

**NORTHERN ORANGE COUNTY
SELF-FUNDED WORKERS'
COMPENSATION AGENCY**

ANNUAL FINANCIAL REPORT

JUNE 30, 2018 AND 2017

**NORTHERN ORANGE COUNTY SELF-FUNDED WORKERS' COMPENSATION AGENCY
(A Joint Powers Entity)**

COSTA MESA, CALIFORNIA

JUNE 30, 2018

BOARD OF DIRECTORS

<u>REPRESENTATIVE</u>	<u>MEMBER</u>	<u>OFFICE</u>
Kathleen Thomason	Greater Anaheim Special Education Local Plan Area	<u>President</u>
Eric Fano	Savanna School District	Vice President
Lynn Simmons	Coastline Regional Occupational Program	Secretary/Treasurer
Rick Holash	Buena Park School District	Member
Tim McLellan	Cypress School District	Member
Carol Argomaniz	La Habra City School District	Member
Nancy Nien	Los Alamitos Unified School District	Member
Cheryl Blount	Magnolia School District	Member
Tonia Watkins	North Orange County Regional Occupational Program	Member
Scott Martin	Centralia School District	Member
Cindy Fox	College and Career Advantage	Member
Tony Wold	Westminster School District	Member

**NORTHERN ORANGE COUNTY SELF-FUNDED
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JUNE 30, 2018 AND 2017**

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FINANCIAL SECTION



VAVRINEK, TRINE, DAY & CO., LLP
Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Northern Orange County Self-Funded Workers' Compensation Agency
Costa Mesa, California

Report on the Financial Statements

We have audited the accompanying financial statements of the Northern Orange County Self-Funded Workers' Compensation Agency (the Agency) as of and for the years ended June 30, 2018 and 2017, and the related notes to the financial statements, which collectively comprise the Agency'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.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America, the State Controller's *Minimum Audit Requirements for California Special Districts*, 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 auditor's 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 Agency'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 Agency'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.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Northern Orange County Self-Funded Workers' Compensation Agency, as of June 30, 2018 and 2017, and the respective 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 on pages 3 through 12, 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 26, 2018, on our consideration of the Northern Orange County Self-Funded Workers' Compensation Agency'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 solely 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 the effectiveness of Northern Orange County self-Funded Workers' Compensation Agency's 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 Northern Orange County Self-Funded Workers' Compensation Agency's internal control over financial reporting and compliance.

Varrinck, Trine, Day & Co., LLP

Rancho Cucamonga, California
September 26, 2018

**NORTHERN ORANGE COUNTY SELF-FUNDED
WORKERS' COMPENSATION AGENCY
(A Joint Powers Entity)**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2018 AND 2017**

This discussion and analysis provides an overview of the financial condition of Northern Orange County Self-Funded Workers' Compensation Agency (NOCSFWCA) for the fiscal years ended June 30, 2018 and June 30, 2017. It discusses NOCSFWCA's financial operations and analyzes the significant financial changes from the prior year. Readers should review the financial management information report and the independent financial audit in conjunction with this report to enhance their understanding of NOCSFWCA's financial performance.

Introduction and Background:

NOCSFWCA is a public risk sharing pool established pursuant to a Joint Power Agreement effective October 1, 1977, to self-fund workers' compensation. Participation in NOCSFWCA gives members the advantage of pooled member contributions, sharing of claim liability risk and purchase of insurance at a lower cost. NOCSFWCA's membership consists of 12 individual member districts, from the Northern Orange County area. A Full Board of Directors comprised of one representative from each member governs NOCSFWCA. Each member has one vote. The Board elects from its members, a President, Vice President, Secretary, and Treasurer.

NOCSFWCA is able to retain a degree of control over their rate structure adding to the stability and longevity of their program. NOCSFWCA operates on a fiscal/program year from July 1st through June 30th with each program year operating separately from every other program year. By tracking financial activity by program year, only the members participating in a given program year will receive rebates or assessments. Further, other items such as administrative expenses and investment revenue can be accurately allocated to the proper program year's pooled equity or deficit.

Since its inception, NOCSFWCA has been proactive in controlling its costs by developing a comprehensive risk management program and safety credit reimbursement plan. The purpose of the reimbursement plan is to provide a fund for each member to designate their portion of rebates and additional contributions. This fund is then utilized at the discretion of the members for reimbursement and implementation of various safety and loss control programs within their districts.

Accredited with excellence by the California Association of Joint Powers Authorities (CAJPA), NOCSFWCA has maintained a high level of performance, member satisfaction, and fiscal stewardship among organizations of its kind.

Mission Statement:

"The mission of Northern Orange County Self-Funded Workers' Compensation Agency is to protect the members financial resources exposed to workers' compensation losses. Through its collective resources the authority will provide risk management and loss control services to assist in the reduction of claims with the goal of providing a safe work environment."

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Program Structure:

NOCSFWCA participated in SAWCX II from 1988-1989 to 1994-1995 for its excess coverage in the self-insured program years. As a member of SAWCX II, they paid an annual member contribution based upon their Self-Insured Retention (SIR) and shared in all rebates or deficits proportionate to their participation. On a biannual basis SAWCX II performs an actuarial review to analyze estimated ultimate incurred loss costs. Based upon increases in actuarial estimates, the Board of Directors has taken action to assess the current and former members of SAWCX II for deficit program years.

On July 1, 1995, NOCSFWCA took advantage of the insurance market and the lower rate structure by selecting a fully insured program that existed until June 30, 2003. In program year 2003-2004, NOCSFWCA joined as a member of the Protected Insurance Program for Schools (PIPS) under a Finite Risk Sharing program that utilizes reinsurance and continued as a member through 2017-2018.

Financial Management and Control:

NOCSFWCA is responsible for establishing and maintaining an internal control structure designed to ensure that assets are protected from loss, theft, or misuse and to ensure that adequate accounting data are compiled to allow for preparation of financial statements in conformity with generally accepted accounting principles (GAAP).

NOCSFWCA has contracted with Keenan & Associates for administrative management responsibilities. These services include ensuring that NOCSFWCA meets its commitment to the members for operational efficiency, organizational integrity and for implementing policies established by the Board of Directors as set forth in organizational documents and bylaws. Service Enhancement Technologies (SETECH), a Division of Keenan & Associates, provides financial management and financial reporting to the Board. Budgetary control is provided by verification of budgeted amounts before expenses and the continued analysis of all account totals compared to budgeted amounts. Detailed financial statements and Treasurer's Reports include budget-to-actual comparisons and are provided to the NOCSFWCA Board on a quarterly basis. A comprehensive financial management information report is provided semi-annually and is the basis for the independent financial audit.

NOCSFWCA has also contracted with Bay Actuarial Consultants to provide an independent actuarial review of the overall program. This is the basis for the Claim Liabilities reflected on the Statement of Net Position and in compliance with GASB Statement No. 10. Vavrinek, Trine, Day & Co., LLP, Certified Public Accountants, performs an independent audit examination of the financial statements in accordance with generally accepted auditing standards on an annual basis.

Basic Financial Statements:

NOCSFWCA's financial statements are prepared in conformity with generally accepted accounting principles and necessarily include amounts based upon reliable estimates and judgments. The financial statements include the Statement of Net Position, Statements of Revenues, Expenses, and Changes in Net Position, and Statement of Cash Flows.

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**MANAGEMENT'S DISCUSSION AND ANALYSIS
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The Statement of Net Position provides information on NOCSFWCA's program assets and liabilities, with the difference reported as Net Position. The Statement of Revenues, Expenses, and Changes in Net Position, presents information showing total operating revenue versus operating expenses for fiscal years 2017-2018 and 2016-2017 and the resulting effect on Net Position. The Statement of Cash Flows provides a reconciliation of the change during the fiscal year 2017-2018 in cash and cash equivalents.

NOCSFWCA calculates the financial position of each program year on the basis that each year stands on its own. Specifically, the funding determined necessary for each claim year is collected in that claim year, and all liabilities and expenses of each claim year are accounted for in the year they are incurred. At the close of each year, an evaluation of the Net Position of individual program years is conducted, and any funds remaining after taking into account outstanding liabilities and other obligations, are considered eligible for return to members in accordance with NOCSFWCA's Capital Target Policy adopted on June 24, 2015 and reviewed annually. Over NOCSFWCA's 41 years of operation, it has declared and returned net member experience rebates of \$10,249,621.

FINANCIAL ANALYSIS

Condensed Statement of Net Position:

Below is a summary of the Statement of Net Position showing total assets versus total liabilities with a percentage of change from the 2016-2017 to the 2017-2018 program year.

	As of June 30,			
	2018	2017	Difference	Percentage
Current Assets				
Deposits and Investments	\$ 1,979,041	\$ 1,855,580	\$ 123,461	6.65 %
Other Assets	7,318	42,423	(35,105)	(82.75)
Total Assets	<u>1,986,359</u>	<u>1,898,003</u>	<u>88,356</u>	<u>4.66</u>
Current Liabilities				
Accounts Payable and Due to Members	1,303,554	1,214,989	88,565	7.29
Claim Liabilities and ULAE	21,000	21,000	-	-
Total Current Liabilities	<u>1,324,554</u>	<u>1,235,989</u>	<u>88,565</u>	<u>7.17</u>
Noncurrent Liabilities				
Claim Liabilities and ULAE	242,368	271,722	(29,354)	(10.80)
Total Liabilities	<u>1,566,922</u>	<u>1,507,711</u>	<u>59,211</u>	<u>3.93</u>
Net Position				
Undesignated	(88,410)	(107,266)	18,856	(17.58)
Designated - Capital Target	507,847	497,558	10,289	2.07
Total Net Position	<u>\$ 419,437</u>	<u>\$ 390,292</u>	<u>\$ 29,145</u>	<u>7.47 %</u>

**NORTHERN ORANGE COUNTY SELF-FUNDED
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**MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2018 AND 2017**

Assets:

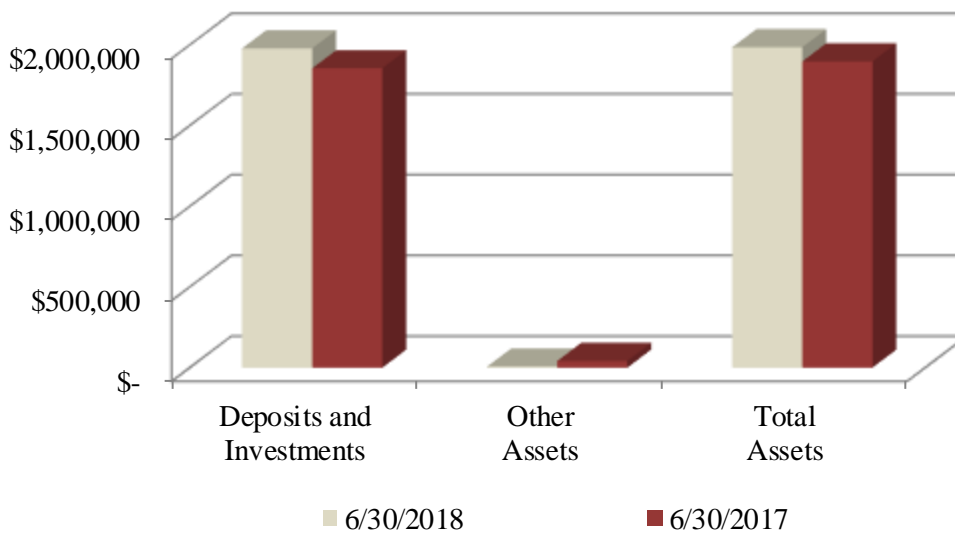
The overall assets of NOCSFWCA increased in 2017-2018 by \$88,356 or 4.66 percent, which is largely attributed to:

- Net Investment income of \$18,574
- Net cash activity in the Safety Credit program in the amount of \$180,844

Offset by:

- Change in accounts payable of \$1,858
- Net cash activity in the Due to Members program in the amount of \$90,921
- Administrative expenditures above budget of \$12,069

This increase in assets can be seen below:



The funds not necessary for the payment of claims are invested in the Orange County Treasury. Those assets needed for current operations are maintained with the State of California Local Agency Investment Fund (L.A.I.F.) and Union Bank general and claim checking accounts.

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**MANAGEMENT'S DISCUSSION AND ANALYSIS
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Liabilities:

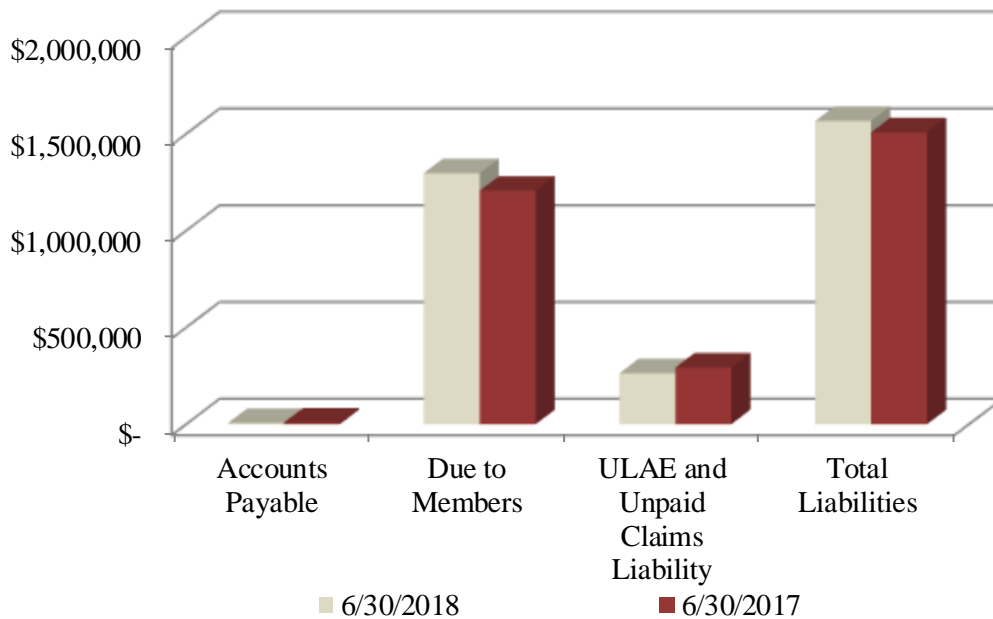
The overall liabilities of NOCSFWCA increased in 2017-2018 by \$59,211 or 3.93 percent, which is mainly attributed to:

- Net activity in the Safety Credit program in the amount of \$181,344

Offset by:

- A decrease in estimated ultimate incurred of \$24,303 for the self-insured program year 1994-1995 and prior, based on the actuarial study dated March 2018
- Net change in accounts payable of \$1,858
- Net activity in the Due to Members and Unearned Revenue for a net of \$90,921

This increase in liabilities can be seen below:



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Fund Net Position:

NOCSFWCA's Net Position of \$419,437 is below the capital target and reflects an actuarially-determined greater than 90 percent probability level funding of its outstanding liabilities. A 90 percent probability level funding means that there is only a 10 percent probability that the outstanding liability is higher or lower than the actuary's best estimate. Most actuarial funding recommendations are at the 70 percent probability level, therefore, NOCSFWCA's financial position provides an increased probability of overall reserve adequacy. Probability level funding recommendations based upon the Bay Actuarial Consultants actuarial study dated March 2018 are:

- 80% probability level \$193,983
- 90% probability level \$357,847

In order to prevent premature release of the Net Position, NOCSFWCA has adopted a capital target policy that is reviewed annually. The capital target is set at an actuarially determined contingency margin at 90 percent probability level plus an additional \$150,000 as approved at the June 24, 2015 Board of Directors meeting. Once the fund balance is calculated, the sum of those funds is reduced by the capital target/contingency margin and the balance is identified for return to members upon approval by the Board of Directors.

When rebates are declared by NOCSFWCA, the members have four choices for the use of the funds: 1) Credit next year's contribution, 2) Credit a Safety Credit Program, 3) Direct return to the member, and 4) Leave in NOCSFWCA in the member's name or in an interest-bearing account.

**NORTHERN ORANGE COUNTY SELF-FUNDED
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**MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2018 AND 2017**

Statement of Revenues, Expenses, and Changes in Net Position:

Revenues exceeded expenses by \$29,145 in 2017-2018, resulting in a net increase to the Fund Net Position of 7.47 percent as shown in the Condensed Statement of Revenues/Expenses shown below.

	<u>As of June 30,</u>		<u>Difference</u>	<u>Percentage</u>
	<u>2018</u>	<u>2017</u>		
Operating Revenue:				
Contributions	\$ 6,006,114	\$ 6,077,553	\$ (71,439)	(1.18) %
Safety Credit Program	(35,214)	(24,776)	(10,438)	42.13
Total Operating Revenue	<u>5,970,900</u>	<u>6,052,777</u>	<u>(81,877)</u>	<u>(1.35)</u>
Operating Expenses:				
PIPS Premium	5,731,005	5,793,038	(62,033)	(1.07)
Claims Activity	(28,640)	16,408	(45,048)	(274.55)
Claims Administration	6,000	8,850	(2,850)	(32.20)
Risk Management Fee	19,032	19,033	(1)	(0.01)
Operating Costs	<u>232,932</u>	<u>215,933</u>	<u>16,999</u>	<u>7.87</u>
Total Operating Expenses	<u>5,960,329</u>	<u>6,053,262</u>	<u>(92,933)</u>	<u>(1.54)</u>
Non Operating Revenues				
Investment Income	<u>18,574</u>	<u>12,788</u>	<u>5,786</u>	<u>45.25</u>
Change in Net Position	29,145	12,303	16,842	136.89
Beginning Net Position	<u>390,292</u>	<u>377,989</u>	<u>12,303</u>	<u>3.25</u>
Ending Net Position	<u>\$ 419,437</u>	<u>\$ 390,292</u>	<u>\$ 29,145</u>	<u>7.47 %</u>

Operating Revenue consists of contributions received from the members. Member contributions decreased from 2016-2017, by \$71,439 or 1.18 percent mainly attributed to:

- A slight increase of 0.22% in the estimated payroll for the 2017/2018 program year,
- Rate increase in the PIPS program of 3.68%.

Offset by,

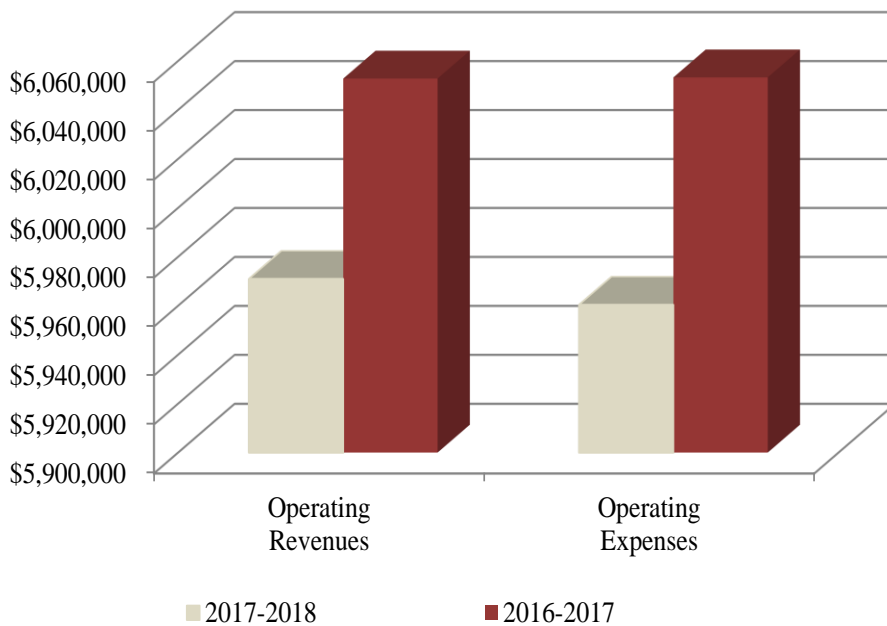
- The estimated to actual payroll contribution increase for 2015-2016 program year of \$270,601 as reflected in 2016-2017 financials,
- The estimated to actual payroll contribution decrease for 2016-2017 program year of \$9,565 as reflected in 2017-2018 financials.

**NORTHERN ORANGE COUNTY SELF-FUNDED
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**MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2018 AND 2017**

Total operating expenses decreased by 1.54 percent in 2017-2018 from \$6,053,262 to \$5,960,329 mainly attributed to the decrease of the PIPS premium, which is consistent with the decrease seen in member contributions.

Below is a graph that reflects a comparison of operating income and expense for 2017-2018 and 2016-2017:



Budgetary Highlights:

Each year the NOCSFWCA Board of Directors approves a budget and establishes rates and funding levels for the program year. The preliminary budget is reviewed by the Board in May, with a final budget to be approved by the Board in June. The final budget incorporates any changes in assumptions or projections that have been made subsequent to the approval of the preliminary budget. NOCSFWCA is not required to make mid-year budget adjustments.

**NORTHERN ORANGE COUNTY SELF-FUNDED
WORKERS' COMPENSATION AGENCY
(A Joint Powers Entity)**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2018 AND 2017**

Below is a summary of the budget information with a comparison to actual expenses. The largest difference between budgeted to actual numbers results from claims activity.

	2017-2018			
	Adopted Budget	Actual	Difference	Percentage
Operating Revenue				
Member Contributions	\$ 6,015,679	\$ 6,006,114	\$ (9,565)	(0.16) %
Safety Credit Program	(35,214)	(35,214)	-	-
Total Operating Revenues	<u>5,980,465</u>	<u>5,970,900</u>	<u>(9,565)</u>	<u>(0.16)</u>
Operating Expenses:				
PIPS Premium	5,740,570	5,731,005	(9,565)	(0.17)
Claims Activity	(6,000)	(28,640)	(22,640)	377.33
Claims Administration	6,000	6,000	-	-
Risk Management Fee	19,033	19,032	(1)	-
Operating Costs	220,862	232,932	12,070	5.46
Total Operating Expenses	<u>5,980,465</u>	<u>5,960,329</u>	<u>(20,136)</u>	<u>(0.34)</u>
Non Operating Income				
Investment Income	<u>15,290</u>	<u>18,574</u>	<u>3,284</u>	<u>21.48</u>
Change in Net Position	15,290	29,145	13,855	90.61
Beginning Net Position	390,292	390,292	-	-
Ending Net Position	<u>\$ 405,582</u>	<u>\$ 419,437</u>	<u>\$ 13,855</u>	<u>3.42 %</u>

Description of Facts or Conditions That are Expected to Have a Significant Effect on Financial Position or Results of Operations

From a California standpoint, the Workers' Compensation rates are beginning to stabilize at current levels primarily as a result of SB 863 passed in 2012 which appears to be stemming the pace of increase especially in the area of medical costs.

This outlook applies equally to large Public Entities such as PIPS or other large JPAs. The difference being that programs like PIPS and other large JPAs is that their program rates will also be largely based on their own experience which are even more stable and therefore predictable than smaller risks.

**NORTHERN ORANGE COUNTY SELF-FUNDED
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**STATEMENTS OF NET POSITION
JUNE 30, 2018 AND 2017**

	<u>2018</u>	<u>2017</u>
ASSETS		
Current Assets		
Deposits and investments	\$ 1,979,041	\$ 1,855,580
Prepaid expense	-	19,032
Receivables	7,318	23,391
Total Assets	<u>1,986,359</u>	<u>1,898,003</u>
LIABILITIES		
Current Liabilities		
Accounts payable	6,729	8,587
Due to members	1,096,825	1,206,402
Unearned Revenue	200,000	-
Current portion of unpaid claims and loss adjustment expenses	21,000	21,000
Total Current Liabilities	<u>1,324,554</u>	<u>1,235,989</u>
Unpaid claims and loss adjustment expenses, non-current portion	<u>242,368</u>	<u>271,722</u>
Total Liabilities	<u>1,566,922</u>	<u>1,507,711</u>
NET POSITION - UNRESTRICTED	<u>\$ 419,437</u>	<u>\$ 390,292</u>

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

**NORTHERN ORANGE COUNTY SELF-FUNDED
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**STATEMENTS OF REVENUES, EXPENSES, AND
CHANGES IN NET POSITION
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

	<u>2018</u>	<u>2017</u>
OPERATING INCOME		
Contributions	\$ 6,006,114	\$ 6,077,553
Safety credit program	(35,214)	(24,776)
Total Operating Income	<u>5,970,900</u>	<u>6,052,777</u>
OPERATING EXPENSES		
Excess insurance	5,731,005	5,793,038
Claims payments	714	1,565
Provision (credit) for loss reserves	(27,954)	15,924
Credit for ULAE	(1,400)	(1,081)
Claims administration	6,000	8,850
Administration expenses	20,697	23,761
JPA administration	90,750	90,750
Risk management	19,032	19,033
Contract services	27,320	27,320
DSIP assessment	94,165	74,102
Total Operating Expenses	<u>5,960,329</u>	<u>6,053,262</u>
Operating Income (Loss)	<u>10,571</u>	<u>(485)</u>
NON-OPERATING REVENUES		
Interest, net of interest allocated directly to members of \$16,181 in 2018 and \$9,415 in 2017	<u>18,574</u>	<u>12,788</u>
CHANGE IN NET POSITION	29,145	12,303
NET POSITION, BEGINNING OF YEAR	<u>390,292</u>	<u>377,989</u>
NET POSITION, END OF YEAR	<u>\$ 419,437</u>	<u>\$ 390,292</u>

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

**NORTHERN ORANGE COUNTY SELF-FUNDED
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**STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

	<u>2018</u>	<u>2017</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from members and others, net	\$ 6,061,323	\$ 6,131,917
Cash recovered (paid) for claims and settlements	17,779	(19,821)
Cash paid for excess insurance	(5,731,005)	(5,793,038)
Cash paid to suppliers for goods and services	<u>(239,888)</u>	<u>(261,872)</u>
Net Cash Provided by Operating Activities	<u>108,209</u>	<u>57,186</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest income	<u>15,252</u>	<u>11,231</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	123,461	68,417
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>1,855,580</u>	<u>1,787,163</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u><u>\$ 1,979,041</u></u>	<u><u>\$ 1,855,580</u></u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating income (loss)	\$ 10,571	\$ (485)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:		
Changes in Assets and Liabilities:		
(Increase) decrease in accounts receivable	19,395	(18,861)
(Increase) decrease in prepaid expenses	19,032	(19,032)
Increase (decrease) in accounts payable	(1,858)	1,581
Increase (decrease) in amounts due members	(109,577)	79,140
Increase in unearned revenue	200,000	-
Increase (decrease) in claims and unallocated expense liability	<u>(29,354)</u>	<u>14,843</u>
Net Cash Provided by Operating Activities	<u><u>\$ 108,209</u></u>	<u><u>\$ 57,186</u></u>

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

**NORTHERN ORANGE COUNTY SELF-FUNDED
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(A Joint Powers Entity)**

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2018 AND 2017**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The Northern Orange County Self-Funded Workers' Compensation Agency (the Agency) was formed and became operational on October 1, 1977, when the Cypress Elementary School District, Los Alamitos Unified School District, Magnolia Elementary School District, Savanna Elementary School District, and Westminster Elementary School District joined together under the California Government Code to create a public agency. The following local educational agencies became members of the Agency on the respective dates:

Centralia Elementary School District	10/01/77
La Habra Elementary School District	07/01/78
Buena Park Elementary School District	07/01/79
Greater Anaheim Special Education Local Plan Area (GASELPA)	11/01/85
Coastline Regional Occupational Program	07/01/87
North Orange County Regional Occupational Program	10/01/87
College and Career Advantage (Formerly - South Coast Regional Occupations Program)	07/01/96

The purpose of the Agency is to provide its members the necessary workers' compensation coverage as presented by the laws of the State of California.

The Agency functions as a pool for its respective members. Each member of the Agency is liable only for its prorata share, based on all premiums paid, of all debts and liabilities of the Agency.

The Agency includes all funds and account groups that are controlled by or dependent on the Agency's governing board for financial reporting purposes. The Agency has considered all potential component units in determining how to define the reporting entity, using criteria set forth in accounting principles generally accepted in the United States of America. The Agency determined that there are no potential component units that meet the criteria for inclusion within the reporting entity.

**NORTHERN ORANGE COUNTY SELF-FUNDED
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**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2018 AND 2017**

B. Basis of Accounting

The accompanying financial statements are presented as a proprietary fund on the accrual basis of accounting in accordance with governmental Generally Accepted Accounting Principles (GAAP). Under the accrual basis, revenues and the related assets are recognized when earned, and expenses and related liabilities are recognized when the obligation is incurred. Operating revenues include member contributions net of any applicable rate credits. Operating expenses include the provision for claims and claims adjustment expenses, insurance premiums, premium rebates, and general and administrative expenses. All other revenues and expenses are considered non-operating.

C. Budgets and Budgetary Accounting

Annually, the Board of Directors adopts a budget that is subject to amendment throughout the year to give consideration to unanticipated revenue and expenses primarily resulting from events unknown at the time of budget adoption.

D. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

E. Cash and Cash Equivalents

Cash equivalents consist of highly liquid investments with original maturities of three months or less. For purposes of the Statement of Cash Flows, deposits with the County Treasury and the State Investment Pool Local Agency Investment Fund (LAIF) are considered to be cash equivalents.

F. Prepaid Expenses

Prepaid expenses represent amounts paid in advance of receiving goods or services.

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**NOTES TO FINANCIAL STATEMENTS
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G. Claims Liabilities

The Agency establishes claims liabilities based on estimates of the ultimate cost of claims (including future claims administrative costs) that have been reported but not settled, and of claims that have been incurred but not reported. The length of time for which such costs must be estimated varies depending on the coverage involved. Estimated amounts of salvage and subrogation and excess insurance recoverable on unpaid claims are deducted from the liability for unpaid claims. Because actual claims costs depend on such complex factors as inflation, changes in doctrines of legal liability, and damage awards, the process used in computing claims liabilities does not necessarily result in an exact amount. Claims liabilities are computed periodically using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, claim frequency, and other economic and social factors. A provision for inflation in the calculation of estimated future claims costs is implicit in the calculation because reliance is placed both on actual historical data that reflect past inflation and on other factors that are considered to be appropriate modifiers of past experience. Adjustments to claims liabilities are charged or credited to expense in the periods in which they are made.

H. Member Contributions

Each member's contribution is determined based upon the number of plan participants and the contribution rate for each classification of covered participant. The rates for each member are determined based on each member's loss history, unusual exposures, and other pertinent information. If the total obligations would exceed the total assets of the Agency, the members may be assessed additional contributions.

I. Insurance Coverage

The Agency uses excess insurance agreements to reduce its exposure to large losses. Excess insurance permits recovery of a portion of losses from The Protected Insurance Program for Schools Joint Power Authority (PIPS), although it does not discharge the primary liability of the Agency as direct insurer of the risks insured. The Agency does not report excess insurance risks as liabilities unless it is probable that those risks will not be covered by excess insurance carriers.

Limits of coverage under PIPS for the year ended June 30, 2018 were as follows:

Workers' Compensation	\$ 155,000.00
Employers Liability	
▪ Bodily Injury by Accident – Each Accident	\$ 1,000,000.00
▪ Each Employee Bodily Injury by Disease	\$ 1,000,000.00
▪ Bodily Injury by Disease Limit per Covered Party	\$ 1,000,000.00

J. Income Taxes

The Agency's income is exempt from Federal and State income taxes under Internal Revenue Code Section 115, and the corresponding section of the California Revenue and Taxation Code.

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**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2018 AND 2017**

NOTE 2 - DEPOSITS AND INVESTMENTS

A. Summary of Deposits and Investments

Deposits and investments as of June 30, 2018 and 2017, consist of the following:

	<u>2018</u>	<u>2017</u>
Cash in banks	\$ 4,590	\$ 655
Cash in trust account	100,000	100,000
Investments in County Treasury	1,438,914	1,421,944
Investments in State Investment Pool	435,537	332,981
Total Deposits and Investments	<u>\$ 1,979,041</u>	<u>\$ 1,855,580</u>

B. Policies and Practices

The Agency is authorized under California Government Code to make direct investments in local agency bonds, notes, or warrants within the State; U.S. Treasury instruments; registered State warrants or treasury notes; securities of the U.S. Government, or its agencies; bankers acceptances; commercial paper; certificates of deposit placed with commercial banks and/or savings and loan companies; repurchase or reverse repurchase agreements; medium term corporate notes; shares of beneficial interest issued by diversified management companies, certificates of participation, obligations with first priority security; and collateralized mortgage obligations.

C. Investment in County Treasury

The Agency is considered to be a voluntary participant in an external investment pool as the Agency is required to deposit all receipts and collections of monies with their County Treasurer (*Education Code Section 41001*). The fair value of the Agency's investment in the pool is reported in the accounting financial statements at amounts based upon the Agency's pro-rata share of the fair value provided by the County Treasurer for the entire portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by the County Treasurer, which is recorded on the amortized cost basis.

D. Investment in the State Investment Pool

The Agency is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by California *Government Code* Section 16429 under the oversight of the Treasurer of the State of California. The fair value of the Agency's investment in the pool is reported in the accompanying financial statement at amounts based upon the Agency'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 is recorded on the amortized cost basis.

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**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2018 AND 2017**

E. Custodial Credit Risk - Deposits

This is the risk that in the event of a bank failure, the Agency's deposits may not be returned to it. The Agency does not have a policy for custodial credit risk for deposits. However, 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 percent of the total amount deposited by the public agencies. California law also allows financial institutions to secure public deposits by pledging first trust deed mortgage notes having a value of 150 percent of the secured public deposits and letters of credit issued by the Federal Home Loan Bank of San Francisco having a value of 105 percent of the secured deposits. As of June 30, 2018 and 2017, the Agency's bank balances were not exposed to custodial credit risk.

NOTE 3 - FAIR VALUE MEASUREMENTS

The Agency categorizes the fair value measurements of its investments based on the hierarchy established by generally accepted accounting principles. The fair value hierarchy, which has three levels, is based on the valuation inputs used to measure an asset's fair value. The following provides a summary of the hierarchy used to measure fair value:

Level 1 - Quoted prices in active markets for identical assets that the Agency has the ability to access at the measurement date. Level 1 assets may include debt and equity securities that are traded in an active exchange market and that are highly liquid and are actively traded in over-the-counter markets.

Level 2 - Observable inputs other than Level 1 prices such as quoted prices for similar assets in active markets, quoted prices for identical or similar assets in markets that are not active, or other inputs that are observable, such as interest rates and curves observable at commonly quoted intervals, implied volatilities, and credit spreads. For financial reporting purposes, if an asset has a specified term, a Level 2 input is required to be observable for substantially the full term of the asset.

Level 3 - Unobservable inputs should be developed using the best information available under the circumstances, which might include the Agency's own data. The Agency should adjust that data if reasonably available information indicates that other market participants would use different data or certain circumstances specific to the Agency are not available to other market participants.

Uncategorized - Investments in the State Investment Pool Local Agency Investment Fund and Country Treasury are not measured using the input levels above because the Agency's transactions are based on a stable net asset value per share. All contributions and redemptions are transacted at \$1.00 net asset value per share.

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**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2018 AND 2017**

NOTE 4 - RECEIVABLES

Receivables at June 30, 2018 and 2017, consist of the following:

	<u>2018</u>	<u>2017</u>
Reinsurance receivable	\$ 444	\$ 19,839
Interest income receivable	6,874	3,552
Total Accounts Receivable	<u>\$ 7,318</u>	<u>\$ 23,391</u>

NOTE 5 - ACCOUNTS PAYABLE

Accounts payable at June 30, 2018 and 2017, consist of the following:

	<u>2018</u>	<u>2017</u>
Accounts payable	\$ 6,574	\$ 7,476
Claims payable	155	1,111
Total Accounts Payable	<u>\$ 6,729</u>	<u>\$ 8,587</u>

NOTE 6 - DUE TO MEMBERS

The amounts due to members at June 30, 2018 and 2017, are summarized below:

	<u>2018</u>	<u>2017</u>
Buena Park School District	\$ 121,134	\$ 119,658
Centralia School District	205,620	408,314
Coastline Regional Occupational Program	28,694	28,950
Cypress School District	111,124	109,109
Greater Anaheim Special Education Local Plan Area (GASELPA)	15,472	10,331
La Habra City School District	41,779	35,282
Los Alamitos Unified School District	156,364	154,459
Magnolia School District	102,125	92,290
North Orange County Regional Occupational Program	204,486	150,421
Savanna Elementary	23,833	23,386
Westminster School District	86,194	74,202
Total	<u>\$ 1,096,825</u>	<u>\$ 1,206,402</u>

**NORTHERN ORANGE COUNTY SELF-FUNDED
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**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2018 AND 2017**

NOTE 7 – UNEARNED REVENUE

Unearned revenue at June 30, 2018 consisted of \$200,000 in rebate funds for one of the Authority's members to be applied to offset future member contributions. There was no unearned revenue at June 30, 2017.

NOTE 8 - UNPAID CLAIMS LIABILITIES

As discussed in Note 1, the Agency establishes a liability for both reported and unreported insured events, which includes estimates of both future payments of losses and related claim adjustment expenses. The following represents changes in those aggregate liabilities for the Agency during the years ended June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Claims liabilities at beginning of fiscal year	\$ 275,522	\$ 259,598
Incurred expenses related to:		
Insured events of prior fiscal years	<u>(27,240)</u>	<u>17,489</u>
Payments related to:		
Insured events of prior fiscal years	<u>714</u>	<u>1,565</u>
Claims liabilities at end of fiscal year	<u>\$ 247,568</u>	<u>\$ 275,522</u>

The component units of the unpaid claims and claim adjustment expenses as of June 30, 2018 and 2017, were as follows:

	<u>2018</u>	<u>2017</u>
Claims liability	\$ 247,568	\$ 275,522
Unallocated loss adjustment expenses	<u>15,800</u>	<u>17,200</u>
	263,368	292,722
Current portion	<u>(21,000)</u>	<u>(21,000)</u>
	<u>\$ 242,368</u>	<u>\$ 271,722</u>

**NORTHERN ORANGE COUNTY SELF-FUNDED
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**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2018 AND 2017**

NOTE 9 - NET POSITION

Net position is composed of the following elements as of June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Unrestricted		
Designated - Capital target	\$ 507,847	\$ 497,558
Undesignated	(88,410)	(107,266)
Total Net Position	<u>\$ 419,437</u>	<u>\$ 390,292</u>

NOTE 10 - PARTICIPATION IN PUBLIC ENTITY RISK POOLS

The Agency participates in two joint ventures under joint powers agreements (JPA's) as described below. The relationship between the Agency and the JPAs is that the JPAs are not component units of the Agency for financial reporting purposes.

Schools Alliance for Workers' Compensation Excess Self-Funded (SAWCX II)

SAWCX II arranges for and provides for the joint group purchase of workers' compensation excess protection for its members. SAWCX II is governed by a board consisting of a representative from each member. The board controls the operations of SAWCX II, including approval of an operating budget. Each member pays a premium commensurate with the level of coverage requested and shares surpluses and deficits proportionate to their participation in SAWCX II.

No payments were made to SAWCX II during the 2017-2018 program years.

The Protected Insurance Program for Schools and Community Colleges Joint Powers Authority (PIPS)

The PIPS arranges for and provides for the joint group purchase of workers' compensation reinsurance for its members. The PIPS is governed by an executive board consisting of nine members, five are K-12, and four are community colleges. This board controls the operations of the PIPS including approval of an operating budget. Each member pays a premium commensurate with their experience modification within the pool and shares surpluses and deficits proportionate to their participation in PIPS.

Payments for the current year	<u>\$ 5,731,005</u>
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INDEPENDENT AUDITOR'S REPORTS



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

Board of Directors
Northern Orange County Self-Funded Workers' Compensation Agency
Torrance, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Northern Orange County Self-Funded Workers' Compensation Agency (the Agency) as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise Northern Orange County Self-Funded Workers' Compensation Agency's basic financial statements, and have issued our report thereon dated September 26, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Northern Orange County Self-Funded Workers' Compensation Agency's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Northern Orange County Self-Funded Workers' Compensation Agency's internal control. Accordingly, we do not express an opinion on the effectiveness of Northern Orange County Self-Funded Workers' Compensation Agency's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Agency's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Northern Orange County Self-Funded Workers' Compensation Agency's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our 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*.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Agency's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Agency's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Vavrieh, Trine, Day & Co., LLP

Rancho Cucamonga, California
September 26, 2018

SCHEDULE OF FINDINGS

**NORTHERN ORANGE COUNTY SELF-FUNDED
WORKERS' COMPENSATION AGENCY
(A Joint Powers Entity)**

**SCHEDULE OF FINANCIAL STATEMENT FINDINGS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

There were no findings related to the financial statements that are required to be reported in accordance with *Government Auditing Standards*.

**NORTHERN ORANGE COUNTY SELF-FUNDED
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**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEARS ENDED JUNE 30, 2018 AND 2017**

There were no audit findings reported in the prior year's schedule of financial statement findings.