and Agency obligations with a credit quality rating of "AAA/V1."

**SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016**

3. CASH AND CASH EQUIVALENTS (continued)

CONCENTRATION OF CREDIT RISK

This is the risk of loss attributed to the concentration of the District’s investment in a single issuer.

The following is a summary of the concentration of credit risk by investment type of the Marin County Investment Pool as a percentage of fair value at June 30, 2017:

Investments in Investment Pool	Percent of Portfolio	
	2017	2016
Federal agency - discount	70%	78%
Federal agency - coupons	28%	20%
Money market funds	2%	2%
	100%	100%

CUSTODIAL CREDIT RISK

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

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

4. COLLECTION SYSTEMS AND FACILITIES

A summary of the District's collection systems and facilities for the years ended June 30, 2017 and 2016 respectively, follows:

	<u>Balance at June 30, 2016</u>	<u>Additions</u>	<u>Transfers & Adjustments</u>	<u>Balance at June 30, 2017</u>
Nondepreciable capital assets:				
Land and easements	\$ 115,329	\$ -	\$ -	\$ 115,329
Construction in progress	3,204,067	6,393,082	(9,325,117)	272,032
Total nondepreciable	<u>\$ 3,319,396</u>	<u>\$ 6,393,082</u>	<u>\$ (9,325,117)</u>	<u>\$ 387,361</u>
Depreciable capital assets:				
Subsurface lines	\$ 28,364,238	\$ 70,932	\$ 6,745,103	\$ 35,180,273
Sewage collection facilities	39,499,143	49,533	2,580,013	42,128,689
General plant and administration	1,649,897	3,213	-	1,653,110
Total depreciable	<u>69,513,278</u>	<u>123,678</u>	<u>9,325,116</u>	<u>78,962,072</u>
Less: accumulated depreciation:				
Subsurface lines	10,812,495	485,276	-	11,297,771
Sewage collection facilities	17,631,349	931,117	-	18,562,466
General plant and administration	963,773	133,105	-	1,096,878
Total accumulated depreciation	<u>29,407,617</u>	<u>1,549,498</u>	<u>-</u>	<u>30,957,115</u>
Total collection systems & & facilities-net	<u>\$ 40,105,661</u>	<u>\$ (1,425,820)</u>	<u>\$ 9,325,116</u>	<u>\$ 48,004,957</u>

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

4. COLLECTION SYSTEMS AND FACILITIES (continued)

	<u>Balance at June 30, 2015</u>	<u>Additions</u>	<u>Transfers & Adjustments</u>	<u>Balance at June 30, 2016</u>
Nondepreciable capital assets:				
Land and easements	\$ 115,329	\$ -	\$ -	\$ 115,329
Construction in progress	591,304	5,220,500	(2,607,737)	3,204,067
Total nondepreciable	<u>\$ 706,633</u>	<u>\$ 5,220,500</u>	<u>\$ (2,607,737)</u>	<u>\$ 3,319,396</u>
Depreciable capital assets:				
Subsurface lines	\$ 25,660,029	\$ 91,704	\$ 2,612,505	\$ 28,364,238
Sewage collection facilities	39,191,304	312,607	(4,768)	39,499,143
General plant and administration	1,615,739	34,158	-	1,649,897
Total depreciable	<u>66,467,072</u>	<u>438,469</u>	<u>2,607,737</u>	<u>69,513,278</u>
Less: accumulated depreciation:				
Subsurface lines	10,359,256	453,239	-	10,812,495
Sewage collection facilities	16,793,792	837,557	-	17,631,349
General plant and administration	828,828	134,945	-	963,773
Total accumulated depreciation	<u>27,981,876</u>	<u>1,425,741</u>	<u>-</u>	<u>29,407,617</u>
Total collection systems & & facilities-net	<u>\$ 38,485,196</u>	<u>\$ (987,272)</u>	<u>\$ 2,607,737</u>	<u>\$ 40,105,661</u>

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

5. OBLIGATION TO CITY OF SAN RAFAEL

The District’s staff is provided by the City of San Rafael under a contractual arrangement originated in 1987 that requires the District to pay all related employee costs incurred by the City on its behalf. Quarterly payments are made by the District to the City and include amounts sufficient to cover the City’s currently required contributions to employee benefit plans, including a portion for past service costs. During fiscal year 2014-15, the parties agreed that SRSD was also responsible for unfunded obligations related to past service. These financial statements include an estimate of the District’s obligation to reimburse the City for future funding for benefits incurred through June 30, 2017. As agreed to by the parties, this obligation will be funded over approximately fifteen years and will correspond to the City’s required payments to fund its pension and post-employment health benefits.

The following table represents the Districts portion of the unfunded obligations:

Balance at June 30, 2016	\$ 4,859,007
Actuarial adjustment	324,279
Payments	(655,450)
Balance at June 30, 2017	4,527,836
Less current portion	(720,831)
Balance due after one year	\$ 3,807,005

6. JOINT VENTURES

In October 1979, the District entered into a joint powers agreement with three neighboring sanitation agencies in central Marin County forming the Central Marin Sanitation Agency (CMSA). CMSA serves as a regional wastewater treatment plant for its four member agencies and San Quentin Prison (SQ) and is governed by a six-member Board of Commissioners, two appointed by the Board of Directors of the San Rafael Sanitation District (SRSD), two appointed by the governing board of Sanitary District No. 1 (SD 1), one appointed by the governing board of Sanitary District No. 2 (SD 2), and one appointed by the City Council of the City of Larkspur (Larkspur).

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

6. JOINT VENTURES (continued)

Total project costs for the joint venture were funded from federal (75%) and state (12.5%) clean water grants and from local shares (12.5% total) allocated among the member agencies and SQ based upon the weighted average of the strength and volume of sewage flows per member at inception of the project. Final individual local shares of total project costs were approximately \$7.6 million for SRSD, \$6.3 million for SD 1, \$1.6 million for SD 2, \$1 million for Larkspur, and \$1.4 million for SQ. CMSA derives its annual funding for its operations and capital programs almost exclusively from service charges to its member agencies. The joint powers agreement does not provide an explicit measurable right as required to establish an equity interest for any of the joint venture participants, and in addition to, stipulates that all excess capital funds, if any, and all excess administration, operations and maintenance funds from whatever source, if any, are the property of CMSA.

The financial statements of the Agency are available at the CMSA office. Condensed financial information for the Agency is presented below for June 30, 2016 and 2015, the most recent information available.

	<u>2016</u>	<u>2015</u>
Total assets	\$ 106,391,299	\$ 109,050,874
Deferred outflows of resources	2,092,186	936,613
Total liabilities	(60,370,523)	(62,387,928)
Deferred inflows of resources	<u>(2,487,504)</u>	<u>(2,254,404)</u>
Net position	<u>\$ 45,625,458</u>	<u>\$ 45,345,155</u>
Total revenues	\$ 16,952,527	\$ 17,873,113
Total expenses	(16,834,929)	(16,220,247)
Total contributions and adjustments	162,705	415,845
Prior period adjustment - GASB 68	-	<u>(7,278,030)</u>
Change in net position	<u>\$ 280,303</u>	<u>\$ (5,209,319)</u>

7. COMMITMENTS

As of June 30, 2017, SRSD had several contracts for sewer improvement projects with remaining obligations of approximately \$1,300,000, with the majority expected to be completed within the 2017/18 fiscal year.

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
FISCAL YEARS ENDED JUNE 30, 2017 AND 2016

8. RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees and natural disaster. The District participates in a joint powers agreement with other entities forming the California Sanitation Risk Management Authority (CSRMA), a public entity risk pool currently operating as a common risk management and insurance program for 60 member entities. CSRMA is governed by a Board of Directors composed of one representative from each member agency and meets three times per year in conjunction with conferences of the California Association of Sanitation Agencies. The Board controls the operations of CSRMA including selection of management and approval of operating budgets, independent of any influence by member entities.

The District pays annual premiums to CSRMA for its primary insurance and property insurance programs. Primary and property insurance programs are fully insured wherein CSRMA purchases insurance as a group thereby reducing its costs. CSRMA provides both fully insured and pooled insurance programs for its participating member entities. Because all employees of the District are contracted employees from the City of San Rafael, workers' compensation insurance is not carried by the District but is provided through the City.

The District's primary and property insurance programs transfer risk to commercial insurance policies for claims above deductibles, while the District retains risk for claims to the extent of deductibles. Settled claims for CSRMA have not exceeded coverage in any of the past three fiscal years.

The following summarizes active insurance policies as of June 30, 2017 together with coverage limits for each insured event:

Insurance Program	Limits	Coverage Description
CSRMA - Allied World Ins.	\$ 3,000,000	Gen/Mgt liability - aggregate
CSRMA - Allied World Ins.	\$ 1,000,000	Gen/Mgt liability - occurrence
CSRMA - Allied World Ins.	\$ 1,000,000	Auto liability - accident
CSRMA - Allied World Ins.	\$ 4,000,000	Excess liability
CSRMA - Public Entity Property Insurance Program (P.E.P.I.P)	\$ 12,157,866	Special form property
CSRMA - Illinois Union Ins.	\$ 25,000,000	Pollution liability - tier 1
CSRMA - Illinois Union Ins.	\$ 2,000,000	Pollution liability - tier 2
CSRMA - Lloyds of London	\$ 2,000,000	Cyber liability - third party
CSRMA - Lloyds of London	\$ 2,000,000	Cyber liability - first party
CSRMA - Travelers Ins.	\$ 25,000	Identity theft

SAN RAFAEL SANITATION DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
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8. RISK MANAGEMENT (continued)

The financial statements of CSRMA are available at their office: 100 Pine Street, 11th Floor, San Francisco, CA 94111. Condensed financial information for CSRMA is presented below for the years ended June 30, 2016 and 2015 (latest information available):

	<u>2016</u>	<u>2015</u>
Assets	\$ 28,336,567	\$ 27,418,098
Liabilities	<u>(16,735,609)</u>	<u>(16,714,638)</u>
Net assets	<u>\$ 11,600,958</u>	<u>\$ 10,703,460</u>
Revenues	\$ 11,843,583	\$ 10,895,632
Expenses	<u>(10,946,085)</u>	<u>(11,157,866)</u>
Increase (decrease) in net assets	<u>\$ 897,498</u>	<u>\$ (262,234)</u>

9. RELATED PARTY TRANSACTIONS

The District engages the City of San Rafael to provide the payroll, benefits and related administration for the District's personnel. They also provide the District with various vehicle repairs and other minor services. The City invoiced the District for approximately \$2,974,000 and \$3,076,000 for the years ended June 30, 2017 and 2016, respectively. These amounts included payments required pertaining to unfunded post-employment benefits for contract staff. See Note 5, Obligation to City of San Rafael, for a discussion regarding the contractual obligation between the District and the City of San Rafael.

The District had an obligation to the City of San Rafael for the years ended June 30, 2017 and 2016 of approximately \$32,000 and \$67,000, respectively. These are the result of various operating expenses and capital projects. The District also has a receivable from the City of San Rafael for the years ended June 30, 2017 and 2016 of approximately \$30,000 and \$16,000, respectively, which represents adjustments from payments of estimated amounts made during the year to actual costs as determined at year end.