

**SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY**

**BASIC FINANCIAL STATEMENTS**

**WITH REPORT ON AUDIT  
BY INDEPENDENT  
CERTIFIED PUBLIC ACCOUNTANTS**

**JUNE 30, 2017**

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

TABLE OF CONTENTS

June 30, 2017

	<u>Page Number</u>
Independent Auditors' Report	1 - 2
Basic Financial Statements:	
Statement of Net Position	3 - 4
Statement of Revenues, Expenses and Changes in Net Position	5
Statement of Cash Flows	6 - 7
Notes to the Basic Financial Statements	8 - 19
Supplementary Information:	20
Combining Statement of Net Position	21 - 22
Combining Statement of Revenues, Expenses and Changes in Net Position	23
Combining Statement of Cash Flows	24 - 25
Additional Schedules:	26
Analysis of Available Resources	27
Composition of Available Resources	28

## INDEPENDENT AUDITORS' REPORT

Board of Directors  
South County Regional  
Wastewater Authority  
Gilroy, California

We have audited the accompanying financial statements of the South County Regional Wastewater Authority (the Authority) as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Authority'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. 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 auditors consider internal control relevant to the Authority'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 Authority'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 basic financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of June 30, 2017 and the respective changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

## **Other Matters**

### *Required Supplementary Information*

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing 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. Our opinion on the basic financial statements is not affected by this missing information.

### *Other Information*

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Authority's basic financial statements. The combining statements and additional schedules, as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining statements are fairly stated in all material respects in relation to the basic financial statements as a whole.

The additional schedules have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

*White Nelson Dick Evans LLP*

Irvine, California  
January 18, 2018

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

STATEMENT OF NET POSITION

June 30, 2017

ASSETS:

Current assets:

Cash and cash equivalents (Note 2)	\$ 6,329,812
Accounts receivable	24,240
Due from City of Gilroy	727,250
Due from City of Morgan Hill	514,235
Due from other governments	13,203
	13,203

Total current assets	7,608,740
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Noncurrent assets:

Capital assets (Note 3):

Buildings and improvements	67,494,863
Land improvements	10,681,371
Infrastructure	12,758,116
Fleet (vehicles)	1,120,022
Office furniture, fixtures and equipment	13,736,386
Subtotal	105,790,758
Less: accumulated depreciation	(56,350,005)
Total capital assets being depreciated, net	49,440,753
Land	13,396,202
Construction in progress	34,470,740
	34,470,740

Total capital assets, net	97,307,695
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TOTAL ASSETS	104,916,435
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See accompanying notes to the basic financial statements.

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

STATEMENT OF NET POSITION  
(CONTINUED)

June 30, 2017

LIABILITIES:

Current liabilities:

Accounts payable	\$ 233,652
Retention payable	1,196,197
Due to City of Gilroy	460,287
Due to City of Morgan Hill	306,858
	306,858

Total current liabilities	2,196,994
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Noncurrent liabilities:

Compensated absences	22,953
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Total noncurrent liabilities	22,953
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TOTAL LIABILITIES	2,219,947
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NET POSITION:

Net investment in capital assets	97,307,695
Unrestricted	5,388,793

TOTAL NET POSITION	\$ 102,696,488
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See accompanying notes to the basic financial statements.

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

For the year ended June 30, 2017

OPERATING REVENUES:	
Operating contributions from City of Gilroy	\$ 5,190,414
Operating contributions from City of Morgan Hill	3,479,276
Other charges for services	31,569
	8,701,259
OPERATING EXPENSES:	
Sewage treatment	7,799,374
Pretreatment program	542,506
Plant operations	235,161
Depreciation	2,663,630
	11,240,671
TOTAL OPERATING REVENUES	
	8,701,259
OPERATING LOSS	
	(2,539,412)
NONOPERATING REVENUES:	
Rental income	87,500
Interest income	60,826
Miscellaneous income	7,172
	155,498
TOTAL NONOPERATING REVENUES	
	155,498
LOSS BEFORE CAPITAL CONTRIBUTIONS	
	(2,383,914)
CAPITAL CONTRIBUTIONS:	
Capital contribution from City of Gilroy	4,538,373
Capital contribution from City of Morgan Hill	3,076,881
	7,615,254
TOTAL CAPITAL CONTRIBUTIONS	
	7,615,254
CHANGE IN NET POSITION	
	5,231,340
NET POSITION AT BEGINNING OF YEAR	
	97,465,148
NET POSITION AT END OF YEAR	
	\$ 102,696,488

See accompanying notes to the basic financial statements.

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

STATEMENT OF CASH FLOWS

For the year ended June 30, 2017

CASH FLOWS FROM OPERATING ACTIVITIES:	
Cash received from system users	\$ 8,861,078
Rental income received	87,500
Miscellaneous income	7,172
Cash payments to suppliers for goods and services	(8,761,799)
Cash payments to employees for services	<u>(472,131)</u>
NET CASH USED BY OPERATING ACTIVITIES	<u>(278,180)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:	
Cash paid for capital assets	(7,474,189)
Capital contributions	<u>6,690,393</u>
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	<u>(783,796)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:	
Sale of investment	2,000,000
Interest received on investments	<u>60,826</u>
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>2,060,826</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	998,850
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>5,330,962</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u><u>\$ 6,329,812</u></u>

See accompanying notes to the basic financial statements.

(Continued)

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

COMBINING STATEMENT OF CASH FLOWS  
(CONTINUED)

For the year ended June 30, 2017

RECONCILIATION OF OPERATING LOSS TO NET

CASH USED BY OPERATING ACTIVITIES:

Operating loss	\$ (2,539,412)
Adjustments to reconcile operating loss to net cash used by operating activities:	
Depreciation	2,663,630
Rental income	87,500
Miscellaneous income	7,172
Changes in operating assets and liabilities:	
(Increase) decrease in accounts receivable	31,238
(Increase) decrease in due from City of Gilroy	222,375
(Increase) decrease in due from City of Morgan Hill	145,371
(Increase) decrease in due from other governments	(5,250)
Increase (decrease) in accounts and retention payable	(452,138)
Increase(decrease) in unearned revenue	(438,845)
Increase (decrease) in compensated absences	179
NET CASH USED BY OPERATING ACTIVITIES	\$ (278,180)

CASH AND CASH EQUIVALENTS -  
FINANCIAL STATEMENT CLASSIFICATION:

Current assets:	
Cash and cash equivalents	\$ 6,329,812
TOTAL CASH AND CASH EQUIVALENTS	\$ 6,329,812

There were no significant noncash financing, capital or investing transactions for the year ended June 30, 2017.

See accompanying notes to the basic financial statements.

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS

For the year ended June 30, 2017

1. REPORTING ENTITY AND SIGNIFICANT ACCOUNTING POLICIES:

The financial statements of the South County Regional Wastewater Authority (the Authority) have been prepared in accordance with generally accepted accounting principles (GAAP) as applied to local governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The significant accounting policies of the Authority are described below.

a. Description of Reporting Entity:

The Authority was created on July 1, 1992 by the City of Morgan Hill and the City of Gilroy (Member Agencies). The purpose of the Authority is to plan and implement regional solutions to the wastewater treatment and management problems resulting from the generation of wastewater within the service areas of the Member Agencies. To achieve this purpose, the Authority constructs, maintains and operates facilities for sewage treatment and wastewater reclamation. The City of Gilroy has a 58.1% ownership interest in the Authority. The City of Morgan Hill has a 41.9% ownership interest in the Authority.

The Authority is governed by a Board of Directors which consists of three members from the Gilroy City Council and two members from the Morgan Hill City Council.

The Authority is classified as a joint venture with respect to the two member agencies. The current agreement terminates the joint power agreement entered into in 1979 (the Agreement of 1979). Although the City of Gilroy controls three of the five members of the Board of Directors, the City of Gilroy does not have the ability to impose its will on the Authority beyond its representation on the Board. The Authority's budget and member contribution requirements are approved by the Board of Directors of the Authority. Although the City of Gilroy provides accounting services, engineering services, and administrative support to the Authority, day-to-day operations associated with the Authority have been contracted directly by the Authority to a private provider of services for wastewater management and operations.

b. Basic Financial Statements:

The basic financial statements are comprised of the Statement of Net Position, the Statement of Revenues, Expenses and Changes in Net Position, the Statement of Cash Flows and the notes to the basic financial statements.

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

1. REPORTING ENTITY AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

c. Measurement Focus, Basis of Accounting and Financial Statement Presentation:

The Authority is accounted for as an enterprise fund (proprietary fund type). A fund is an accounting entity with a self-balancing set of accounts established to record the financial position and results of operations of a specific governmental activity. The activities of enterprise funds closely resemble those of ongoing businesses in which the purpose is to conserve and add to basic resources while meeting operating expenses from current revenues. Enterprise funds account for operations that provide services on a continuous basis and are substantially financed by revenues derived from user charges. The Authority utilizes the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized as they are incurred. Internal activity has been eliminated in the accompanying financial statements.

The Authority distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with sewer operations. The principal operating revenues of the Authority are contributions from Member Agencies. Operating expenses include cost of services, general and administrative expenses and depreciation of capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Net position of the Authority has been reported as restricted when its use is constrained more narrowly than the reporting unit in which it is reported as a result of state laws governing such use. When both restricted and unrestricted resources are available for use, the Authority uses restricted resources first, then unrestricted resources as they are needed. For capital expenditures, legally available restricted bond proceeds are used first, then other restricted resources, then unrestricted resources are used if needed.

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

1. REPORTING ENTITY AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

d. New Accounting Pronouncements:

**Current Year Standards:**

GASB 74 - *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, effective for periods beginning after June 15, 2016, and did not impact the Authority.

GASB 77 - *Tax Abatement Disclosure*, effective for periods beginning after December 15, 2015, and did not impact the Authority.

GASB 79 - *Certain External Investment Pools and Pool Participants*, contains certain provisions on portfolio quality, custodial credit risk, and shadow pricing, effective for periods beginning after December 15, 2015, and did not impact the Authority.

GASB 80 - *Blending Requirements for Certain Component Units*, effective for periods beginning after June 15, 2016, and did not impact the Authority.

**Pending Accounting Standards:**

GASB has issued the following statements, which may impact the Authority's financial reporting requirements in the future:

- GASB 75 - *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, effective for periods beginning after June 15, 2017.
- GASB 82 - *Pension Issues*, effective for periods beginning after June 15, 2016, except for certain provisions on selection of assumptions, which are effective in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017.
- GASB 84 - *Fiduciary Activities*, effective for periods beginning after December 15, 2018.
- GASB 85 - *Omnibus 2017*, effective for periods beginning after June 15, 2017.
- GASB 86 - *Certain Debt Extinguishment Issues*, effective for periods beginning after June 15, 2017.
- GASB 87 - *Leases*, effective for periods beginning after December 15, 2019.

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

1. REPORTING ENTITY AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

e. Deferred Outflows/Inflows of Resources:

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to future periods and so will not be recognized as an outflow of resources (expense) until that time. The Authority has no deferred outflows of resources.

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of net position that applies to future periods and so will not be recognized as an inflow of resources (revenue) until that time. The Authority has no deferred inflows of resources.

f. Operating Contributions:

Operating contributions from the members are recognized when the related operating costs are incurred. Members are billed amounts equal to the actual operating expenses incurred less other revenues including contributions from nonmember users.

g. Capital Contributions:

In accordance with generally accepted accounting principles for local governmental units, the Authority has recorded the following transactions as capital contributions:

- Capital grants and other contributions from third parties restricted for property, plant, and equipment.
- Cash contributed from members for property, plant, and equipment.

h. Balances Due To/From Member Agencies:

Balances shown as due to/from agencies represent each member's over/under payment towards the funding of current year operations and plant construction.

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

1. REPORTING ENTITY AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

i. Capital Assets:

Property, plant, and equipment purchases greater than \$10,000 are capitalized at original acquisition cost or estimated acquisition cost. Donated capital assets are recorded at their estimated fair market value at the date of donation. Capital assets acquired under capital leases are recorded at the net present value of the total lease payments. Depreciation is charged to operations, using a straight-line method, based on the estimated useful life of the assets. The estimated useful lives of the assets are as follows:

Furniture and fixtures	10 to 20 years
Vehicles	8 years
Machinery and equipment	5 to 25 years
Treatment plant	40 years
Buildings	40 years
Sewer lines	50 years
Land improvements	50 years

j. Investments:

Investments are reported in the accompanying Statement of Net Position at fair value.

Changes in fair value that occur during the fiscal year are recognized as *increase (decrease) in fair value of investments* reported for that fiscal year. *Interest income* includes interest earnings, and any gains or losses realized upon the liquidation or sale of investments.

k. Cash Equivalents:

For purposes of the statement of cash flows, cash represents funds that effectively may be withdrawn at any time without prior notice of penalty (such as demand deposits and mutual funds). Cash equivalents are investments that are short-term and highly liquid and that are both readily convertible to known amounts of cash and so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. Cash equivalents have an original maturity date of three months or less from the date of purchase.

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

1. REPORTING ENTITY AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

1. Use of Estimates:

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

2. CASH AND INVESTMENTS:

**Cash and Investments:**

Cash and investments as of June 30, 2017 are classified in the accompanying financial statements as follows:

Statement of Net Position:

Current Assets:

Cash and cash equivalents	\$ <u>6,329,812</u>
Total cash and investments	\$ <u><u>6,329,812</u></u>

Cash and investments as of June 30, 2017 consisted of the following:

Equity in City of Gilroy investment pool	\$ 20,574
Investments	<u>6,309,238</u>
Total cash and investments	\$ <u><u>6,329,812</u></u>

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

2. CASH AND INVESTMENTS (CONTINUED):

**Investments Authorized by the California Government Code and the Authority's Investment Policy:**

The table below identifies the investment types that are authorized for the Authority by the California Government Code and the Authority's investment policy. The table also identifies certain provisions of the California Government Code (or the Authority's investment policy, if more restrictive) that address interest rate risk, credit risk, and concentration of credit risk. This table does not address investments of debt proceeds with fiscal agent that are governed by the provisions of debt agreements of the Authority, rather than the general provisions of the California Government Code or the Authority's investment policy.

Investment Types <u>Authorized by State Law</u>	Authorized by Investment <u>Policy</u>	Maximum Maturity*	Maximum Percentage of Portfolio*	Maximum Investment in One Issuer*
Local Agency Bonds	Yes	5 years	None	None
U.S. Treasury Obligations	Yes	2 years	None	None
U.S. Government Sponsored Agency Securities	Yes	5 years	None	None
Banker's Acceptances	No	180 days	40%	30%
Commercial Paper	No	270 days	25%	10%
Negotiable Certificates of Deposit	Yes	2 years	30%	None
Repurchase Agreements	No	1 year	None	None
Reverse Repurchase Agreements	No	92 days	20% of base value	None
Medium-Term Notes	No	5 years	30%	None
Mutual Funds	Yes	N/A	20%	10%
Money Market Mutual Funds	Yes	N/A	20%	10%
Mortgage Pass-Through Securities	Yes	5 years	20%	None
County Pooled Investment Funds	Yes	N/A	None	None
Local Agency Investment Fund	Yes	N/A	None	None
JPA Pools (other investment pools)	Yes	N/A	None	None

\* Based on state law requirements or investment policy requirements, whichever is more restrictive.

N/A - Not Applicable

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

2. CASH AND INVESTMENTS (CONTINUED):

**Disclosures Relating to Interest Rate Risk:**

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

Information about the sensitivity of the fair values of the Authority's investments to market interest rate fluctuations is provided by the following table that shows the distribution of the Authority's investments by maturity:

Investment Type	Remaining Maturity (in Months) 12 Months or Less
Equity in City of Gilroy investment pool	\$ 20,574
Local Agency Investment Fund	6,309,238
	\$ 6,329,812

**Disclosures Relating to Credit Risk:**

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the minimum rating required by (where applicable) the California Government Code, or the Authority's investment policy, and the actual rating by Standard & Poor's as of year end for each investment type.

Investment Type	Minimum Legal Rating	Total as of June 30, 2017	Not Rated
Equity in City of Gilroy investment pool	N/A	\$ 20,574	\$ 20,574
Local Agency Investment Fund	N/A	6,309,238	6,309,238
		\$ 6,329,812	\$ 6,329,812

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

2. CASH AND INVESTMENTS (CONTINUED):

**Concentration of Credit Risk:**

The investment policy of the Authority contains no limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code. There are no investments in any one issuer (other than U.S. Treasury securities, mutual funds, and external investment pools) that represent 5% or more of total Authority investments.

**Custodial Credit Risk:**

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. 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.

**Investment in State Investment Pool:**

The Authority is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by the California Government Code under the oversight of the Treasurer of the State of California. The fair value of the Authority's investment in this pool is reported in the accompanying financial statements at amounts based upon the Authority's pro rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis. LAIF is not rated.

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

2. CASH AND INVESTMENTS (CONTINUED):

**Equity in Cash and Investment Pool of the City of Gilroy:**

The Authority does not have a separate bank account; however, the Authority's cash and investments are maintained in an investment pool managed by the City. The Authority is a voluntary participant in that pool. This pool is governed by and under the regulatory oversight of the Investment Policy adopted by the City Council of the City. The fair value of the Authority's investment in this pool is reported in the accompanying financial statements at amounts based upon the Authority's pro rata share of the fair value calculated by the City for the entire City portfolio. The balance available for withdrawal is based on the accounting records maintained by the City, which are recorded on an original cost basis. At June 30, 2017, the Authority had a cash balance of \$20,574.

**Fair Value Measurements:**

The Authority categorizes its fair value measurement within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the assets. Level 1 inputs are quoted prices in active markets for identical assets, Level 2 inputs are significant other observable inputs, and Level 3 inputs are significant unobservable inputs.

The Authority's investments in Equity in City of Gilroy investment pool and LAIF are not subject to the fair value measurement hierarchy.

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

3. CAPITAL ASSETS:

Capital asset activity for the year ended June 30, 2017 is as follows:

	Beginning Balance <u>July 1, 2016</u>	Additions	Deletions	Ending Balance <u>June 30, 2017</u>
Capital assets, not being depreciated:				
Land	\$ 13,396,202	\$ -	\$ -	\$ 13,396,202
Construction in progress	<u>27,028,351</u>	<u>7,442,389</u>	<u>-</u>	<u>34,470,740</u>
Total capital assets, not being depreciated	<u>40,424,553</u>	<u>7,442,389</u>	<u>-</u>	<u>47,866,942</u>
Capital assets, being depreciated:				
Buildings and improvements	67,494,863	-	-	67,494,863
Land improvements	10,681,371	-	-	10,681,371
Infrastructure	12,758,116	-	-	12,758,116
Fleet (vehicles)	1,088,223	31,799	-	1,120,022
Office furniture and equipment	<u>13,736,386</u>	<u>-</u>	<u>-</u>	<u>13,736,386</u>
Total capital assets, being depreciated	<u>105,758,959</u>	<u>31,799</u>	<u>-</u>	<u>105,790,758</u>
Less accumulated depreciation for:				
Buildings and improvements	(32,947,632)	(1,704,691)	-	(34,652,323)
Land improvements	(4,956,212)	(190,341)	-	(5,146,553)
Infrastructure	(3,808,676)	(295,411)	-	(4,104,087)
Fleet (vehicles)	(977,517)	(44,163)	-	(1,021,680)
Office furniture and equipment	<u>(10,996,338)</u>	<u>(429,024)</u>	<u>-</u>	<u>(11,425,362)</u>
Total accumulated depreciation	<u>(53,686,375)</u>	<u>(2,663,630)</u>	<u>-</u>	<u>(56,350,005)</u>
Total capital assets being depreciated, net	<u>52,072,584</u>	<u>(2,631,831)</u>	<u>-</u>	<u>49,440,753</u>
Total capital assets, net	<u>\$ 92,497,137</u>	<u>\$ 4,810,558</u>	<u>\$ -</u>	<u>\$ 97,307,695</u>

Depreciation expense was \$2,663,630 for the year ended June 30, 2017.

SOUTH COUNTY REGIONAL  
WASTEWATER AUTHORITY

NOTES TO THE BASIC FINANCIAL STATEMENTS  
(CONTINUED)

For the year ended June 30, 2017

5. SUBSEQUENT EVENTS:

Events occurring after June 30, 2017 have been evaluated for possible adjustments to the financial statements or disclosure as of January 18, 2018, which is the date these financial statements were available to be issued.

**SUPPLEMENTARY INFORMATION**

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

COMBINING STATEMENT OF NET POSITION

June 30, 2017

	Plant Construction	Sewage Treatment Operations	Totals
<b>ASSETS:</b>			
Current assets:			
Cash and cash equivalents	\$ -	\$ 6,329,812	\$ 6,329,812
Accounts receivable	-	24,240	24,240
Due from City of Gilroy	539,430	187,820	727,250
Due from City of Morgan Hill	389,021	125,214	514,235
Due from other governments	-	13,203	13,203
Due from other funds	-	950,458	950,458
<b>Total current assets</b>	<b>928,451</b>	<b>7,630,747</b>	<b>8,559,198</b>
Noncurrent assets:			
Capital assets:			
Buildings and improvements	-	67,494,863	67,494,863
Land improvements	-	10,681,371	10,681,371
Infrastructure	-	12,758,116	12,758,116
Fleet (vehicles)	-	1,120,022	1,120,022
Office furniture, fixtures and equipment	-	13,736,386	13,736,386
Subtotal	-	105,790,758	105,790,758
Less: accumulated depreciation	-	(56,350,005)	(56,350,005)
Total capital assets being depreciated, net	-	49,440,753	49,440,753
Land	-	13,396,202	13,396,202
Construction in progress	12,423,227	22,047,513	34,470,740
<b>Total capital assets, net</b>	<b>12,423,227</b>	<b>84,884,468</b>	<b>97,307,695</b>
<b>TOTAL ASSETS</b>	<b>13,351,678</b>	<b>92,515,215</b>	<b>105,866,893</b>

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

COMBINING STATEMENT OF NET POSITION  
(CONTINUED)

June 30, 2017

	Plant Construction	Sewage Treatment Operations	Totals
<b>LIABILITIES:</b>			
Current liabilities:			
Accounts payable	\$ -	\$ 233,652	\$ 233,652
Retention payable	186,212	1,009,985	1,196,197
Due to City of Gilroy	-	460,287	460,287
Due to City of Morgan Hill	-	306,858	306,858
Due to other funds	950,458	-	950,458
Total current liabilities	1,136,670	2,010,782	3,147,452
Noncurrent liabilities:			
Compensated absences	-	22,953	22,953
Total noncurrent liabilities	-	22,953	22,953
TOTAL LIABILITIES	1,136,670	2,033,735	3,170,405
<b>NET POSITION:</b>			
Net investment in capital assets	12,423,227	84,884,468	97,307,695
Unrestricted	(208,219)	5,597,012	5,388,793
TOTAL NET POSITION	\$ 12,215,008	\$ 90,481,480	\$ 102,696,488

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

COMBINING STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

For the year ended June 30, 2017

	Plant Construction	Sewage Treatment Operations	Totals
<b>OPERATING REVENUES:</b>			
Operating contributions from City of Gilroy	\$ -	\$ 5,190,414	\$ 5,190,414
Operating contributions from City of Morgan Hill	-	3,479,276	3,479,276
Other charges for services	-	31,569	31,569
<b>TOTAL OPERATING REVENUES</b>	<b>-</b>	<b>8,701,259</b>	<b>8,701,259</b>
<b>OPERATING EXPENSES:</b>			
Sewage treatment	-	7,799,374	7,799,374
Pretreatment program	-	542,506	542,506
Plant operations	-	235,161	235,161
Depreciation	-	2,663,630	2,663,630
<b>TOTAL OPERATING EXPENSES</b>	<b>-</b>	<b>11,240,671</b>	<b>11,240,671</b>
<b>OPERATING LOSS</b>	<b>-</b>	<b>(2,539,412)</b>	<b>(2,539,412)</b>
<b>NONOPERATING REVENUES (EXPENSES):</b>			
Rental income	-	87,500	87,500
Interest income	-	60,826	60,826
Miscellaneous income (expense)	(8,209)	15,381	7,172
<b>TOTAL NONOPERATING REVENUES (EXPENSES)</b>	<b>(8,209)</b>	<b>163,707</b>	<b>155,498</b>
<b>LOSS BEFORE CAPITAL CONTRIBUTIONS</b>	<b>(8,209)</b>	<b>(2,375,705)</b>	<b>(2,383,914)</b>
<b>CAPITAL CONTRIBUTIONS:</b>			
Capital contribution from City of Gilroy	941,206	3,597,167	4,538,373
Capital contribution from City of Morgan Hill	678,770	2,398,111	3,076,881
<b>TOTAL CAPITAL CONTRIBUTIONS</b>	<b>1,619,976</b>	<b>5,995,278</b>	<b>7,615,254</b>
<b>CHANGE IN NET POSITION</b>	<b>1,611,767</b>	<b>3,619,573</b>	<b>5,231,340</b>
<b>NET POSITION AT BEGINNING OF YEAR</b>	<b>10,603,241</b>	<b>86,861,907</b>	<b>97,465,148</b>
<b>NET POSITION AT END OF YEAR</b>	<b>\$ 12,215,008</b>	<b>\$ 90,481,480</b>	<b>\$ 102,696,488</b>

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

COMBINING STATEMENT OF CASH FLOWS

For the year ended June 30, 2017

	Plant Construction	Sewage Treatment Operations	Totals
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Cash received from system users	\$ -	\$ 8,861,078	\$ 8,861,078
Rental income received	-	87,500	87,500
Miscellaneous income (expense)	(8,209)	15,381	7,172
Cash payments to suppliers for goods and services	(333,699)	(8,428,100)	(8,761,799)
Cash payments to employees for services	-	(472,131)	(472,131)
	<b>NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES</b>	<b>63,728</b>	<b>(278,180)</b>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:</b>			
Cash received from/(paid to) other funds	950,458	(950,458)	-
	<b>NET CASH PROVIDED (USED) BY NONCAPITAL FINANCING ACTIVITIES</b>	<b>(950,458)</b>	<b>-</b>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>			
Cash paid for capital assets	(1,556,069)	(5,918,120)	(7,474,189)
Capital contributions	695,115	5,995,278	6,690,393
	<b>NET CASH PROVIDED (USED) BY CAPITAL AND RELATED FINANCING ACTIVITIES</b>	<b>77,158</b>	<b>(783,796)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Sale of investment	-	2,000,000	2,000,000
Interest received on investments	-	60,826	60,826
	<b>NET CASH PROVIDED BY INVESTING ACTIVITIES</b>	<b>2,060,826</b>	<b>2,060,826</b>
	<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>1,251,254</b>	<b>998,850</b>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	<b>252,404</b>	<b>5,078,558</b>	<b>5,330,962</b>
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<b>\$ -</b>	<b>\$ 6,329,812</b>	<b>\$ 6,329,812</b>

(Continued)

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

COMBINING STATEMENT OF CASH FLOWS  
(CONTINUED)

For the year ended June 30, 2017

	Plant Construction	Sewage Treatment Operations	Totals
<b>RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:</b>			
Operating loss	\$ -	\$ (2,539,412)	\$ (2,539,412)
Adjustments to reconcile operating loss to net cash provided (used) by operating activities:			
Depreciation	-	2,663,630	2,663,630
Rental income	-	87,500	87,500
Miscellaneous income (expense)	(8,209)	15,381	7,172
Changes in operating assets and liabilities:			
(Increase) decrease in accounts receivable	-	31,238	31,238
(Increase) decrease in due from City of Gilroy	-	222,375	222,375
(Increase) decrease in due from City of Morgan Hill	-	145,371	145,371
(Increase) decrease in due from other governments	-	(5,250)	(5,250)
Increase (decrease) in accounts and retention payable	(128,769)	(323,369)	(452,138)
Increase (decrease) in unearned revenue	(204,930)	(233,915)	(438,845)
Increase (decrease) in compensated absences	-	179	179
	<u>          -</u>	<u>          179</u>	<u>          179</u>
 NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	<u>\$ (341,908)</u>	<u>\$ 63,728</u>	<u>\$ (278,180)</u>
 <b>CASH AND CASH EQUIVALENTS - FINANCIAL STATEMENT CLASSIFICATION:</b>			
Current assets:			
Cash and cash equivalents	\$ -	\$ 6,329,812	\$ 6,329,812
 TOTAL CASH AND CASH EQUIVALENTS	<u>\$ -</u>	<u>\$ 6,329,812</u>	<u>\$ 6,329,812</u>

**ADDITIONAL SCHEDULES**

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

ANALYSIS OF AVAILABLE RESOURCES

For the year ended June 30, 2017

	<u>Plant Construction</u>	<u>Sewage Treatment Operations</u>	<u>Totals</u>
<b>BEGINNING RESOURCES AVAILABLE:</b>			
Operating reserve	\$ (263,917)	\$ 5,231,928	\$ 4,968,011
<b>TOTAL BEGINNING RESOURCES</b>	<u>(263,917)</u>	<u>5,231,928</u>	<u>4,968,011</u>
<b>SOURCE OF FUNDS (WORKING CAPITAL):</b>			
Revenues	-	8,804,140	8,804,140
Investment income	-	60,826	60,826
Member capital contributions	1,619,976	5,995,278	7,615,254
<b>TOTAL SOURCES</b>	<u>1,619,976</u>	<u>14,860,244</u>	<u>16,480,220</u>
<b>USE OF FUNDS (WORKING CAPITAL):</b>			
Expenses (excluding depreciation)	8,209	8,577,041	8,585,250
Capital expenditures incurred	1,556,069	5,918,120	7,474,189
<b>TOTAL USES</b>	<u>1,564,278</u>	<u>14,495,161</u>	<u>16,059,439</u>
<b>ADJUSTMENTS:</b>			
Adjustments for other assets and liabilities		113,675	113,675
<b>TOTAL ADJUSTMENTS</b>	<u>-</u>	<u>113,675</u>	<u>113,675</u>
<b>TOTAL CHANGES IN RESOURCES</b>	<u>55,698</u>	<u>478,758</u>	<u>534,456</u>
<b>ENDING RESOURCES AVAILABLE</b>	<u>\$ (208,219)</u>	<u>\$ 5,710,686</u>	<u>\$ 5,502,467</u>
<b>RECAP OF ENDING RESOURCES:</b>			
Operating reserve	<u>\$ (208,219)</u>	<u>\$ 5,710,686</u>	<u>\$ 5,502,467</u>
<b>TOTAL ENDING RESOURCES</b>	<u>\$ (208,219)</u>	<u>\$ 5,710,686</u>	<u>\$ 5,502,467</u>

SOUTH COUNTY REGIONAL WASTEWATER AUTHORITY

COMPOSITION OF AVAILABLE RESOURCES

For the year ended June 30, 2017

	Plant Construction	Sewage Treatment Operations	Totals
<b>BEGINNING RESOURCES AVAILABLE:</b>			
Cash	\$ 252,404	\$ 7,078,558	\$ 7,330,962
Receivables	3,590	63,430	67,020
Payables	(519,911)	(1,910,060)	(2,429,971)
TOTAL BEGINNING RESOURCES	\$ (263,917)	\$ 5,231,928	\$ 4,968,011
<b>ENDING RESOURCES AVAILABLE:</b>			
Cash	\$ -	\$ 6,329,812	\$ 6,329,812
Receivables	928,451	1,290,934	2,219,385
Payables	(1,136,670)	(1,910,060)	(3,046,730)
TOTAL ENDING RESOURCES	\$ (208,219)	\$ 5,710,686	\$ 5,502,467