

# **MODESTO IRRIGATION DISTRICT**

Modesto, California

## **FINANCIAL STATEMENTS**

Including Independent Auditors' Report

As of and for the Years Ended December 31, 2016 and 2015

# MODESTO IRRIGATION DISTRICT

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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
Modesto Irrigation District  
Modesto, California

We have audited the accompanying financial statements of the Modesto Irrigation District and its fiduciary funds (the District), as of and for the years ended December 31, 2016 and 2015, 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 opinions 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. Those standards require that we plan and perform the audits 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 District'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 District'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 opinions.

### ***Opinions***

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the District and its fiduciary funds as of December 31, 2016 and 2015, and the respective changes in financial position and cash flows, where applicable, thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

To the Board of Directors  
Modesto Irrigation District

***Other Matters***

*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the required supplementary information 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.

*Supplementary Information*

Our audits were conducted for the purpose of forming opinions on the basic financial statements as a whole. The combining statements of fiduciary net position and changes in fiduciary net position are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The 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 of fiduciary net position and changes in fiduciary net position are fairly stated in all material respects in relation to the basic financial statements as a whole.

*Baker Tilly Virchow Krause, LLP*

Madison, Wisconsin  
May 16, 2017

# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

Years ended December 31, 2016 and 2015 - Unaudited

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### **Overview:**

The following management discussion and analysis of the Modesto Irrigation District (District) provides an overview of the financial activities and transactions for fiscal years 2016 and 2015 in the context of the requirements of the Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended. This discussion and analysis should be read in conjunction with the District's audited financial statements and accompanying notes.

### **Financial Reporting:**

The District's accounting records are maintained in accordance with Generally Accepted Accounting Principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB).

### **Explanation of Financial Statements:**

District financial statements include a Balance Sheet; Statement of Revenues, Expenses and Changes in Net Position; Statement of Cash Flows, Statement of Fiduciary Net Position, and Statement of Changes in Fiduciary Net Position.

### **Balance Sheet:**

The Balance Sheet provides information about assets, liabilities, and equity of the District at a specific point in time. Assets are economic resources the District owns that have value and can either be sold or used by the District to produce products or services that can be sold. Assets include power generation plants, vehicles, equipment, inventory, cash and investments, and customer accounts receivable.

Liabilities are amounts of money that the District owes to others. This includes debt, money owed to suppliers for materials, payroll, and taxes owed to other governmental agencies.

Equity or Net Position are the funds that will be left if the District sold all of its assets and paid off all of its liabilities.

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

The Statement of Revenues, Expenses and Changes in Net Position is more commonly known as the Income Statement. This statement provides information regarding the District's operations including revenue earned and expenses incurred over a one year period. The "bottom line" of the statement shows the District's end of year net position.

# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

Years ended December 31, 2016 and 2015 - Unaudited

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### **Statement of Cash Flows:**

The Statement of Cash Flows reports the District's inflows and outflows of cash. This report provides management with information regarding cash on hand and the ability to pay expenses and purchase assets.

A cash flow statement reflects changes over time rather than absolute dollar amounts at a point in time. The bottom line of the cash flow statement shows the net increase or decrease in cash for the period. Cash flow statements are divided into three activities: (1) operating activities; (2) investing activities; and (3) capital financing activities.

1. Operating Activities – analyzes the cash flow from operational activities (Operating Income and Expenses). This section of the cash flow statement reconciles the operating income to the actual cash MID received from or used in its operating activities. To facilitate this, the operating income is adjusted for any non-cash items (depreciation expenses) and any cash that was used or provided by other operating assets and liabilities.
2. Investing Activities – reflects the cash flow from all investing activities including purchases or sales of investment securities.
3. Capital Financing Activities – shows the cash flow from all financing activities. Typical sources of cash flow include funds received from borrowings, paying back debt service, and the purchase of capital assets.

### **Statement of Fiduciary Net Position:**

The Statement of Fiduciary Net Position (Balance Sheet) reports the financial resources available for future pension and other retirement benefits.

### **Statement of Changes in Fiduciary Net Position:**

The Statement of Changes in Fiduciary Net Position (Income Statement) reflects the additions and deductions and net increase (decrease) in net position held in trust for pension benefits.

# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

Years ended December 31, 2016 and 2015 - Unaudited

The following is a comparative financial summary for years ending December 31, 2016, 2015, and 2014.

### Financial Summary

#### Balance Sheet

(\$ in thousands)

	December 31, 2016	December 31, 2015	December 31, 2014	Change from 2015 to 2016
<b>Assets and Deferred Outflows of Resources</b>				
Utility plant, net	\$ 717,198	\$ 716,917	\$ 710,459	\$ 281
Other noncurrent assets and investments	314,726	295,993	200,311	18,733
Current assets	160,087	191,671	152,628	(31,584)
Deferred outflows of resources	68,144	54,298	41,698	13,846
<b>Total Assets and Deferred Outflows of Resources</b>	<b>\$ 1,260,155</b>	<b>\$ 1,258,879</b>	<b>\$ 1,105,096</b>	<b>\$ 1,276</b>
<b>Liabilities, Deferred Inflows of Resources, and Net Position</b>				
Long-term debt, net	\$ 705,695	\$ 760,885	\$ 719,525	\$ (55,190)
Noncurrent liabilities	185,515	171,794	104,326	13,721
Current liabilities	81,378	74,329	78,023	7,049
Deferred inflow of resources	42,865	43,623	37,632	(758)
Net position				
Net investment in capital assets	62,377	22,611	7,403	39,766
Unrestricted	182,325	185,637	158,187	(3,312)
<b>Total Liabilities, Deferred Inflows, and Net Position</b>	<b>\$ 1,260,155</b>	<b>\$ 1,258,879</b>	<b>\$ 1,105,096</b>	<b>\$ 1,276</b>

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

(\$ in thousands)

	December 31, 2016	December 31, 2015	December 31, 2014	Change from 2015 to 2016
Operating revenues	\$ 413,790	\$ 424,999	\$ 416,762	\$ (11,209)
Operating expenses	(347,161)	(361,994)	(354,597)	14,833
Operating income (loss)	66,629	63,005	62,165	3,624
<b>Non-operating Income (Expenses)</b>				
Investment and other income, net	3,592	7,886	9,341	(4,294)
Interest expense	(39,598)	(39,545)	(39,145)	(53)
Other non-operating income, net	4,568	5,077	5,453	(509)
Non-operating income (expense)	(31,438)	(26,582)	(24,351)	(4,856)
Contributed Capital - Electric/Water	1,263	6,235	6,017	(4,972)
Change in net position	36,454	42,658	43,831	(6,204)
Net position, beginning of year	208,248	165,590	121,759	42,658
<b>Net Position, End of Year</b>	<b>\$ 244,702</b>	<b>\$ 208,248</b>	<b>\$ 165,590</b>	<b>\$ 36,454</b>

# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

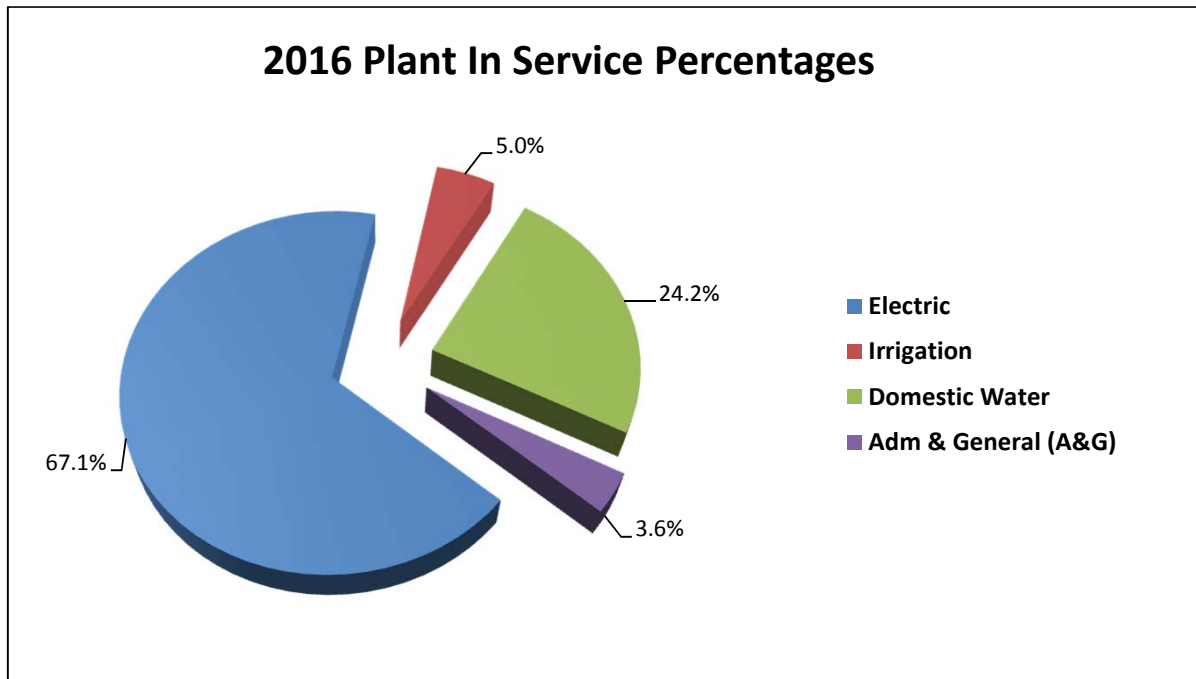
Years ended December 31, 2016 and 2015 - Unaudited

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### ASSETS and DEFERRED OUTFLOWS

#### ***Utility Plant, net***

MID has invested approximately \$717.2 million in utility plant assets net of accumulative depreciation and transferred approximately \$21.3 million of assets from construction in progress to utility plant in service in 2016. The following chart reflects the percentage breakdown of Utility Plant net of depreciation by category as of December 31, 2016.



Utility plant increased by approximately \$0.3 million in 2016 due to additions in plant and service offset by construction work in progress and depreciation.

Utility plant increased by approximately \$6.5 million in 2015 due to additions in plant and service offset by reductions in construction work in progress and depreciation.

#### ***Other non-current assets and investments***

Other non-current assets and investments increased \$18.7 million in 2016. The increase is due to both an increase in Investments - unrestricted of \$26.0 million and an increase in Other long-term assets due to a \$3.0 million increase in the amount due to TANC. This increase is partially offset by a decrease in capital improvement funds of \$11.6 million.

Other non-current assets and investments increased \$95.7 million in 2015. Significant changes include an increase of \$71.1 million of bond proceeds due to the issuance of the 2015A bonds offset by \$15.7 million in project fund uses. Other significant changes include an increase in regulatory asset of \$61.3 million, and an increase in Other long-term assets of \$6.6 million due from TANC offset by the re-class from "investments – unrestricted" to "cash and cash equivalents – unrestricted" of approximately \$29.4 million. The re-class was made to allow for payments on debt, capital costs, and other cash needs.



# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

Years ended December 31, 2016 and 2015 - Unaudited

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### ***Current assets***

Current assets decreased by approximately \$31.6 million in 2016. The decrease is based on a combination of changes in the District's portfolio between long-term investments and short-term investments. The "cash and cash equivalents" for both unrestricted and restricted had a net decrease of \$14.8 million. Additional significant changes include decreases in Materials and supplies of \$13.8 million and Other current assets of \$2.4 million.

Current assets increased by approximately \$39.0 million in 2015. The increase is based on a combination of changes in the District's portfolio from long-term investments to short-term plus electric sales increasing cash. The "cash and cash equivalents" for both unrestricted and restricted had a net increase of \$41.1 million. Additional significant changes include decreases in Customer accounts receivable, net of \$0.9 million and Other current assets, net of \$1.6 million.

### ***Deferred Outflows of Resources***

In 2016 deferred outflows of resources increased by \$13.8 million. The change is due to deferred outflows related to pension increasing by \$14.0 million and Unamortized loss on advanced refunding increasing approximately \$3.5 million due to the debt refundings in the current year. This was offset by decreases in Deferred cash flow hedges of approximately \$3.7 million.

In 2015 deferred outflows of resources increased by \$12.6 million. The change is due to deferred outflows related to pension increase of \$13.5 million offset by Deferred cash flow hedges of approximately \$0.3 million and Unamortized loss on advanced refunding of approximately \$0.6 million.

## **LIABILITIES AND NET POSITION**

### ***Long-term debt***

Long-term debt decreased by \$55.2 million in 2016 due to scheduled debt service payments and the refunding of the 2004B, 2006A, and a portion of the 2009A COP bonds with the 2016 Refunding Revenue Bonds and cash on hand.

Long-term debt increased by \$41.4 million in 2015 due to issuance of the 2015 A&B Bonds offset by debt service payments.

### ***Non-current liabilities***

Non-current liabilities increased by \$13.7 million in 2016 primarily due to an increase of \$17.1 million in Net pension liability and an increase in Unamortized premium of \$10.2 million, offset by changes in Unamortized debt discounts, Other liabilities, and Equity interest in M-S-R totaling \$13.6 million.

Non-current liabilities increased by \$67.5 million in 2015 primarily due to the implementation of GASB 68 and the addition of net pension liability of \$74.5 million and an increase in Unamortized premium of \$4.4 million offset by changes in Unamortized debt discounts, Other liabilities, and Equity interest in M-S-R totaling \$11.9 million.

# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

Years ended December 31, 2016 and 2015 - Unaudited

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### ***Current liabilities***

Current liabilities increased by \$7.0 million in 2016 due to a increase in Current portion of long-term debt of \$9.8 million due to the current portion due on the new 2016 Refunding Revenue Bonds, offset by a decrease in Derivatives financial instrument maturing within one-year and Interest payable of \$2.9 million.

Current liabilities decreased by \$3.7 million in 2015 due to a decrease in accounts payable of \$3.8 million and Derivatives financial instrument maturing within one-year of \$0.8 offset by increases in Current liabilities payable from restricted assets of \$0.9 million.

### ***Deferred inflow of resources***

Deferred inflow of resources is unearned revenue which reflects the difference between the time the District bills the City of Modesto for Domestic Water and when the expense for depreciation is recovered and recorded. In 2016 the amount decreased by \$0.8 million.

### ***Net position***

In 2016, the District's net investment in capital assets increased by \$39.8 million primarily due to investments in fixed assets and scheduled debt payments from current year.

Unrestricted net position decreased by approximately \$3.3 million in 2016 primarily due to the decrease in operating revenue for the current year.

In 2015, the District's net investment in capital assets increased by \$15.2 million primarily due to investments in fixed assets and scheduled debt payments from current year.

Unrestricted net position increased by approximately \$27.4 million in 2015 primarily due to the increase in revenue for the current year.

# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

Years ended December 31, 2016 and 2015 - Unaudited

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### STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

#### Operating Revenues

##### Changes from 2015 to 2016

In 2016 operating revenue decreased by \$11.2 million or approximately 2.64%.

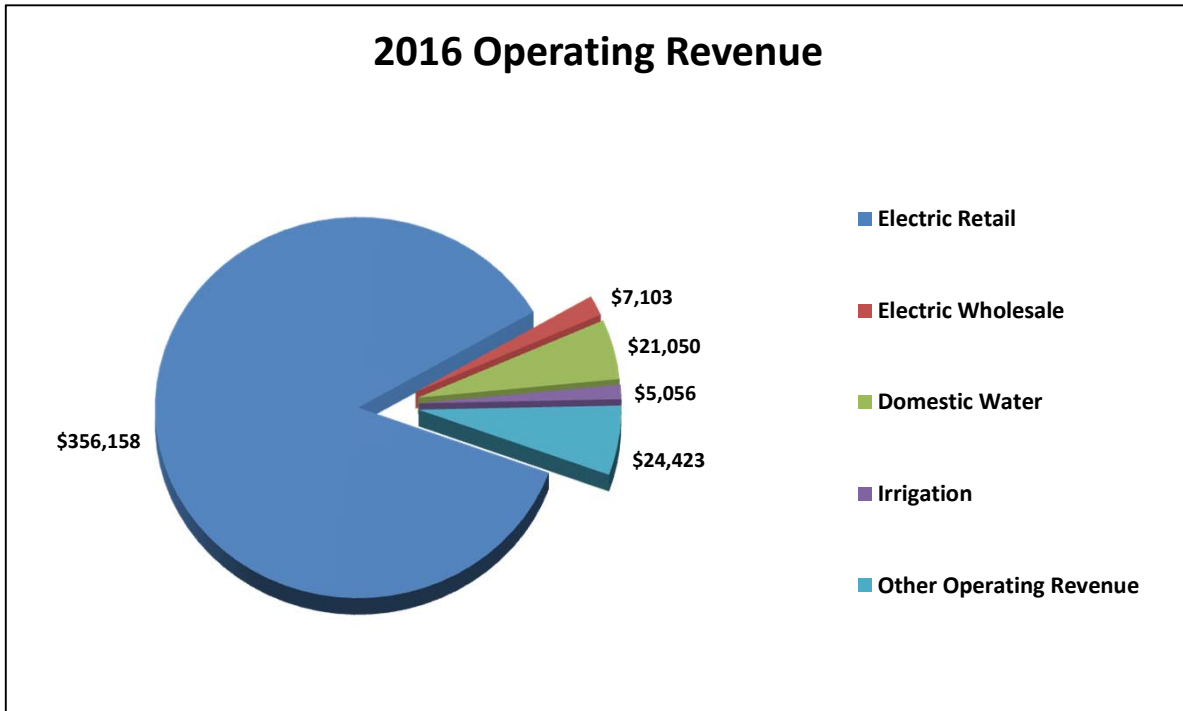
Retail electric revenue increased by \$4.3 million or approximately 1.23%. Retail consumption has remained relatively constant with changes in revenue due to small increases in customer demand.

Wholesale electric revenue decreased by \$8.9 million or approximately 55.66% due to reductions in generation sold during the year.

Domestic Water revenue increased of \$8.1 million or 62.54% due to increased costs associated with operating Phase 2 of the plant and an increase in depreciation expense.

Other operating revenue decreased by \$13.9 million or 36.3% due to equity in public power agencies, greenhouse gas revenue, and late fees.

The following is the District's 2016 operating revenue (**dollars are in thousands**):



# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

Years ended December 31, 2016 and 2015 - Unaudited

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### Operating Revenues

#### Changes from 2014 to 2015

In 2015 operating revenue increased by \$8.2 million or approximately 1.98%.

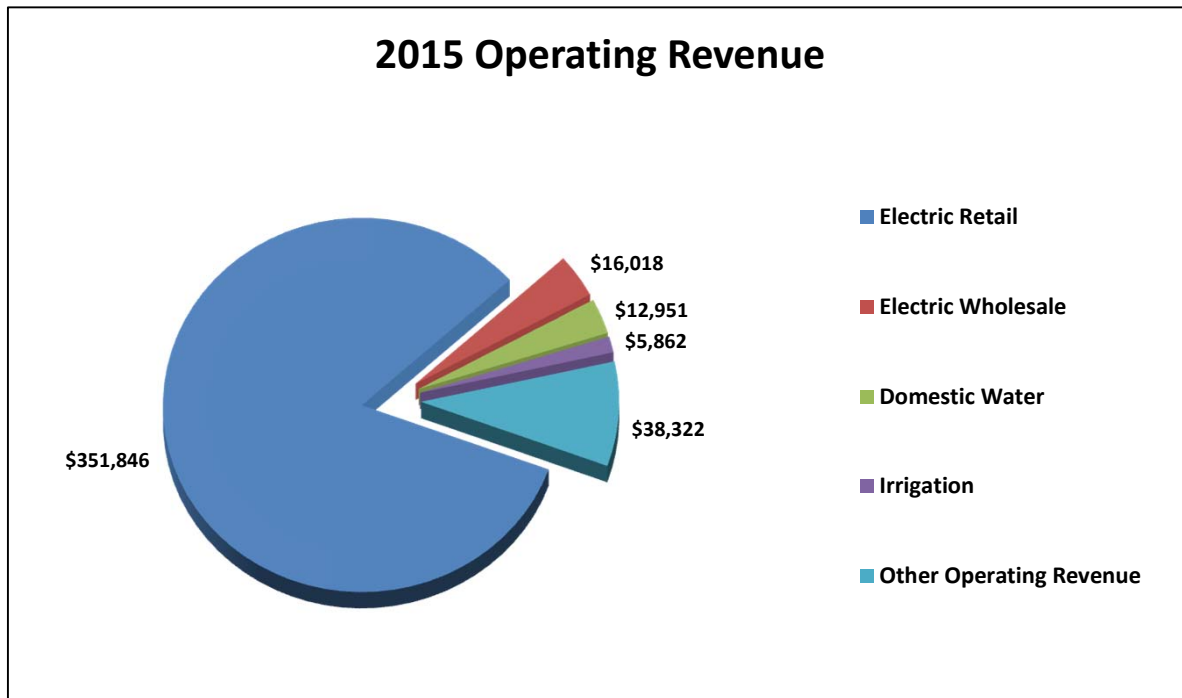
Retail electric revenue decreased by \$8.75 million or approximately 2.43%. Retail consumption has remained relatively constant with changes in revenue due to decreases in customer demand.

Wholesale electric revenue decreased by \$0.7 million or approximately 4.26%. The decrease is due to reductions in generation sold related to the operations of the Lodi Energy Center.

Domestic Water revenue increased of \$1.8 million or 16.27% due to rate changes related to the drought. Irrigation revenue increased by \$0.9 million or 18.14% due to rate changes related to the drought.

Other operating revenue includes equity in public power agencies, greenhouse gas revenue, and late charges. Other operating revenue increased by \$15.0 million or 64.26% due to equity in public power agencies, greenhouse gas revenue, and late fees.

The following is the District's 2015 operating revenue (**dollars are in thousands**):



# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

Years ended December 31, 2016 and 2015 - Unaudited

### Operating Expenses

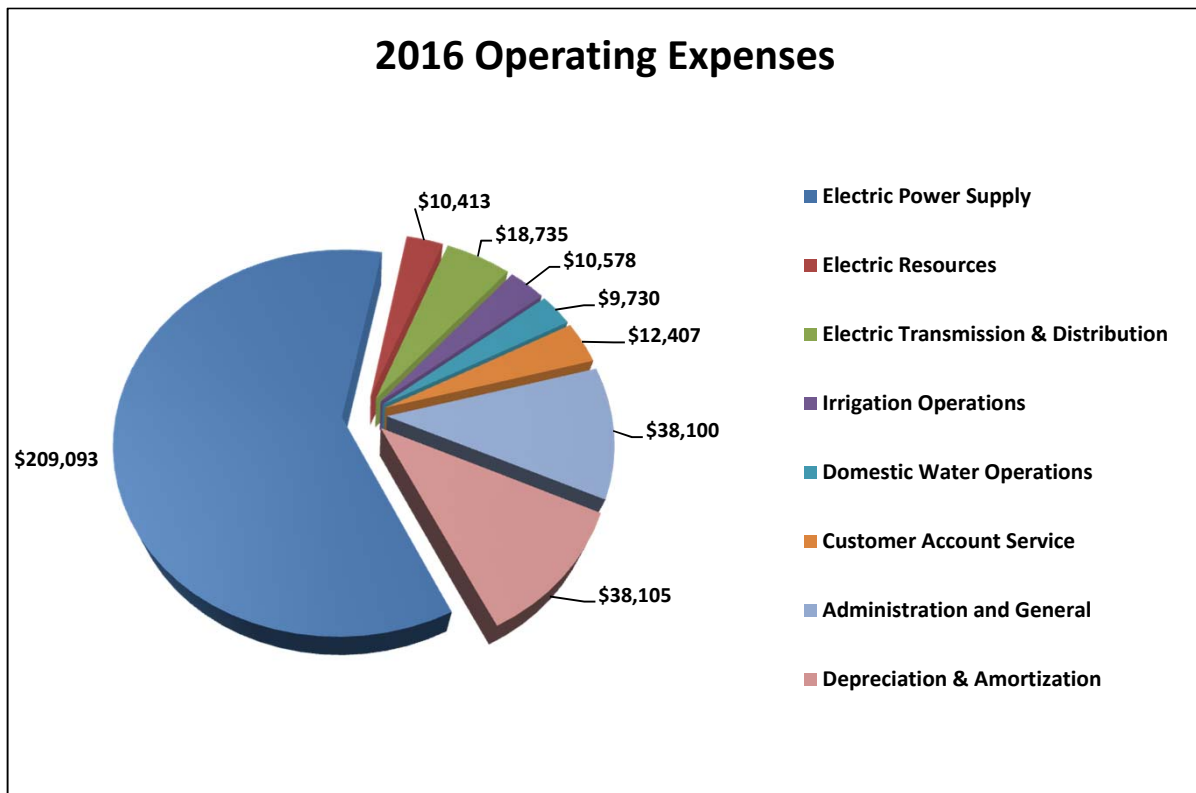
#### Changes from 2015 to 2016

Total operating expenses reflect a decrease of approximately \$14.8 million in 2016. The decrease is primarily due to decreased costs for Purchased power, offset by changes in Electric transmission and distribution, Domestic water operations, administration and general, and depreciation.

Purchased power and power generation expenses for 2016 reflect a decrease of approximately \$20.5 million or 8.92%. The change is mainly due to a decrease in Purchased power costs.

Expenses for Domestic Water reflect an increase of 17.3% related to increased costs for operations and maintenance due to the expansion of the plant. Irrigation operations reflects a decrease of \$0.5 million or 4.8%.

The following depicts the 2016 operational expenses (**dollars are in thousands**):



# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

Years ended December 31, 2016 and 2015 - Unaudited

### Operating Expenses

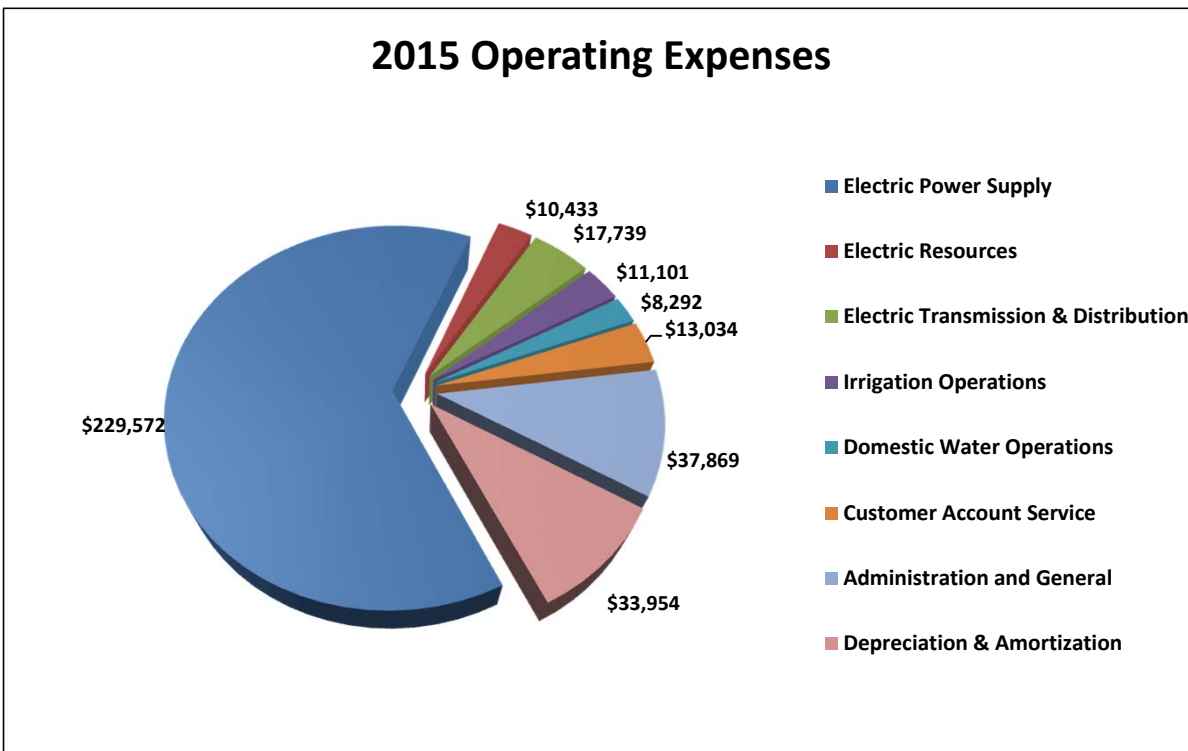
#### Changes from 2014 to 2015

Total operating expenses reflect an increase of approximately \$7.4 million in 2015. The increase is primarily due to increased cost for Irrigation operations, Domestic water operations, administration and general, and depreciation offset by a decrease in purchase power.

Purchased power and power generation expenses for 2015 reflect an increase of approximately \$0.7 million or 0.29%. The change is mainly due to availability and pricing of purchased power and a reduction in hydro power generation.

Water operations expenses for Domestic Water and Irrigation reflect increases of approximately \$1.1 million or 14.83% for Domestic Water and \$0.4 million or 3.96% for Irrigation respectively. The increase is primarily due to increased costs in operations and maintenance.

The following depicts the 2015 operational expenses (**dollars are in thousands**):



# MODESTO IRRIGATION DISTRICT

## Management's Discussion and Analysis

Years ended December 31, 2016 and 2015 - Unaudited

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### **Non-Operating Revenue (Expenses)**

#### ***Investment income***

Investment income decreased in 2016 by \$0.8 million due to reduction in interest on investments and unrealized losses on investments held.

Investment and other income decreased in 2015 by \$1.0 million due to reduction in interest on investments offset by capital contributions for Water and Electric, capitalized interest, and amortization of premium.

#### ***Interest expense***

Interest expense for 2016 remained relatively constant over the prior year.

Interest expense for 2015 decreased \$0.4 million over the prior year due to reductions in principal of outstanding debt.

#### ***Other non-operating Income, net***

Other non-operating income decreased in 2016 by \$0.5 million over the prior year due to changes in rental and miscellaneous revenue.

### **Contacting the Modesto Irrigation District**

This financial report is designed to provide our customers, investors, and creditors with a general overview of the District's finances. If you have questions about this report or need additional information, please contact the Controller's Office at P.O. Box 4060, Modesto, CA 95352.

# MODESTO IRRIGATION DISTRICT

## BALANCE SHEETS

As of December 31, 2016 and 2015

		<i>(Dollars in Thousands)</i>	
<b>ASSETS AND DEFERRED OUTFLOWS</b>		<u>2016</u>	<u>2015</u>
<b>CAPITAL ASSETS</b>			
Plant in service		\$ 1,294,442	\$ 1,274,965
Less accumulated depreciation		<u>(618,587)</u>	<u>(582,648)</u>
Plant in service - net		675,855	692,317
Construction work in progress		41,343	24,600
Total Capital Assets		<u>717,198</u>	<u>716,917</u>
<b>OTHER ASSETS AND INVESTMENTS</b>			
Cash and investments - restricted		112,561	111,486
Investments - unrestricted		103,995	77,962
Interest receivable - restricted		343	237
Capital improvement fund		9,799	21,435
Regulatory costs for future recovery		66,409	67,771
Equity interest in TANC		3,350	3,872
Other long-term assets		<u>18,269</u>	<u>13,230</u>
Total Other Assets and Investments		<u>314,726</u>	<u>295,993</u>
<b>CURRENT ASSETS</b>			
Cash and cash equivalents - unrestricted		91,100	105,114
Cash and cash equivalents - restricted		8,581	9,385
Interest receivable - unrestricted		952	752
Customer accounts receivable, net		34,765	33,825
Wholesale power receivables		7	2
Materials and supplies		15,919	29,751
Prepayments		1,599	3,232
Other current assets, net		<u>7,164</u>	<u>9,610</u>
Total Current Assets		<u>160,087</u>	<u>191,671</u>
Total Assets		<u>1,192,011</u>	<u>1,204,581</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>			
Deferred cash flow hedges - unrealized loss on derivatives		26,727	30,449
Unamortized loss on refunding		13,883	10,339
Deferred outflows related to pension		<u>27,534</u>	<u>13,510</u>
Total Deferred Outflows of Resources		<u>68,144</u>	<u>54,298</u>
<b>TOTAL ASSETS AND DEFERRED OUTFLOWS</b>		<u>\$ 1,260,155</u>	<u>\$ 1,258,879</u>



<b>LIABILITIES, DEFERRED INFLOWS AND NET POSITION</b>	<i>(Dollars in Thousands)</i>	
	<u>2016</u>	<u>2015</u>
<b>NONCURRENT LIABILITIES</b>		
Long-term debt, net of current portion	\$ 705,695	\$ 760,885
Unamortized premium	41,109	30,929
Unamortized debt discount	(2,577)	(2,881)
Net pension liability	93,447	76,334
Other liabilities	11,839	14,216
Derivative financial instruments	26,480	29,080
Equity interest in M-S-R	15,217	24,116
Total Noncurrent Liabilities	<u>891,210</u>	<u>932,679</u>
<b>CURRENT LIABILITIES</b>		
Accounts payable and other accruals	32,481	32,365
Current liabilities payable from restricted assets		
Current portion of long-term debt	36,150	26,320
Interest payable	12,500	14,275
Derivative financial instruments maturing within one year	247	1,369
Total Current Liabilities	<u>81,378</u>	<u>74,329</u>
Total Liabilities	<u>972,588</u>	<u>1,007,008</u>
<b>DEFERRED INFLOWS OF RESOURCES</b>		
Unearned revenue	<u>42,865</u>	<u>43,623</u>
<b>NET POSITION</b>		
Net investment in capital assets	62,377	22,611
Unrestricted	<u>182,325</u>	<u>185,637</u>
Total Net Position	<u>244,702</u>	<u>208,248</u>
<b>TOTAL LIABILITIES, DEFERRED INFLOWS AND NET POSITION</b>	<u>\$ 1,260,155</u>	<u>\$ 1,258,879</u>

See accompanying notes to financial statements.

# MODESTO IRRIGATION DISTRICT

## STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION For the Years Ended December 31, 2016 and 2015

	<i>(Dollars in Thousands)</i>	
	<u>2016</u>	<u>2015</u>
<b>OPERATING REVENUES</b>		
Residential, commercial and industrial electric	\$ 356,158	\$ 351,846
Wholesale electric	7,103	16,018
Domestic water	21,050	12,951
Irrigation water	5,056	5,862
Equity in net income of public power agencies	12,614	11,979
Other operating income, net	<u>11,809</u>	<u>26,343</u>
Total Operating Revenues	<u>413,790</u>	<u>424,999</u>
<b>OPERATING EXPENSES</b>		
Purchased power	174,009	194,556
Power generation	35,084	35,016
Electric resources	10,413	10,433
Electric transmission and distribution	18,735	17,739
Irrigation operations	10,578	11,101
Domestic water operations	9,730	8,292
Customer account service	12,407	13,034
Administrative and general	38,100	37,869
Depreciation and amortization	<u>38,105</u>	<u>33,954</u>
Total Operating Expenses	<u>347,161</u>	<u>361,994</u>
<b>OPERATING INCOME</b>	<u>66,629</u>	<u>63,005</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>		
Investment income	1,511	2,274
Interest expense	(39,598)	(39,545)
Capitalized interest	859	3,210
Amortization of debt discount	(125)	(117)
Amortization of premium	5,799	5,152
Amortization of loss on refunding	(3,853)	(2,019)
Regulatory amounts collected in rates	(599)	(614)
Other nonoperating income, net	<u>4,568</u>	<u>5,077</u>
Total Nonoperating Expenses	<u>(31,438)</u>	<u>(26,582)</u>
Change in Net Position Before Contributions	35,191	36,423
<b>CAPITAL CONTRIBUTIONS - ELECTRIC</b>	1,263	717
<b>CAPITAL CONTRIBUTIONS - DOMESTIC WATER</b>	<u>-</u>	<u>5,518</u>
<b>CHANGE IN NET POSITION</b>	36,454	42,658
NET POSITION - Beginning of Year	<u>208,248</u>	<u>165,590</u>
<b>NET POSITION - END OF YEAR</b>	<u>\$ 244,702</u>	<u>\$ 208,248</u>

See accompanying notes to financial statements.

## MODESTO IRRIGATION DISTRICT

### STATEMENTS OF CASH FLOWS For the Years Ended December 31, 2016 and 2015

	<i>(Dollars in Thousands)</i>	
	<u>2016</u>	<u>2015</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Receipts from customers	\$ 403,030	\$ 404,274
Receipts from public power agencies	4,237	-
Payments to suppliers for goods and services	(250,800)	(272,270)
Payments to employees for services	(43,077)	(42,179)
Net Cash Flows Provided by Operating Activities	<u>113,390</u>	<u>89,825</u>
<b>CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES</b>		
Net proceeds (payments) from issuance of long-term debt obligations	-	73,995
Payments to escrow for refunding	(8,831)	-
Repayment of long-term debt	(26,320)	(26,145)
Debt issuance costs	(685)	(680)
Construction expenditures	(36,495)	(38,637)
Interest paid	(41,373)	(39,195)
Payment to U.S. Treasury for arbitrage on outstanding debt	(2,333)	-
Contributions received for construction	1,546	5,953
Net Cash Flows Used in Capital Financing Activities	<u>(114,491)</u>	<u>(24,709)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Investments purchased	(106,565)	(42,007)
Investments sold and matured	71,543	52,677
Interest received	3,373	2,446
Net Cash Flows Provided by (Used in) Investing Activities	<u>(31,649)</u>	<u>13,116</u>
<b>Net Change in Cash and Cash Equivalents</b>	<u>(32,750)</u>	<u>78,232</u>
CASH AND CASH EQUIVALENTS, Beginning of Year	<u>155,900</u>	<u>77,668</u>
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<u>\$ 123,150</u>	<u>\$ 155,900</u>
<b>SUPPLEMENTAL DISCLOSURE OF NONCASH FINANCING AND INVESTING ACTIVITIES</b>		
Market adjustment for greenhouse gas allowances	\$ -	\$ 15,122
Noncash contributions by developers	\$ 450	\$ 282
Capitalized interest	\$ 859	\$ 3,210
Amortization	\$ 1,222	\$ 2,402
Change in arbitrage liability	\$ (550)	\$ (471)
Bond proceeds used in refunding debt	\$ (112,395)	\$ (31,847)
Unrealized gain (loss) on investments	\$ (1,618)	\$ (394)

See accompanying notes to financial statements.

	<i>(Dollars in Thousands)</i>	
	<u>2016</u>	<u>2015</u>
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH FLOWS PROVIDED BY OPERATING ACTIVITIES</b>		
Operating income	\$ 66,629	\$ 63,005
Adjustments to reconcile operating income to net cash flows provided by operating activities		
Other non-operating income	4,568	5,077
Depreciation and amortization	38,105	33,954
Undistributed income from public power agencies	(12,614)	(11,979)
Distributions from public power agencies	4,237	-
Change in operating assets, liabilities, and deferred inflows		
Customer accounts receivable, net	(940)	883
Wholesale power receivables	(5)	74
Other current assets, net	(3,326)	(5,035)
Materials and supplies	13,832	(178)
Prepayments	1,633	(328)
Regulatory assets	-	(61,254)
Accounts payable and other accruals	(466)	(2,094)
Pension related deferrals and liabilities	3,089	62,824
Unearned revenue and other liabilities	(1,352)	4,876
	<u>113,390</u>	<u>89,825</u>
<b>NET CASH FLOWS PROVIDED BY OPERATING ACTIVITIES</b>	<b>\$ 113,390</b>	<b>\$ 89,825</b>
 <b>RECONCILIATION OF CASH AND CASH EQUIVALENTS TO BALANCE SHEET ACCOUNTS</b>		
Cash and cash equivalents - unrestricted	\$ 91,100	\$ 105,114
Cash and cash equivalents - restricted	8,581	9,385
Investments - unrestricted	103,995	77,962
Cash and investments - restricted	112,561	111,486
Capital improvement fund	<u>9,799</u>	<u>21,435</u>
Total Cash and Investments	326,036	325,382
Less: Noncash equivalents	<u>(202,886)</u>	<u>(169,482)</u>
<b>CASH AND CASH EQUIVALENTS</b>	<b>\$ 123,150</b>	<b>\$ 155,900</b>

See accompanying notes to financial statements.

# MODESTO IRRIGATION DISTRICT

## STATEMENTS OF FIDUCIARY NET POSITION As of December 31, 2016 and 2015

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	<i>(Dollars in Thousands)</i>	
	<u>2016</u>	<u>2015</u>
<b>ASSETS</b>		
<b>CASH AND CASH EQUIVALENTS</b>	\$ 13,049	\$ 5,814
<b>RECEIVABLES</b>		
Accrued interest	256	392
Dividends	29	30
<b>INVESTMENTS AT FAIR VALUE</b>		
Fixed income securities	56,662	57,368
Publicly traded domestic stocks	111,251	100,305
Publicly traded international stocks	34,896	32,303
Real estate investment trust	12,037	12,472
Stable value	14,646	8,156
Mutual funds	129,162	125,259
Hedge funds	15,649	22,173
Total Assets	<u>387,637</u>	<u>364,272</u>
<b>LESS: ACCRUED LIABILITIES</b>	<u>827</u>	<u>901</u>
<b>NET POSITION HELD IN TRUST FOR RETIREE BENEFITS</b>	<u>\$ 386,810</u>	<u>\$ 363,371</u>

See accompanying notes to financial statements.

# MODESTO IRRIGATION DISTRICT

## STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION As of December 31, 2016 and 2015

	<i>(Dollars in Thousands)</i>	
	<u>2016</u>	<u>2015</u>
<b>ADDITIONS</b>		
Additions to net position attributed to:		
Investment income:		
Net appreciation (depreciation) of investments	\$ 19,517	\$ (7,610)
Dividend income	5,154	5,910
Interest income	1,969	2,438
Investment expenses	<u>(1,106)</u>	<u>(1,234)</u>
Net investment income	25,534	(496)
Contributions		
Employee contributions	2,854	2,381
Employer contributions	21,766	21,202
Other contributions	<u>51</u>	<u>342</u>
Total Contributions	<u>24,671</u>	<u>23,925</u>
 Total Additions	 <u>50,205</u>	 <u>23,429</u>
<b>DEDUCTIONS</b>		
Deductions from net position attributed to:		
Distributions to plan members and beneficiaries	21,103	18,987
Medical premiums paid	5,440	5,061
Administrative expenses	188	171
Consultant and professional services expenses	<u>35</u>	<u>35</u>
Total Deductions	<u>26,766</u>	<u>24,254</u>
 <b>Net increase (decrease) in net position held in trust for retiree benefits</b>	 23,439	 (825)
<b>NET POSITION HELD IN TRUST FOR RETIREE BENEFITS</b>		
Beginning of year	<u>363,371</u>	<u>364,196</u>
 <b>END OF YEAR</b>	 <u>\$ 386,810</u>	 <u>\$ 363,371</u>

See accompanying notes to financial statements.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 1 – ORGANIZATION AND DESCRIPTION OF BUSINESS**

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The Modesto Irrigation District (the "District") was formed in 1887 and operates as a nonregulated special district of the State of California. The District provides electric power on an exclusive basis within a 160 square mile service area in Stanislaus County and in the Don Pedro Reservoir area in Tuolumne County. The District also provides electric power in portions of southern San Joaquin County. The District provides irrigation water to an area of California's Central Valley that lies between the Tuolumne and Stanislaus rivers. The District also operates a surface water treatment plant that provides water for the City of Modesto's (the "City") domestic water supply.

The District is managed by a Board of Directors. The District's Board of Directors has the authority to fix rates and charges for the District's commodities and services. As a public power utility, the District is not subject to regulation or oversight by the California Public Utilities Commission (CPUC). The District may also incur indebtedness including issuing bonds. The District is exempt from payment of federal and state income taxes.

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

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The financial statements of the District have been prepared in conformity with accounting principles generally accepted in the United States of America. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The significant accounting principles and policies utilized by the District are described below.

### ***REPORTING ENTITY***

As required by accounting principles generally accepted in the United States of America, these financial statements present the District, its component unit, the Modesto Irrigation District Financing Authority (the "Authority"), and the following fiduciary funds (collectively referred to as "the Plan"):

Retirement System Basic Retirement Plan (a pension trust fund) is a single-employer noncontributory defined benefit plan for all eligible District employees and Directors.

Retirement System Supplemental Retirement Plan (a pension trust fund) is a defined contribution plan and serves as partial or full replacement of social security for participants, depending upon date of employment.

Retiree Medical Benefits Plan (an other post-employment benefit trust fund) is a single-employer defined benefit healthcare plan for all eligible retirees and their spouses.

The Authority, a joint power authority composed of the District and the City of Redding, provides financing for public improvements of the District. The District's Board of Directors serves as the Authority's Board, and District employees provide all of the Authority's administrative and management functions. All of the Authority's financial transactions, except the payment of debt service, are transacted with the District. Accordingly, all operations of the Authority are consolidated into the District's financial statements.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)**

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### ***MEASUREMENT FOCUS, BASIS OF ACCOUNTING AND FINANCIAL STATEMENT PRESENTATION***

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used. Revenues, expenses, gains, losses, assets, deferred outflows of resources, liabilities and deferred inflows of resources resulting from exchange and exchange-like transactions are recognized when the exchange takes place. The District's accounting records generally follow the Uniform System of Accounts for Public Utilities and Licensees prescribed by the Federal Energy Regulatory Commission (FERC).

In February 2015, the GASB issued Statement No. 72 – *Fair Value Measurement and Application*. The statement addresses accounting and financial reporting issues to fair value measurements. It defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This standard was implemented January 1, 2016.

Presentation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect 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.

### ***CASH AND CASH EQUIVALENTS***

Cash equivalents include all debt instruments with maturity dates of 90 days or less from the date of purchase and all investments in the Local Agency Investment Fund (LAIF), and money market mutual funds. LAIF has an equity interest in the State of California Pooled Money Investment Account (PMIA). PMIA funds are on deposit with the State's Centralized Treasury System and are managed in compliance with the California Government Code, according to a statement of investment policy which sets forth permitted investment vehicles, liquidity parameters and maximum maturity of investments. The PMIA cash and investments are recorded at amortized cost which approximates fair value. The District's deposits with LAIF are generally available for withdrawal on demand.

### ***INVESTMENTS***

Generally, all investments are carried at their fair value, except for guaranteed investment contracts (GICs), which are carried at cost. Fair values are based on methods and inputs as outlined in Note 3. Fair values may have changed significantly after year-end.



# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)**

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### ***DERIVATIVE FINANCIAL INSTRUMENTS***

The District's Basic Retirement Plan has foreign currency forward contracts, which meet the definition of derivative financial instruments and are immaterial to the Plan. The derivative instruments are recorded on the statements of fiduciary net position at fair value, with a corresponding charge to appreciation (depreciation) in the statement of changes in fiduciary net position. Fair value is based on quoted market prices. The District's Basic Retirement Plan's derivative transactions are designed to reduce foreign currency exchange risk.

The District's derivative instruments are discussed in Note 8.

### ***ALLOWANCE FOR DOUBTFUL ACCOUNTS***

The District recognizes an estimate of uncollectible accounts for its customer accounts receivable related to electric service based upon its historical experience with collections. The District has an allowance for doubtful accounts for its electric retail customers of \$428 and \$1,141 as of December 31, 2016 and 2015, respectively. The District's net expense relating to doubtful accounts for all accounts receivable is included in the accompanying statements of revenues, expenses, and changes in net position as an offset to operating revenues. The District recorded bad debt expense of \$658 and \$751 at December 31, 2016 and 2015, respectively.

### ***MATERIALS AND SUPPLIES***

Materials and supplies are generally used for construction, operation and maintenance work, and are not for resale. They are valued at the lower of cost or fair value utilizing the average cost method and charged to construction or expense when used.

The balance includes greenhouse gas allowances used for generation. These are valued at the lower of cost or fair value utilizing the average cost method and charged to generation expense when used. Any allowances held for sale are recorded at fair value at year end.

### ***RESTRICTED ASSETS***

Mandatory segregations of assets are presented as restricted assets. Such segregations are required by bond agreements and other external parties. Current liabilities payable from these restricted assets are so classified.

### ***CAPITAL IMPROVEMENT FUND***

The District bills each customer a per kilowatt-hour capital infrastructure surcharge. These funds are segregated to pay for future capital improvements.

### ***PREPAYMENTS***

The balance represents payments to vendors for costs applicable to future accounting periods.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)**

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### ***REGULATORY COSTS FOR FUTURE RECOVERY***

As a regulated entity, the District's financial statements are prepared in accordance with GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which require that the effects of the rate making process be recorded in the financial statements. Accordingly, certain expenses and credits normally reflected in the change in net position as incurred are recognized when included in rates. The District records regulatory assets and credits to reflect rate-making actions of the Board. The account includes the unamortized debt issuance costs of previously issued bonds of the District and the unfunded net pension liability under GASB Statement No. 68.

### ***OTHER CURRENT AND LONG-TERM ASSETS***

The balance represents miscellaneous receivables and deposits. \$2,128 and \$2,396 of the 2016 and 2015 balances, respectively, are receivables from the City of Modesto for a domestic water pipeline project. Approximately \$1,854 and \$2,130 of the 2016 and 2015 balances, respectively, are not expected to be collected within one year. The balance of other long-term assets also includes the net OPEB asset, discussed in Note 9, and a receivable from TANC, discussed in Note 6.

### ***CAPITAL ASSETS***

Capital assets are generally defined by the District as assets with an initial, individual cost of more than \$5 and an estimated useful life in excess of three years.

Capital assets are stated at cost. Costs and related accumulated depreciation of assets sold or otherwise disposed of are eliminated from the accounts and related gains or losses are considered non-operating. The costs of replacement are charged to District plant. Repair and maintenance costs are charged to expense in the period incurred. Interest costs incurred less any related interest earned during periods of construction of District plant assets are capitalized at a rate based on the District's borrowings related to that construction.

Depreciation is computed using the straight-line method over the useful lives of the assets, which generally range from twenty to fifty years for electric and domestic water plant assets and ten to one hundred years for irrigation system assets. The estimated useful lives of furniture, fixtures, equipment and other assets range from five to twenty years.

### ***DEFERRED OUTFLOWS OF RESOURCES***

A deferred outflow of resources represents a consumption of net position that applies to a future period and will not be recognized as an outflow of resources (expense) until that future time.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)**

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### ***ACCRUED VACATION***

Under terms of employment, employees are granted vacation time in varying amounts. Only benefits considered to be vested are disclosed in these statements. Vested vacation pay is accrued when earned in the financial statements. The liability is liquidated from general operating revenues of the District. At December 31, 2016 and 2015, the District recorded accrued vacation time of \$3,210 and \$3,046, respectively. The liability is included in accounts payable and other accruals in the accompanying balance sheet.

### ***OTHER LIABILITIES***

Other liabilities include customer meter deposits, power cost true-ups, potential rate refunds, arbitrage liability, and other miscellaneous long-term liabilities.

### ***ASSET RETIREMENT OBLIGATIONS***

The District has identified potential retirement obligations related to certain transmission, distribution and irrigation canal facilities located on properties that do not have perpetual lease rights. The District's nonperpetual leased land rights generally are renewed continuously because the District intends to utilize these facilities indefinitely. Since the timing and extent of any potential asset retirements are unknown, the fair value of any obligations associated with these facilities cannot be reasonably estimated. Accordingly, a liability has not been recorded at December 31, 2016 and 2015 for these assets.

The District has identified retirement obligations for transformers that are known to contain PCB oil and has estimated a liability for the disposal of these transformers at retirement at the discounted value of estimated future cash outflows. The retirement obligation was written-off in 2015 due to the District generating more revenues from the scrap material of the transformers than the cost to dispose.

The District accrues costs related to capital assets when an obligation to decommission facilities or other liability is legally required.

### ***NET PENSION LIABILITY***

A net pension liability is recorded in accordance with GASB Statement No. 68. The liability is the difference between the actuarial total pension liability and the Plan's fiduciary net position as of the measurement date. See Note 9 for additional information.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)**

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### ***LONG-TERM DEBT***

Long-term debt and other obligations are reported as liabilities. Bond premiums and discounts are amortized over the life of the bonds using the effective interest rate method. Gains or losses on prior refundings are amortized over the remaining life of the old debt or the life of the new debt, whichever is shorter. The balance at year end for premiums and discounts is shown as an increase or decrease in the liability section of the balance sheet. The balance at year end for the loss on refunding is shown as a deferred outflow of resources in the balance sheet.

### ***DEFERRED INFLOWS OF RESOURCES***

A deferred inflow of resources represents an acquisition of net position that applies to a future period and therefore will not be recognized as an inflow of resources (revenue) until that future time.

Billings to the City in connection with the Domestic Water Project (the "Project") in advance of the operation of the facility were recorded as unearned revenues. Annual differences between billings to the City and the District's annual Project costs are charged or credited to unearned revenues. These differences are being amortized over the life of the facility. Accordingly, the District's financial statements reflect Domestic Water operations on a break-even basis, consistent with the operating agreements between the District and the City.

### ***NET POSITION***

GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, requires the classification of net position into three components – net investment in capital assets; restricted; and unrestricted. These classifications are defined as follows:

*Net investment in capital assets* – This component of net position consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net position component as the unspent proceeds.

*Restricted* – this component of net position consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

*Unrestricted* – This component of net position consists of net position that does not meet the definition of "restricted" or "net investment in capital assets".

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

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)**

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### ***REVENUES AND EXPENSES***

The District 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 the District's principal ongoing operations. The principal operating revenues of the District are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

### ***Electric and Irrigation Revenues***

Retail and wholesale electric revenues are billed on the basis of monthly cycle bills and are recorded as revenue when the electricity is delivered. The District records an estimate for unbilled revenues earned from the dates its retail customers were last billed to the end of the month. At December 31, 2016 and 2015, unbilled revenues of \$20,771 and \$20,025, respectively, are included in customer accounts receivable in the balance sheet.

Irrigation revenues are recognized when billed based on annual assessments, payable with installment payments due in June and December.

### ***Purchased Power***

The majority of the District's power needs are provided by power purchases. These power purchases are principally made under long-term agreements with the M-S-R Public Power Agency and the Hetch Hetchy System, owned and operated by the City and County of San Francisco. Additionally, the District purchases power from others under various power purchase agreements. Gains or losses on power purchase and sale transactions that are settled without physical delivery are recorded as net additions or reductions to purchased power expense.

### ***Capital Contributions***

Cash and capital assets are contributed to the District from customers and external parties. The value of property contributed to the District is reported as capital contributions on the statements of revenues, expenses and changes in net position.

### ***COMPARATIVE DATA***

Certain amounts presented in the prior year data have been reclassified in order to be consistent with the current year's presentation.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)**

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### ***EFFECT OF NEW ACCOUNTING STANDARDS ON CURRENT PERIOD FINANCIAL STATEMENTS***

GASB has approved GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*, Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, Statement No. 80, *Blending Requirements for Certain Component Units, an amendment of GASB Statement No. 14*, Statement No. 81, *Irrevocable Split-Interest Agreements*, Statement No. 82, *Pension Issues, an amendment of GASB Statements No. 67, No. 68, and No. 73*, Statement No. 83, *Certain Asset Retirement Obligations*, Statement No. 84, *Fiduciary Activities*, and Statement No. 85, *Omnibus 2017*. When they become effective, application of these standards may restate portions of these financial statements.

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## **NOTE 3 – CASH AND INVESTMENTS**

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The District's investment policies are governed by the California Government Codes and its bond Indenture, which restricts the District's investment securities to obligations which are unconditionally guaranteed by the United States (U.S.) Government or its agencies or instrumentalities; direct and general obligations of the State of California (State) or any local agency within the State; bankers' acceptances; commercial paper; certificates of deposit; time certificates of deposit; repurchase agreements; reverse repurchase agreements or securities lending agreements; medium-term corporate notes; shares of beneficial interest; mortgage pass-through securities; financial futures and financial option contracts; and deposits with the LAIF. Investments in LAIF are unregistered, pooled funds. LAIF is a component of the Pooled Money Investment Account Portfolio managed by the State Treasurer, in accordance with Government Code Sections 16430 and 16480. The fair value of the District's investments in LAIF approximates the value of its pool shares.

The District's investment policy includes restrictions for investments relating to maximum amounts invested as a percentage of total portfolio and with a single issuer, maximum maturities, and minimum credit ratings.

Deposits in each local and area bank are insured by the FDIC in the amount of \$250 for time and savings accounts (including NOW accounts), \$250 for interest-bearing demand deposit accounts (interest bearing and noninterest bearing). In addition, if deposits are held in an institution outside of the state in which the government is located, insured amounts are further limited to a total of \$250 for the combined amount of all deposit accounts.

The District maintains a rate stabilization fund to protect District customers from extreme rate increases that would otherwise be necessitated by dramatic short-term changes in purchased power or other operating costs. Annual transfers into and out of the fund are determined by the District's Board of Directors (Board), which may utilize these unrestricted funds for any lawful purposes. The rate stabilization fund consists of an undivided portion of the District's general operating funds. No transfers occurred during fiscal years 2016 and 2015.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 3 – CASH AND INVESTMENTS (cont.)**

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The Plan investment policies are governed primarily by the “Prudent Person Rule” which restricts the Plan’s investments to only those securities which would be selected by a person of prudence, diligence and intelligence in the management of his or her own affairs, giving due consideration to safety or principal and income. The Plan, under the guidelines of its investment policies, is authorized to invest its cash in various financial instruments, including cash and equivalents, domestic equities, international equities, convertible securities, bankers acceptances, commercial paper, certificates of deposit, repurchase and reverse repurchase agreements, financial futures, financial option contracts, medium term notes, corporate bonds, shares issued by diversified management companies, hedge funds, and deposits with the LAIF.

The Plan’s investment policy and guidelines are established by and may be amended by the District’s Retirement Committee (the “Committee”) and the District’s Board of Directors. The Committee is responsible for overseeing the investment management of the Plan. This includes, but is not limited to, reviewing and evaluating investment activities regularly to assure that the Plan’s investment policy and guidelines are followed.

The Plan’s investment policy includes restrictions for investments related to maximum amounts invested as a percentage of total portfolios, with a single issuer, and within market sectors and styles, minimum market capitalization, maximum maturities, and minimum credit ratings.

### ***DISTRICT CASH AND INVESTMENTS (EXCLUSIVE OF THE FIDUCIARY FUNDS)***

The following disclosures relate to the District, exclusive of the fiduciary funds.

The District categorizes its fair value measurements 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 asset (liability). 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.

The valuation methods for recurring fair value measurements include the following:

- > Institutional bond quotes for US government agency securities, corporate medium term notes, and US Treasuries.
- > Trader-entered price information for money market mutual funds.
- > JJ Kenny municipal information for municipal bonds.
- > Market prices at year end for California Carbon Allowances for inventory held for sale.
- > Bloomberg pricing of similar assets for its interest rate swap.
- > Market information from NYMEX for its natural gas swaps and futures.

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

### NOTE 3 – CASH AND INVESTMENTS (cont.)

#### *DISTRICT CASH AND INVESTMENTS (EXCLUSIVE OF THE FIDUCIARY FUNDS) (cont.)*

The following table sets forth by level, within the fair value hierarchy, the District's assets at fair value as of December 31, 2016 and 2015:

Investment Type	December 31, 2016			Total
	Level 1	Level 2	Level 3	
US Government Agencies	\$ -	\$ 115,652	\$ -	\$ 115,652
US Treasury Notes	31,261	-	-	31,261
Money Market Funds	47,078	-	-	47,078
Corporate Medium Term Notes	-	32,026	-	32,026
Municipal Bonds	-	4,056	-	4,056
Derivative Financial Instruments	(890)	(25,837)	-	(26,727)
<b>Total</b>	<b>\$ 77,449</b>	<b>\$ 125,897</b>	<b>\$ -</b>	<b>\$ 203,346</b>

Investment Type	December 31, 2015			Total
	Level 1	Level 2	Level 3	
US Government Agencies	\$ -	\$ 103,560	\$ -	\$ 103,560
Money Market Funds	81,858	-	-	81,858
Corporate Medium Term Notes	-	40,097	-	40,097
Municipal Bonds	-	4,064	-	4,064
Inventory Held for Sale	-	15,122	-	15,122
Derivative Financial Instruments	(2,790)	(27,659)	-	(30,449)
<b>Total</b>	<b>\$ 79,068</b>	<b>\$ 135,184</b>	<b>\$ -</b>	<b>\$ 214,252</b>

#### ***Custodial Credit Risk***

##### **Deposits**

Custodial credit risk is the risk that in the event of a financial institution failure, the District's deposits may not be returned to the District.

As of December 31, 2016 and 2015, none of the District's bank balances are known to be individually exposed to custodial credit risk.

The District's investment policy does not address this risk.



# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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## NOTE 3 – CASH AND INVESTMENTS (cont.)

### *DISTRICT CASH AND INVESTMENTS (EXCLUSIVE OF THE FIDUCIARY FUNDS) (cont.)*

#### *Custodial Credit Risk (cont.)*

#### **Investments**

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party.

As of December 31, 2016 and 2015, the District's investments were exposed to custodial credit risk as follows:

Neither Insured Nor Registered and Held by the Counterparty's Trust Department or Agent in the District's Name	2016	2015
US Agencies Implicitly Guaranteed	\$ 27,740	\$ 48,658
US Agencies Explicitly Guaranteed	87,912	54,902
Corporate Medium Term Notes	32,026	40,097
Municipal Bonds	4,056	4,064
US Treasury	-	-
	31,261	
Totals	\$ 182,995	\$ 147,721

The District's investment policy addresses this risk. All securities owned by the District shall be held in safekeeping by a third party custodian, acting as agent for the District under the terms of a custody agreement.

#### **Credit Risk**

Credit risk is the risk an issuer or other counterparty to an investment will not fulfill its obligations.

As of December 31, 2016 and 2015, the District's investments were rated as follows:

Investment Type	Standard & Poors	
	2016	2015
LAIF	NR	NR
Money Market Mutual Funds	NR	NR
Federal Farm Credit Bank Notes	AA+	AA+
Federal Home Loan Bank Bonds	AA+	AA+
Corporate Medium Term Notes	AA- - A+	BBB+ - AA+
Investment Agreement Contracts	NR	NR
Municipal Bonds	AA-	AA-
US Treasury	n/a	-

The District's investment policy addresses this risk. The District limits investments to those allowed by Sections 53601 of the California Government code that address the risk allowable for each investment.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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## NOTE 3 – CASH AND INVESTMENTS (cont.)

### *DISTRICT CASH AND INVESTMENTS (EXCLUSIVE OF THE FIDUCIARY FUNDS) (cont.)*

#### **Concentration of Credit Risk**

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer.

At December 31, 2016 and 2015, the District's investment portfolio was concentrated as follows:

Investment Type	Percentage of Portfolio	
	2016	2015
Corporate Medium Term Notes	10%	13%
Federal Home Loan Bank Bonds	7%	9%
Federal Farm Credit Bank Notes	2%	7%

The District's investment policy addresses this risk and places limits on the amounts invested in specific types of investments.

#### **Interest Rate Risk**

Interest rate risk is the risk changes in interest rates will adversely affect the fair value of an investment.

As of December 31, 2016, the District's investments exposed to interest rate risk were as follows:

Investment Type	Fair Value	Investment Maturities in Years		
		Less than 1 Year	1 – 5 Years	Greater than 5 Years
Federal Home Loan Bank Bonds	\$ 21,750	\$ -	\$ 21,750	\$ -
Fannie Mae	50,059	2,001	48,058	-
Federal Farm Credit Bank Notes	5,990	5,990	-	-
Freddie Mac	37,852	-	37,852	-
Corporate Medium Term Notes	32,026	6,992	25,034	-
LAIF	61,209	61,209	-	-
Money Market Fund	46,985	46,985	-	-
Municipal Bonds	4,056	-	4,056	-
US Treasury	31,261	-	31,261	-
Totals	<u>\$ 291,188</u>	<u>\$ 123,177</u>	<u>\$ 168,011</u>	<u>\$ -</u>

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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## NOTE 3 – CASH AND INVESTMENTS (cont.)

### *DISTRICT CASH AND INVESTMENTS (EXCLUSIVE OF THE FIDUCIARY FUNDS) (cont.)*

#### *Interest Rate Risk (cont.)*

As of December 31, 2015, the District's investments exposed to interest rate risk were as follows:

Investment Type	Fair Value	Investment Maturities in Years		
		Less than 1 Year	1 – 5 Years	Greater than 5 Years
Federal Home Loan Bank Bonds	\$ 27,783	\$ 1,998	\$ 25,785	\$ -
Fannie Mae	30,957	1,998	28,959	-
Federal Farm Credit Bank Notes	20,875	1,995	18,880	-
Freddie Mac	23,945	10,001	13,944	-
Corporate Medium Term Notes	40,097	15,094	25,003	-
LAIF	49,697	49,697	-	-
Money Market Fund	81,858	81,858	-	-
Municipal Bonds	4,064	-	4,064	-
<b>Totals</b>	<b>\$ 279,276</b>	<b>\$ 162,641</b>	<b>\$ 116,635</b>	<b>\$ -</b>

Though the District has restrictions as to the maturities of some of the investments, it does not have a formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increases in interest rates.

#### ***FIDUCIARY FUND INVESTMENTS***

The Plans categorize its fair value measurements 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 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.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of relevant observables and minimize the use of unobservable inputs.

The valuation methods for recurring fair value measurements include the following:

- > Fixed income securities, publicly traded domestic stocks, publicly traded international stocks, and the real estate investment trust are valued at the most recent closing price reported on the market on which individual securities are traded. The level 3 publicly traded international stocks are valued based on a manual method using pricing provided by various sources as the issuer, investment manager, fund accountant, etc. or default price if a price is not provided.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
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## NOTE 3 – CASH AND INVESTMENTS (cont.)

### *FIDUCIARY FUND INVESTMENTS* (cont.)

- > Mutual funds are valued at the daily closing price as reported by the fund. Mutual funds held by the Plan are open-end mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily net asset value (NAV) and to transact at that price. The level 2 and level 3 mutual funds are valued based on a manual method using pricing provided by various sources such as the issuer, investment manager, fund accountant, etc. or default price if a price is not provided.
- > The hedge funds are collective funds that seek to maintain a stable net asset value.
- > Stable value fund is a collective fund that seeks to maintain a stable net asset value. It invests primarily in a diversified portfolio of fixed income securities from US and foreign issuers, including corporate, mortgage-backed, and government, and agency bonds.

The preceding methods may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Plan believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following table sets forth by level, within the fair value hierarchy, the Plan's assets at fair value as of December 31, 2016 and 2015:

Investment Type	December 31, 2016			Total
	Level 1	Level 2	Level 3	
Money Market Funds	\$ 72	\$ -	\$ -	\$ 72
Mutual Funds	121,102	4,776	3,214	129,092
Fixed Income Securities	2,128	54,534	-	56,662
Publicly Traded Domestic Stocks	111,251	-	-	111,251
Publicly Traded International Stocks	16,541	-	18,355	34,896
Real Estate Investment Trust	976	11,061	-	12,037
<b>Total</b>	<b>\$ 252,070</b>	<b>\$ 70,371</b>	<b>\$ 21,569</b>	<b>344,010</b>
Investments measured at the net asset value				
Hedge funds				15,649
Stable value				14,646
<b>Total Investments Measured at Fair Value</b>				<b>\$ 374,305</b>

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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### NOTE 3 – CASH AND INVESTMENTS (cont.)

#### *FIDUCIARY FUND INVESTMENTS* (cont.)

Investment Type	December 31, 2015			Total
	Level 1	Level 2	Level 3	
Money Market Funds	\$ 208	\$ -	\$ -	\$ 208
Mutual Funds	118,129	4,491	2,639	125,259
Fixed Income Securities	10,098	47,270	-	57,368
Publicly Traded Domestic Stocks	100,305	-	-	100,305
Publicly Traded International Stocks	16,688	-	15,615	32,303
Real Estate Investment Trust	982	11,490	-	12,472
Total	<u>\$ 246,410</u>	<u>\$ 63,251</u>	<u>\$ 18,254</u>	327,915
Investments measured at the net asset value				
Hedge funds				22,173
Stable value				<u>8,156</u>
Total Investments Measured at Fair Value				<u>\$ 358,244</u>

*Investments Measured Using NAV per Share Practical Expedient:* These funds have no unfunded commitments, the redemption frequency is Daily – Bi-annually, and the redemption notice period ranges from 0 – 92 days.

#### ***Custodial Credit Risk***

##### **Deposits**

As of December 31, 2016 and 2015, \$2,591 and \$3,883, of the Plan's bank balances are known to be exposed to custodial credit risk, respectively.

The Plan's investment policy does not address this risk.

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
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### NOTE 3 – CASH AND INVESTMENTS (cont.)

#### *FIDUCIARY FUND INVESTMENTS* (cont.)

##### **Credit Risk**

As of December 31, 2016 and 2015, the Plan's investments were rated as follows:

Investment Type	Standard & Poors	
	2016	2015
LAIF	NR	NR
Publicly Traded Domestic Stocks	NR	NR
Publicly Traded International Stocks	NR	NR
REIT	NR	NR
Hedge Funds	NR	NR
Prudential Core Plus Bond	A2 (Moody's)	-
Asset Backed Securities	AAA – BBB, n/a	AAA – A, n/a
Freddie Mac Pool	n/a	n/a
Fannie Mae Pool	n/a	n/a
Corporate Notes	AAA – BB+	AA+ – BB+
Corporate and Foreign Bonds	AAA – BB-, n/a, NR	AA- – B-, n/a, NR
Private Placements	A- - BBB-, NR	A+ – BB-, NR
U.S. Government Treasury	n/a	n/a
Mortgage Backed Obligation	A	A
Income Funds*	-	NR

To mitigate the risk that an issuer of an investment will not fulfill its obligation to the owner of the investment, the Plan limits investments in certain securities to those that met or exceed certain minimum credit ratings established by nationally recognized rating agencies. Commercial paper must be rated at a minimum of A-1 and P-1 by Standard & Poor's and Moody's, respectively. Bankers acceptances and certificates of deposit must have been purchased from larger well-capitalized banks with a minimum of an A rating from one of the major rating agencies. Banker's acceptances must also be eligible for both purchases and discount by the Federal Reserve Bank. The pooled fund investments with LAIF are not rated. Noninvestment Grade securities may be purchased up to a maximum of 20% of the portfolio value. The preceding table shows the Standard and Poor's (S&P) credit ratings of the Plan's deposits and investments, at December 31, 2016 and 2015.

\*As of December 31, 2015, the Plans are invested in income funds which are not rated, but are significantly invested in U.S. Government Treasury and Agency investments.

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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### NOTE 3 – CASH AND INVESTMENTS (cont.)

#### *FIDUCIARY FUND INVESTMENTS (cont.)*

##### ***Interest Rate Risk***

As of December 31, 2016, the Plan's investments exposed to interest rate risk were as follows:

Investment Type	Fair Value	Investment Maturities in Years		
		Less than 1 Year	1 – 5 Years	Greater than 5 Years
Asset Backed Securities	\$ 4,322	\$ -	\$ 1,563	\$ 2,759
Corporate and & Foreign Bonds	10,616	199	1,763	8,654
Commercial Mortgage Backed Securities	88	-	88	-
Freddie Mac Pool	2,038	-	-	2,038
Fannie Mae Pool	2,394	-	-	2,394
Corporate Bonds/Notes	9,453	447	5,296	3,710
Private Placements	1,907	113	1,223	571
Prudential Core Plus Bond	37,914	-	-	37,914
U.S. Government Treasury	2,128	-	1,581	547
<b>Totals</b>	<b>\$ 70,860</b>	<b>\$ 759</b>	<b>\$ 11,514</b>	<b>\$ 58,587</b>

As of December 31, 2015, the Plan's investments exposed to interest rate risk were as follows:

Investment Type	Fair Value	Investment Maturities in Years		
		Less than 1 Year	1 – 5 Years	Greater than 5 Years
Asset Backed Securities	\$ 9,512	\$ -	\$ 3,367	\$ 6,145
Corporate and & Foreign Bonds	19,060	25	6,093	12,942
Commercial Mortgage Backed Securities	107	-	107	-
Freddie Mac Pool	2,622	-	-	2,622
Fannie Mae Pool	4,736	-	-	4,736
Corporate Bonds/Notes: Others	9,148	-	6,171	2,977
Private Placements	2,085	-	1,397	688
U.S. Government Treasury	10,098	-	7,077	3,021
<b>Totals</b>	<b>\$ 57,368</b>	<b>\$ 25</b>	<b>\$ 24,212</b>	<b>\$ 33,131</b>

The Plan has restrictions as to the maturities of some of the investments and has a formal policy that allocates investments to manage its exposure to fair value losses arising from increases in interest rates.

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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### NOTE 3 – CASH AND INVESTMENTS (cont.)

#### *FIDUCIARY FUND INVESTMENTS* (cont.)

##### *Interest Rate Risk* (cont.)

As of December 31, 2015, the retiree medical plan had fair value investments in the PIMCO funds of \$10,034. As of December 31, 2015 PIMCO funds' weighted average maturity (in years) was 8.40.

As of December 31, 2015, the retiree medical plan had fair value investments in the Dodge & Cox funds of \$3,969. As of December 31, 2015 the funds' maturity diversification was as follows:

Investment Maturities in Years	Percentage
Less than 1 Year	4.7%
1 – 5 Years	50.0
5 – 10 Years	23.5
10 – 15 Years	2.7
15 – 20 Years	5.0
20 – 25 Years	8.7
25 and Over	5.4

##### *Foreign Currency Risk*

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit denominated in a foreign currency.

The Plan had investments in mutual funds which were exposed to foreign currency risk. The Plan's exposure to foreign currency risk in U.S. dollars as of December 31, 2016 and 2015 is summarized in the following table.

Currency by Investment and Fair Value	2016	2015
Australian Dollar	\$ 626	\$ 625
Canadian Dollar	281	-
Brazilian Real	669	1,413
British Pound	4,524	7,070
Euro	5,159	8,624
Hong Kong Dollar	456	293
Japanese Yen	3,463	3,930
Mexican Peso	50	443
New Zealand Dollar	739	1,195
Russian Ruble	89	819
South Korean Won	1,086	1,040
Swedish Krona	263	430
Swiss Franc	1,498	2,720
Other	2,201	5,719
Total Investment Fair Value	\$ 21,104	\$ 34,321



## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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### NOTE 3 – CASH AND INVESTMENTS (cont.)

#### *FIDUCIARY FUND INVESTMENTS* (cont.)

#### *Foreign Currency Risk* (cont.)

The Plan has restrictions relating to maximum amounts invested in certain non-U.S. investments, as a percentage of total portfolio, and with a single issuer. The Plan has a formal policy that allocates investments to manage its exposure to fair value losses arising from changes in currency exchange rates.

In addition, the Plan investments in international equity open-ended mutual funds stated at fair value as of December 31, 2016 and 2015 were:

Mutual Fund Name	2016 Fair Value	2015 Fair Value
Oppenheimer International Growth Fund	\$ 2,951	\$ 2,785
Brandes International Equity Fund	3,214	2,639
Totals	\$ 6,165	\$ 5,424

### NOTE 4 – RESTRICTED ASSETS

Certain proceeds of the District's debt, as well as certain resources set aside for their repayment, are classified as restricted assets on the balance sheet because their use is limited. The following accounts are reported as restricted assets:

	Carrying Value as of Year-End	
	2016	2015
Restricted Accounts		
Project fund	\$ 70,988	\$ 71,367
Reserve fund	40,686	39,242
Redemption fund	8,581	9,385
Domestic water and reserve contingency fund	887	877
Total Restricted Accounts	\$ 121,142	\$ 120,871

#### **DEBT RELATED ACCOUNTS**

- Redemption - Used to segregate resources accumulated for debt service payments over the next twelve months.
  
- Reserve - Used to report resources set aside to make up potential future deficiencies in the redemption account.
  
- Project - Used to report debt proceeds restricted for use in construction.

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
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### NOTE 4 – RESTRICTED ASSETS (cont.)

#### *DOMESTIC WATER RESERVE AND CONTINGENCY*

As a condition of the Treatment and Delivery Agreement with the City of Modesto for domestic water, the District has established an account for the payment of emergency maintenance items that arise.

#### *REMEDATION FUND*

As a condition of the Natural Gas and Supply Agreement with the M-S-R Energy Authority, the District has established a fund to track proceeds received from the sale of gas delivered per the supply agreement. These proceeds will be used for future gas supply needs. There was no balance in this account in either 2016 or 2015.

### NOTE 5 – CHANGES IN CAPITAL ASSETS

A summary of changes in capital assets for 2016 follows:

	Balance 1/1/16	Increases	Decreases	Balance 12/31/16
Capital assets, not being depreciated/amortized				
Land and land rights	\$ 35,013	\$ -	\$ 11	\$ 35,002
Intangibles assets, not being depreciated/amortized	5,262	105	-	5,367
Total Capital Assets Not Being Depreciated/Amortized	40,275	105	11	40,369
Capital assets being depreciated/amortized				
Intangible assets, being depreciated/ amortized	45,231	36	-	45,267
Electric system	849,999	16,789	464	866,324
Domestic water plant	215,777	1,083	-	216,860
Irrigation system	51,125	856	-	51,981
General and administrative facilities	72,558	2,868	1,785	73,641
Total Capital Assets Being Depreciated/Amortized	1,234,690	21,632	2,249	1,254,073
Total Capital Assets	1,274,965	21,737	2,260	1,294,442
Less: Accumulated depreciation/amortization	(582,648)	(38,105)	(2,166)	(618,587)
Construction in progress	24,600	38,020	21,277	41,343
Net Capital Assets	\$ 716,917	\$ 21,652	\$ 21,371	\$ 717,198

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
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### NOTE 5 – CHANGES IN CAPITAL ASSETS (cont.)

A summary of changes in capital assets for 2015 follows:

	Balance 1/1/15	Increases	Decreases	Balance 12/31/15
Capital assets, not being depreciated/amortized				
Land and land rights	\$ 35,009	\$ 4	\$ -	\$ 35,013
Intangibles assets, not being depreciated/amortized	5,262	-	-	5,262
Total Capital Assets Not Being Depreciated/Amortized	40,271	4	-	40,275
Capital assets being depreciated/amortized				
Intangible assets, being depreciated/ amortized	45,231	-	-	45,231
Electric system	833,930	16,860	791	849,999
Domestic water plant	108,774	107,003	-	215,777
Irrigation system	50,416	709	-	51,125
General and administrative facilities	71,021	2,386	849	72,558
Total Capital Assets Being Depreciated/Amortized	1,109,372	126,958	1,640	1,234,690
Total Capital Assets	1,149,643	126,962	1,640	1,274,965
Less: Accumulated depreciation/amortization	(550,293)	(33,954)	(1,599)	(582,648)
Construction in progress	111,109	40,170	126,679	24,600
Net Capital Assets	\$ 710,459	\$ 133,178	\$ 126,720	\$ 716,917

### NOTE 6 – INVESTMENT IN PUBLIC POWER AGENCIES

The District's investments in public power agencies are accounted for using the equity method of accounting and consist of the following at December 31, 2016 and 2015:

	2016	2015
M-S-R Public Power Agency	\$ (15,217)	\$ (24,116)
Transmission Agency of Northern California (TANC)	\$ 3,350	\$ 3,872

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
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## **NOTE 6 – INVESTMENT IN PUBLIC POWER AGENCIES (cont.)**

### ***M-S-R PUBLIC POWER AGENCY***

The District, the City of Santa Clara, and the City of Redding formed M-S-R Public Power Agency (Agency) for the principal purpose of acquiring electric power resources for the electric systems of its members. The District owns a 50% interest in generation assets owned by the Agency. The District's deficit investment derives from its proportionate interest in the Agency's deficit and the District's commitment to repay its share of the Agency's debt, among other costs and obligations, through its take-or-pay commitment. The generation activities of the Agency consist of a 28.8% ownership interest in a 507-megawatt (MW) unit of a coal-fired electricity generating plant located in New Mexico (the San Juan Plant). The Agency was a participant in the Southwest Transmission Project, a 500-kilovolt alternating current transmission line between Central Arizona and Southern California that provides a firm transmission path for the transmission of electric power from the San Juan plant. The Agency sold its interest in the Southwest Transmission Project in 2016. The District is obligated to make interest and other generation and transmission project related payments to the Agency commensurate with its 50% interest in the Agency, and receives 50% of the electrical power generated by the Agency. In 2006, the Agency entered into agreements with PPM Energy, Inc., now known as Iberdrola Renewables, Inc., to purchase renewable energy from the Big Horn wind project. The District's share of the Big Horn output is 12.5% and is obligated to make payments commensurate with its share of the project.

On July 31, 2015, the Agency entered into an agreement with the other participants of the San Juan Plant to exit its interest in the project effective December 31, 2017. At December 31, 2016, the Agency's net book value of the total construction work in progress and plant in service related to the San Juan project was \$70,082. The balance of the related bonds outstanding at December 31, 2016 was \$160,995. The District will remain liable for its proportionate share of the Agency's long-term debt related to the San Juan project.

During 2016 and 2015, the District incurred purchased power costs of \$56,391 and \$61,503, respectively, in connection with these Agency resources. At December 31, 2016 and 2015, the District had a payable of \$5,597 and \$6,550, respectively, to the Agency for its proportionate share of project related expenditures.

Summarized financial information of the Agency is as follows at December 31:

	2016	2015
Total assets	\$ 173,660	\$ 226,066
Total deferred outflows of resources	5,474	7,415
Total Assets and Deferred Outflows	\$ 179,134	\$ 233,481
Total liabilities	\$ 209,568	\$ 281,712
Total net position	(30,434)	(48,231)
Total Liabilities and Net Position	\$ 179,134	\$ 233,481
Changes in Net Position During the Year	\$ 17,797	\$ 22,038

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 6 – INVESTMENT IN PUBLIC POWER AGENCIES (cont.)**

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### ***M-S-R PUBLIC POWER AGENCY (cont.)***

The long term debt of the Agency, which totals \$160,995 and \$234,335 at December 31, 2016 and 2015, respectively, is secured by a pledge and assignment of the net electric revenues of the Agency and are supported by take-or-pay commitments, which are an operating expense of the Participant's electric system. The District's portion of the Agency's principal and interest payments during the year were \$18,767 and \$20,349 for December 31, 2016 and 2015, respectively.

### ***M-S-R ENERGY AUTHORITY***

The District, the City of Santa Clara, and the City of Redding formed M-S-R Energy Authority (Authority) for the principal purpose to acquire, construct, maintain, operate and finance projects for the benefit of any one or more of the Members. On September 10, 2009, the Authority entered into a series of thirty-year prepaid gas contracts with Citigroup Energy, Inc., which are financed by non-recourse revenue bonds. The Authority also entered into matching Natural Gas Supply Agreements ("Supply Agreements") whereby each member is obligated to purchase the natural gas from the Authority at a discount from the Index Price. The Supply Agreements will continue in effect until September 30, 2039, unless terminated earlier due to certain defaults, as set forth therein, or the termination of the matching prepaid gas contract. If the Authority fails on any day to deliver the quantity of natural gas required to be delivered pursuant to a Supply Agreement, the member will have no obligation for any of the natural gas supply that was not delivered as a result of such delivery default.

Billings to the members are designed to provide, over the life of the project, full recovery of costs as defined by the indenture and project contracts, and as prescribed by the Authority. Rates are structured to systematically provide for the current debt service requirements, operating costs and reserves. The net costs to be recovered from future participant billings consist primarily of timing differences related to the debt service requirements included in rates. In accordance with GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, certain income and expense amounts which would be recognized during the current time period are deferred and not included in the determination of income until such costs are recoverable through participant billings. Under the current rate structure, costs are expected to be recovered over the 30-year term of the Natural Gas Supply Agreement.

During 2016 and 2015, the District incurred purchased gas costs of \$3,992 and \$4,239, respectively, in connection with the Authority. At December 31, 2016 and 2015, the District had a payable of \$519 and \$374, respectively, for purchased gas and project related expenses.

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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### **NOTE 6 – INVESTMENT IN PUBLIC POWER AGENCIES (cont.)**

#### ***M-S-R ENERGY AUTHORITY (cont.)***

Summarized financial information of the Authority is as follows at December 31:

	2016	2015
Total Assets	<u>\$ 904,707</u>	<u>\$ 904,661</u>
Total liabilities	\$ 904,707	\$ 904,661
Total net position	<u>-</u>	<u>-</u>
Total Liabilities and Net Position	<u>\$ 904,707</u>	<u>\$ 904,661</u>
Changes in Net Position During the Year	<u>\$ -</u>	<u>\$ -</u>

The long term debt of the Authority totaled \$901,620 at December 31, 2016 and 2015. The Authority did not make any principal payments in 2016 or 2015. The District's portion of the Authority's interest payments during the year were \$13,211 in 2016 and 2015.

#### ***TRANSMISSION AGENCY OF NORTHERN CALIFORNIA (TANC)***

TANC is a joint power agency that owns a portion of the California Oregon Transmission Project (COTP), a transmission line between central California and southern Oregon. As of July 1, 2015, through a 25-year layoff agreement and the termination of a layoff between MID and some of the other TANC members, the District has a 23.5% ownership interest in TANC for a net total scheduling entitlement of 320 MW. As a result of the 2015 25-year layoff agreement, the District assumed the debt payment associated with the acquisition of approximately 25 MW of additional COTP transfer capability. TANC is entitled to approximately 87% of the 1,600 MW transmission capacity of the COTP. In addition, the District has a 34% share of TANC's transmission entitlement under the South of Tesla transmission agreements with Pacific Gas & Electric Company (PG&E) that provides the District with 102 MW of transmission between Tesla and Midway. The District is responsible for 34% of the South of Tesla operating costs. In July 2006, TANC changed the method used to invoice members for transmission costs. TANC began invoicing its members at the monthly TANC Open Access Transmission Tariff (OATT) rate. The OATT rate is charged to the member based on their entitlement share of kW. During 2016 and 2015, the District incurred transmission costs of \$12,126 and \$11,828, respectively, relating to these projects, which are included in purchased power expense in the accompanying statements of revenues, expenses and changes in net position. At December 31, 2016 and 2015, the District has a receivable from TANC in the amount of \$13,494 and \$10,493, respectively, included in other long-term assets in the accompanying balance sheet. In 2006, the District began selling excess transmission capabilities from the COTP transmission lines through TANC, as agent of the District. The District recognized \$1,101 and \$2,330 in revenues from transmission sales in the 2016 and 2015, respectively.

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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### **NOTE 6 – INVESTMENT IN PUBLIC POWER AGENCIES (cont.)**

#### ***TRANSMISSION AGENCY OF NORTHERN CALIFORNIA (TANC) (cont.)***

Summarized unaudited financial information of TANC is as follows at December 31:

	2016 (unaudited)	2015 (unaudited)
Total Assets and Deferred Outflows of Resources	\$ 340,882	\$ 392,239
Total liabilities and deferred inflows of resources	\$ 327,296	\$ 377,201
Total net position	13,586	15,038
 Total Liabilities, Deferred Inflows of Resources, and Net Position	 \$ 340,882	 \$ 392,239
 Changes in Net Position for 6 Months Ended	 \$ (10,363)	 \$ -

The long term debt of TANC (unaudited), which totals \$250,565 and \$286,964 at December 31, 2016 and 2015, respectively, is collateralized by a pledge and assignment of net revenues of each agency, supported by take-and-pay commitments of the District and the other members. Should other members of these agencies default on their obligations to the agencies, the District would be required to make “step up” payments to cover a portion of the defaulted payments. The District’s portion of TANC’s principal and interest payments during the year were \$2,457 and \$9,790 for December 31, 2016 and 2015, respectively.

#### ***BALANCING AUTHORITY OF NORTHERN CALIFORNIA (BANC)***

The District and three other California municipal utilities formed BANC in 2009. One new member joined in 2013. BANC was formed to perform North American Electric Reliability Corporation (NERC) functions that would otherwise be performed by the BANC members or on their behalf.

Summarized financial information of BANC is as follows at December 31:

	2016	2015
Total Assets	\$ 1,594	\$ 824
Total liabilities	\$ 1,594	\$ 824
Total net position	-	-
 Total Liabilities and Net Position	 \$ 1,594	 \$ 824
 Changes in Net Position During the Year	 \$ -	 \$ -

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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## **NOTE 6 – INVESTMENT IN PUBLIC POWER AGENCIES (cont.)**

### ***MODESTO IRRIGATION DISTRICT FINANCING AUTHORITY***

The Authority is a joint power authority that provides financing for public improvements of the District, and is accounted for as a component unit of the District. The revenues and expenses of the Authority are eliminated upon consolidation with the District. The Authority's summary financial information as of December 31, 2016 and 2015 and for the years then ended is as follows:

	2016	2015
<b>Assets</b>		
Current assets	\$ 12,744	\$ 11,579
Other noncurrent assets	87,592	87,667
Debt service installment receivable, less current portion	231,823	240,814
Total Assets	332,159	340,060
<b>Deferred Outflows of Resources</b>		
Total Assets and Deferred Outflows of Resources	\$ 360,297	\$ 370,499
<b>Liabilities and Net Position</b>		
Current liabilities	\$ 12,398	\$ 11,247
Derivative financial instruments	25,836	27,659
Long-term debt	321,821	331,418
Other noncurrent liabilities	242	175
Net position	-	-
Total Liabilities and Net Position	\$ 360,297	\$ 370,499
<b>Revenues and Expenses</b>		
Revenues:		
Debt service contributions	\$ 13,169	\$ 11,601
Interest income	784	397
Other non-operating income	1,343	1,323
Total Revenues	15,296	13,321
Interest expense	(15,296)	(13,321)
<b>Change in net position</b>	-	-
NET POSITION, Beginning of Year	-	-
<b>NET POSITION, END OF YEAR</b>	\$ -	\$ -



## MODESTO IRRIGATION DISTRICT

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### NOTE 6 – INVESTMENT IN PUBLIC POWER AGENCIES (cont.)

#### MODESTO IRRIGATION DISTRICT FINANCING AUTHORITY (cont.)

	2016	2015
<b>Cash Flows</b>		
Net cash used by noncapital financing activities	\$ (845)	\$ 74,017
Net cash provided by investing activities	(36,887)	(7,498)
<b>Net Change in Cash and Cash Equivalents</b>	(37,732)	66,519
CASH AND CASH EQUIVALENTS – Beginning of the Year	74,984	8,465
<b>CASH AND CASH EQUIVALENTS – END OF THE YEAR</b>	\$ 37,252	\$ 74,984

### NOTE 7 – LONG-TERM DEBT

#### LONG-TERM DEBT

The following bonds have been issued:

Date	Issue	Final Maturity	Interest Rate	Original Amount	Outstanding Amount 12/31/16
3/17/04	2004B Certificates of Participation Bonds	7/1/35	5.00 – 5.50%	\$ 66,025	\$ -
7/25/06	2006A Certificates of Participation Bonds	10/1/36	4.00 – 5.00	146,950	-
6/26/07	2007F Domestic Water Revenue Bonds	9/1/37	Index Rate	93,190	93,190
3/31/09	2009A Certificates of Participation	10/1/39	4.10 – 6.10	132,145	116,545
6/23/10	2010A Taxable Electric System Revenue Bonds	10/1/40	4.78 – 7.20	60,325	58,035
6/23/10	2010B Electric System Revenue Bonds	10/1/39	5.00	39,930	39,930
7/23/11	2011A Electric System Refunding Revenue Bonds	7/1/26	3.85 – 5.00	125,380	93,050
8/31/11	2011C Electric System Refunding Revenue Bonds	7/1/31	4.50 – 5.00	32,840	32,450
10/25/12	2012A Electric System Refunding Revenue Bonds	7/1/32	1.00 – 5.00	90,065	85,055
8/14/13	2013G Domestic Water Refunding Revenue Bonds	9/11/22	4.75 – 5.13	43,270	30,870
7/15/15	2015A Electric System Revenue Bond	10/1/40	4.00 – 5.00	67,690	67,690
7/15/15	2015B Electric System Refunding Revenue Bond	10/1/36	2.00 – 5.00	30,190	29,790
10/1/16	2016 Electric System Refunding Revenue Bond	10/1/34	2.00 – 5.00	92,240	95,240

# MODESTO IRRIGATION DISTRICT

## NOTES TO FINANCIAL STATEMENTS As of and for the Years Ended December 31, 2016 and 2015 (Dollars in Thousands)

### NOTE 7 – LONG-TERM DEBT (cont.)

#### **GENERAL DEBT TERMS**

The net revenue of the District’s electric system is pledged for repayment of COPs and Revenue Bonds. The Domestic Water Revenue Bonds are collateralized by a pledge of payments made by the City of Modesto relating to domestic water services. Interest on certificates and revenue bonds is generally payable semi-annually, except for interest on certain COPs that is payable on the last day of each interest rate reset period.

Interest earnings on tax exempt bond funds are subject to arbitrage rules of the Internal Revenue Service if interest earnings on the unspent tax exempt funds are greater than the stated bond yield on the tax exempt debt. As of December 31, 2016 and 2015, the District has recorded a liability of \$242 and \$2,026, respectively, for a potential arbitrage rebate to the IRS. Arbitrage rebates are due five years from the issuance date of the tax exempt debt.

GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, disclosures for pledged revenues are as follows:

<u>Electric System</u>	<u>2016</u>	<u>2015</u>
Principal and interest payments	\$ 57,562	\$ 56,009
Gross revenues	\$ 379,694	\$ 399,313
Total remaining principal and interest	\$ 939,933	\$ 1,087,770
Percent of future gross revenues	10%	11%
<u>Domestic Water System</u>		
Principal and interest payments	\$ 10,131	\$ 10,187
Gross revenues	\$ 23,114	\$ 20,098
Total remaining principal and interest	\$ 190,116	\$ 202,208
Percent of future gross revenues	34%	40%

The District is in compliance with required bond covenants.

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
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### NOTE 7 – LONG-TERM DEBT (cont.)

#### *LONG-TERM DEBT REPAYMENT*

Revenue bonds debt service requirements to maturity follows:

<u>Year Ending December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Interest Subsidy</u>	<u>Total</u>
2017	\$ 36,150	\$ 37,085	\$ (1,282)	\$ 71,953
2018	38,155	35,492	(1,242)	72,405
2019	39,315	33,564	(1,199)	71,680
2020	41,000	31,561	(1,153)	71,408
2021	43,425	29,437	(1,104)	71,758
2022 – 2026	186,460	117,414	(5,326)	298,548
2027 – 2031	149,285	77,519	(5,326)	221,478
2032 – 2036	137,165	40,865	(4,508)	173,522
2037 – 2040	<u>70,890</u>	<u>7,748</u>	<u>(1,341)</u>	<u>77,297</u>
Total Requirements	<u>\$ 741,845</u>	<u>\$ 410,685</u>	<u>\$ (22,481)</u>	<u>\$ 1,130,049</u>

Pursuant to the requirements of the Balanced Budget and Emergency Deficit Control Act of 1985, as amended, certain automatic reductions were effective March 1, 2013 for qualified bonds including the District's 2010A series Bonds. The District received a reduced interest subsidy payment during 2016 and 2015 due to budget sequestration by the federal government. In 2016 and 2015, the District recognized \$1,343 and \$1,323, respectively, in revenues for its Build America Bonds, as a component of other non-operating income, net in the statements of revenues, expenses and changes in net position. Federal subsidies for these bonds will be reduced by 6.9% through the end of the federal fiscal year (September 30, 2017) or convening U.S. Congressional action, at which time the sequestration rate is subject to change.

The District had outstanding debt obligations totaling \$109,995 and \$75,310 at December 31, 2016 and 2015, which were defeased and excluded from the District's long-term debt.

#### *ADVANCE REFUNDING*

On September 29, 2016, bonds in the amount of \$63,555 were issued with an average interest rate of 4.90% to advance refund \$66,025 of series 2004B Certificates of Participation Bonds with an average interest rate of 5.42%. The net proceeds were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the old bonds. As a result, the old bonds are considered defeased and the liability for the old bonds has been removed from the balance sheet.

The cash flow requirements on the old bonds prior to the advance refunding was \$113,747 with refunding receipts of \$6,472 from 2016 through 2035. The cash flow requirements on the new bonds are \$69,771 with refunding receipts of \$6,483 from 2016 through 2035. The advance refunding resulted in an economic gain of \$29,676.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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## **NOTE 7 – LONG-TERM DEBT (cont.)**

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### ***ADVANCE REFUNDING (cont.)***

On July 15, 2015 bonds in the amount of \$30,190 were issued with an average interest rate of 4.82% to advance refund \$29,800 of series 2006A outstanding bonds with an average interest rate of 4.78%. The net proceeds were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for a portion of the future debt payments on the old bonds. As a result, those portions of the old bonds are considered defeased and the liability for that portion of the old bonds has been removed from the balance sheet.

The cash flow requirements on the old bonds prior to the advance refunding was \$49,892 from 2015 through 2036. The cash flow requirements on the new bonds are \$48,544 and refunding receipts of \$1,564 from 2015 through 2036. The advance refunding resulted in an economic gain of \$1,870.

### ***CURRENT REFUNDING***

On September 29, 2016, bonds in the amount of \$31,685 were issued with an average interest rate of 4.99% to refund \$35,515 of series 2006A Certificates of Participation Bonds with an average interest rate of 4.98%. The net proceeds were used to prepay the outstanding debt service requirements on the old bonds.

The cash flow requirements on the old bonds prior to the current refunding was \$57,811 from 2016 through 2036. The cash flow requirements on the new bonds are \$45,515 with refunding receipts of \$3,232 from 2016 through 2036. The advance refunding resulted in an economic gain of \$9,917.

### ***CASH DEFEASANCE***

On October 1, 2016, the District used \$14,380 of cash on hand, including \$382 of restricted funds, to defease \$12,740 of the outstanding series 2009A Certificate of Participation Bonds. The cash on hand, net of expenses, were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for a portion of the future debt service payments on the bonds. As a result, that portion of the bonds are considered defeased and the liability for that portion of the bonds has been removed from the statement of net position.

The cash flow requirements on the old bonds prior to this transaction was \$30,140 from 2017 through 2039.

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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### NOTE 7 – LONG-TERM DEBT (cont.)

#### *LONG-TERM OBLIGATION SUMMARY*

Long-term obligation activity for the year ended December 31, 2016 is as follows:

	1/1/16 Balance	Additions	Reductions	12/31/16 Balance	Due Within One Year
Domestic water					
revenue bonds	\$ 128,380	\$ -	\$ 4,320	\$ 124,060	\$ 4,535
Certificate of participation	235,620	-	119,075	116,545	2,985
Revenue bonds	423,205	95,240	17,205	501,240	28,630
Unamortized debt discount	(2,881)	-	(304)	(2,577)	-
Unamortized premium	30,929	17,155	6,975	41,109	-
Net pension liability	76,334	29,233	12,120	93,447	-
Other liabilities	14,216	2,313	4,690	11,839	-
Derivative financial					
instruments	30,449	-	3,722	26,727	247
Equity interest in M-S-R	24,116	1,650	10,549	15,217	-
<b>Totals</b>	<b>\$ 960,368</b>	<b>\$ 145,591</b>	<b>\$ 178,352</b>	<b>\$ 927,607</b>	<b>\$ 36,397</b>

Long-term obligation activity for the year ended December 31, 2015 is as follows:

	1/1/15 Balance	Additions	Reductions	12/31/15 Balance	Due Within One Year
Domestic water					
revenue bonds	\$ 132,490	\$ -	\$ 4,110	\$ 128,380	\$ 4,320
Certificate of participation	275,860	-	40,240	235,620	4,795
Revenue bonds	336,920	97,880	11,595	423,205	17,205
Unamortized debt discount	(2,649)	(356)	(124)	(2,881)	-
Unamortized premium	26,529	10,034	5,634	30,929	-
Net pension liability	1,833	76,334	1,833	76,334	-
Other liabilities	14,860	576	1,220	14,216	-
Derivative financial					
instruments	30,795	-	346	30,449	1,369
Equity interest in M-S-R	35,135	-	11,019	24,116	-
<b>Totals</b>	<b>\$ 851,773</b>	<b>\$ 184,468</b>	<b>\$ 75,873</b>	<b>\$ 960,368</b>	<b>\$ 27,689</b>

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
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## NOTE 8 – DERIVATIVE INSTRUMENTS

### SUMMARY OF NOTIONAL AMOUNTS AND FAIR VALUES

The District enters into contracts to hedge its exposure to power and natural gas prices, and to procure energy supplies. The District also enters into contracts to hedge its exposure to fluctuating interest rates. These contracts are evaluated pursuant to GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, to determine whether they meet the definition of derivative instruments, and, if so, whether they effectively hedge the expected cash flows associated with interest rate and energy exposures.

The District applies hedge accounting for derivatives that are deemed effective hedges. Under hedge accounting, the increase (decrease) in the fair value of a hedge is reported as a deferred inflow (outflow) on the balance sheets. For the reporting periods, all of the District's derivatives meet the effectiveness tests.

For energy derivatives, fair values are estimated by comparing contract prices to forward market prices quoted by third party market participants or provided in relevant industry publications. For interest rate derivatives, the District subscribes to a financial information service that it uses to verify fair value estimates obtained from its counterparties.

The following is a summary of the fair values and notional amounts of derivative instruments outstanding as of December 31, 2016 (amounts in thousands; gains shown as positive amounts, losses as negative).

	2016 Change in Fair Value		Fair Value, End of 2016		Notional (Thousands)
	Classification	Amount	Classification	Amount	
<b>Effective Cash Flow Hedges</b>					
Interest Rate Derivatives:					
Pay-fixed swaps, interest rate	Deferred Outflow	\$ 1,822	Derivative	\$ (25,837)	\$ 93,190
Energy Derivatives:					
Pay-fixed swaps, natural gas	Deferred Outflow	1,831	Derivative	(897)	2,039 mmBtu
Options Contracts	Deferred Outflow	69	Derivative	7	180 mmBtu

The following is a summary of the fair values and notional amounts of derivative instruments outstanding as of December 31, 2015 (amounts in thousands; gains shown as positive amounts, losses as negative).

	2015 Change in Fair Value		Fair Value, End of 2015		Notional (Thousands)
	Classification	Amount	Classification	Amount	
<b>Effective Cash Flow Hedges</b>					
Interest Rate Derivatives:					
Pay-fixed swaps, interest rate	Deferred Outflow	\$ 254	Derivative	\$ (27,659)	\$ 93,190
Energy Derivatives:					
Pay-fixed swaps, natural gas	Deferred Outflow	(879)	Derivative	(2,728)	2,256 mmBtu
Options Contracts	Deferred Outflow	64	Derivative	(62)	540 mmBtu

# MODESTO IRRIGATION DISTRICT

## NOTES TO FINANCIAL STATEMENTS As of and for the Years Ended December 31, 2016 and 2015 (Dollars in Thousands)

### NOTE 8 – DERIVATIVE INSTRUMENTS (cont.)

#### OBJECTIVE AND TERMS OF HEDGING DERIVATIVE INSTRUMENTS

The objectives and terms of the District's hedging derivative instruments that were outstanding at December 31, 2016 are summarized in the table below. The table is aggregated by the credit ratings (using the Standard & Poor's scale) of the District's counterparties. For counterparties having multiple ratings, the rating indicating the greatest degree of risk is used.

The interest rate swaps are designed to synthetically fix the cash flows associated with variable rate bonds. The interest rate that the District pays on the 2007F bonds is 67% of LIBOR plus a spread. With the interest rate swaps, the District pays the counterparty a fixed rate and receives 67% of LIBOR. Netting out the LIBOR-based payments, the District's effective interest rate is the sum of the fixed rate paid to the swap counterparty and the spread.

The District hedges its power and natural gas costs so that it can offer predictable rates to its retail electric customers, stabilize its finances and enhance its credit profile. The District maintains a Risk Management Program (RMP) to control the price, credit, and operational risks arising from its power and natural gas market activities. Under the RMP, authorized District personnel assemble a portfolio of swaps, options, futures, and forward contracts over time with the goal of making the District's purchased power and fuel budget more predictable.

Type	Objective	Notional (Thousands)	Effective Date	Maturity Date	Terms	Counterparty Rating
Pay-fixed swaps, interest rate	Hedge cash flows on the 2007F bonds	\$93,190	Jun -07	Sep-37	Pay 4.378-4.440%; Receive 67% of LIBOR	A
Option contracts, natural gas	Hedge cash flows on PG&E citygate gas purchases	180 mmBtu	Dec-16	Dec-17	Collar with \$3.15/mmBtu floor, \$4.00 cap; Settle on NYMEX	n/a
Pay-fixed swaps, natural gas	Hedge cash flows on PG&E citygate gas purchases	2,039 mmBtu	Sep-14	Dec-19	Pay \$3.13-4.84/mmBtu; Receive NGI PG&E citygate price	Between A To BBB

Objectives and terms of the District's hedging derivative instruments that were outstanding at December 31, 2015 are summarized in the table below:

Type	Objective	Notional (Thousands)	Effective Date	Maturity Date	Terms	Counterparty Rating
Pay-fixed swaps, interest rate	Hedge cash flows on the 2007F bonds	\$93,190	Jun -07	Sep-37	Pay 4.378-4.440%; Receive 67% of LIBOR	A
Option contracts, natural gas	Hedge cash flows on PG&E citygate gas purchases	540 mmBtu	Oct-16	Dec-16	Collar with \$2.60/mmBtu floor, \$3.25 cap; Settle on NYMEX	n/a
Pay-fixed swaps, natural gas	Hedge cash flows on PG&E citygate gas purchases	2,256 mmBtu	Mar-13	Dec-18	Pay \$3.80-4.84/mmBtu; Receive NGI PG&E citygate price	Between A To BBB

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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## NOTE 8 – DERIVATIVE INSTRUMENTS (cont.)

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### *RISKS OF DERIVATIVE INSTRUMENTS*

**Credit risk** – Credit risk is the risk of loss due to a counterparty defaulting on its obligations. The District seeks to minimize credit risk by transacting with creditworthy counterparties. Interest rate swap counterparties are evaluated at the time of transaction execution. For energy counterparties, the District follows a procedure under its RMP wherein the District will accept more potential credit risk from counterparties having greater amounts of tangible net worth and higher credit ratings. The procedure restricts the District from executing energy hedge transactions with counterparties rated lower than BBB by Standard & Poor's or Fitch rating services, or Baa2 by Moody's.

The District uses industry standard agreements to document derivative transactions. These agreements include netting clauses whereby, if the District and the counterparty owe each other payment, the party owing the greater amount pays the net. The District also uses collateral posting provisions to manage credit risk. These provisions require an out-of-the-money party to post cash, letters of credit, or other pre-agreed liquid securities to the extent that the mark-to-market value of derivative positions with a given counterparty exceeds a threshold value. Thresholds are negotiated individually with counterparties, and the netting provisions include rights to set off against posted collateral.

To avoid concentrations of credit risk, and to avoid the risk of itself having to post large amounts of collateral, the District seeks to spread transactions across counterparties so that, even with an adverse move in the market, the threshold values would likely not be exceeded. As of December 31, 2016 and 2015, the District did not have any collateral posted with its derivative counterparties and did not hold any collateral posted by its counterparties.

The District is exposed to credit risk to the extent that it has net fair value gains on its derivative positions with individual counterparties. If counterparty failed, those value amounts could be lost. As of December 31, 2016 and 2015, the District was not in-the-money with certain of its counterparties; the District's only net gains were on exchange-traded instruments.

**Basis risk** – Basis risk is the risk that arises when a hedged item and a derivative intended to hedge that item are based on different indices. The District is exposed to basis risk when it hedges its natural gas purchases, which are priced at the PG&E citygate index, with NYMEX futures and options contracts, which settle based on the price in Henry Hub, Louisiana. If the markets diverge such that PG&E citygate prices increase relative to Henry Hub prices, the District would be negatively affected on the futures and options contracts that mature in 2017.

**Termination risk** – Termination risk is the risk that a derivative will terminate prior to its scheduled maturity due to a contractual event. Contractual events include bankruptcy, illegality, default, and mergers in which the successor entity does not meet credit criteria. One aspect of termination risk is that the District would lose the hedging benefit of a derivative that becomes subject to a termination event. Another aspect of termination risk is that, if at the time of termination the mark-to-market value of the derivative was a liability to the District, the District could be required to pay that amount to the counterparty. Termination risk is associated with all of the District's derivatives up to the fair value amounts.



## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
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### NOTE 8 – DERIVATIVE INSTRUMENTS (cont.)

#### *HEDGED DEBT*

Net cash flows for the District's synthetic fixed-rate debt are shown below. These amounts assume that the interest rates of the bonds and the reference rates of the hedging derivative instruments remain at December 31, 2016 levels. These rates will vary and, as they do, interest payments on the variable-rate bonds and net receipts/payments on the interest rate swaps will vary. The table shows only the District's effectively hedged synthetic fixed-rate debt, which is a subset of the District's total debt. As of December 31, 2016, all of the District's variable-rate debt is effectively hedged.

Year Ending December 31,	Principal	Interest	Net Payment on Derivatives	Total
2017	\$ -	\$ 1,198	\$ 2,925	\$ 4,123
2018	-	1,198	2,925	4,123
2019	-	1,198	2,925	4,123
2020	-	1,198	2,925	4,123
2021	-	1,198	2,925	4,123
2022 – 2026	18,265	5,606	13,655	37,526
2027 – 2031	27,955	4,078	9,870	41,903
2032 – 2036	35,100	2,065	4,996	42,161
2037	11,870	116	280	12,266
Totals	<u>\$ 93,190</u>	<u>\$ 17,855</u>	<u>\$ 43,426</u>	<u>\$ 154,471</u>

### NOTE 9 – EMPLOYEE BENEFIT PLANS

The District maintains two retirement plans and a retiree medical benefits plan for its eligible employees. The Retirement Committee of the District's Board of Directors oversees the plans. The District has a Retirement Department that performs plan administrative functions. Plan investments are managed by the District Treasury Department and third-party investment managers. All funds of the plans are separate assets of the retirement plans, and are not assets of the District.

#### *BASIC RETIREMENT PLAN*

The District implemented GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*, effective January 1, 2015. The cumulative effect of the change in net position due to the change in accounting standard, or the initial unfunded liability is shown as a regulatory cost for future recovery on the balance sheet. The District plans to recover these costs in a future rate study.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

## **NOTE 9 – EMPLOYEE BENEFIT PLANS (cont.)**

### ***BASIC RETIREMENT PLAN (cont.)***

**Plan Description.** The Basic Retirement Plan (the Plan) is a single-employer defined benefit pension plan for eligible employees. All employees who normally work 20 hours per week or more and at least five months per year, except leased employees, employees whose work classification is excluded from coverage under the Plan by a collective bargaining agreement, and individuals employed in work experience and student intern classifications, are eligible. There are three tiers of employees covered. Tier 1 is comprised of Pre-2006 eligible employees. Tier 2 is comprised of Post-2005 eligible employees. Tier 3 is comprised of Post-2012 eligible employees. The Plan provides retirement, disability and death benefits to plan members and beneficiaries. The District issues publicly available stand-alone financial statements and required supplementary information of the Plan that may be obtained by contacting the District. The fiduciary net position reported in these statements has been determined on the same basis as the plan.

**Benefits Provided.** Benefits provided for Tier 1 and 2 employees include monthly benefits of 2.75% of the final average monthly earnings multiplied by a credited service factor. Tier 3 employees receive a monthly benefit equal to a percentage between 1% if retirement occurs at age 52 and 2.5% if retirement occurs at age 67 or older multiplied by a credited service factor. For ages 52 through 67, the percentage is between 1% and 2.5%. Vesting periods are 5 years for all tiers. Normal retirement age is 60 for Tier 1 and 2 employees with reduced early retirement options at 55 with 5 years of service. Tier 3 employees may retire at age 52, but cost of living adjustments are only given to employees that retire on or after age 55 with 5 years of service. Final average compensation is calculated based on the highest average monthly earnings during the 36 consecutive months out of the last 120 months for Tier 1 and Tier 2 employees. Tier 3 employee benefits are calculated as the highest average monthly earnings received during the 36 consecutive month's immediately preceding separation of service. Cost of living adjustments are provided for all employees who have been receiving benefits for more than one year excepted as noted above. The cost of living adjustment is based on the increase in the U.S. Labor Department cost of living index, but it may not exceed 4%. Tier 3 employees that leave the District's service may withdraw his or her contribution if they are not yet vested. Benefit terms may be amended by the Board of Directors.

**Employees Covered by Benefit Terms.** At the December 31, 2015 and 2014 valuation dates, the following employees were covered by the benefit terms:

	2015	2014
Inactive employees or beneficiaries currently receiving benefits	404	387
Inactive employees entitled to but not yet receiving benefits	51	53
Active employees	429	412
Totals	884	852

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## **NOTE 9 – EMPLOYEE BENEFIT PLANS (cont.)**

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### ***BASIC RETIREMENT PLAN (cont.)***

**Contributions.** The Board of Directors has established, and may amend, the contribution requirements for Plan members and the District set forth in the terms of the Plan. The Terms of the Plan empower the Retirement Committee of the District (the Committee) to make, at reasonable intervals, an analysis of the funding requirements of the Plan for the payment of retirement benefits and expenses, based on reasonable actuarial assumptions and methods which take into account the experience of the Plan and the reasonable expectations, and on the basis of this analysis, to establish a funding policy for the Plan. The terms of the Plan state that, subject to the Board of Directors' right to suspend or reduce contributions to the Plan at any time, the District shall contribute to the Plan at least once a year, the amounts necessary to maintain the Plan on a sound actuarial basis, in a manner consistent with the funding policy established by the Committee.

The funding policy currently established by the Committee requires the District to contribute an amount set forth in the Recommendation Regarding Total Contributions presented in the Plan actuary's Actuarial report. The Required Annual Contributions set forth in the Recommendation regarding total contributions presented in the Actuarial Report are \$11,781 and \$12,057 which were contributed in 2016 and 2015, respectively.

The District was the sole participating employer and contributing entity. Prior to 1989, participants were allowed to make voluntary contributions and prior to 1977, participating contributions were required. The Plan was amended as of January 1, 2013; new member employees are required to contribute an amount equal to one-half of the defined benefits' normal cost through payroll deductions.

**Net Pension Liability.** The employer's net pension liability was measured as of December 31, 2015 and 2014 for the District's December 31, 2016 and 2015 financial statements, respectively, and the total pension liability used to calculate the net pension liability was determined by an annual actuarial valuation as of that date.

**Actuarial Assumptions.** The total pension liability in the December 31, 2015 and 2014 annual actuarial valuations were determined using the following actuarial assumptions, applied to all periods included in the measurement:

- > Inflation: 2.50%
- > Salary Increases: 4.00%
- > Investment rate of return: 7.50%, net of investment expense, including inflation.
- > Mortality rates used were based on the RP-2000 Blue Collar Generational Mortality Table for Males or Females, as appropriate, with adjustments for mortality improvements based on 75% of Scale AA. This mortality rate is for both pre-retirement and post-retirement.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## NOTE 9 – EMPLOYEE BENEFIT PLANS (cont.)

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### *BASIC RETIREMENT PLAN* (cont.)

- > The plan's investment policy does not establish long-term expected rates of return for each asset class. The target allocation for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>
Cash	0%
Fixed Income and US Governmental Obligations	25%
International Stocks	15%
Domestic Stocks	45%
Hedge Funds	10%
Public Real Estate	5%
Opportunistic Portfolio	0%

**Discount Rate.** The discount rate used to measure the total pension liability is 7.50%. The projection of cash flows used to determine the discount rate assumes that employer and employee contributions will be made at the rates agreed-upon for employees and the actuarially determined rates for employers. Based on these assumptions, the pension plan's fiduciary net position was projected to be available to pay all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

### NOTE 9 – EMPLOYEE BENEFIT PLANS (cont.)

#### *BASIC RETIREMENT PLAN* (cont.)

#### *Changes in Net Pension Liability*

	Increase (Decrease)		
	Total Pension Liability	Plan Fiduciary Net Position	Net Pension Liability
	(a)	(b)	(a) - (b)
<b>Balances at 12/31/14</b>	\$ 293,095	\$ 216,476	\$ 76,619
<b>Changes for the Year</b>			
Service cost	5,996	-	5,996
Interest on total pension liability	21,705	-	21,705
Employer contributions	-	13,221	(13,221)
Employee contributions	-	72	(72)
Net investment income	-	14,852	(14,852)
Benefit payments, including employee refunds	(13,448)	(13,448)	-
Administrative expense	-	(159)	159
<b>Net Changes</b>	14,253	14,538	(285)
<b>Balances at 12/31/15</b>	<b>307,348</b>	<b>231,014</b>	<b>76,334</b>
<b>Changes for the Year</b>			
Service cost	6,460	-	6,460
Interest on total pension liability	22,503	-	22,503
Difference between expected and actual experience	356	-	356
Employer contributions	-	12,120	(12,120)
Employee contributions	-	465	(465)
Net investment income	-	(237)	237
Benefit payments, including employee refunds	(14,508)	(14,508)	-
Administrative expense	-	(142)	142
<b>Net Changes</b>	14,811	(2,302)	17,113
<b>Balances as of 12/31/16</b>	<b>\$ 322,159</b>	<b>\$ 228,712</b>	<b>\$ 93,447</b>

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

## NOTE 9 – EMPLOYEE RETIREMENT PLAN (cont.)

### **BASIC RETIREMENT PLAN** (cont.)

**Sensitivity of the Net Pension Liability to Changes in the Discount Rate.** The following presents the Net Pension Liability of the employer, calculated using the discount rate of 7.50%, as well as what the employer's Net Pension Liability would be using a discount rate that is 1 percentage point lower (6.50%) or 1% higher (8.50%) than the current rate.

	<u>1% Decrease</u>	<u>Current Discount Rate</u>	<u>1% Increase</u>
Net pension liability as of 12/31/2016	\$ 133,149	\$ 93,447	\$ 60,020
Net pension liability as of 12/31/2015	\$ 114,580	\$ 76,334	\$ 44,167

**Pension Plan Fiduciary Net Position.** Detailed information about the pension plan's fiduciary net position is available in the separately issued Modesto Irrigation District Retirement System Basic Retirement Plan report.

**Pension Expense, Deferred Outflows of Resources, and Deferred Inflows of Resources Related to Pensions.** For the year ended December 31, 2016 and 2015, the employer recognized pension expense of \$15,006 and \$11,482, respectively. The employer reported deferred outflows and inflows of resources related to pensions from the following sources:

	<u>December 31, 2016</u>	
	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Net difference between projected and actual investment earnings	\$ 15,386	\$ -
Differences between expected and actual experience	294	-
Contributions subsequent to the measurement date *	<u>11,854</u>	<u>-</u>
Totals	<u>\$ 27,534</u>	<u>\$ -</u>

\* The amount reported as deferred outflows of resources resulting from contributions subsequent to the measurement date will be recognized as a reduction in the net pension liability for the year ending December 31, 2017.

	<u>December 31, 2015</u>	
	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Net difference between projected and actual investment earnings	\$ 1,453	\$ -
Contributions subsequent to the measurement date *	<u>12,057</u>	<u>-</u>
Totals	<u>\$ 13,510</u>	<u>\$ -</u>

\* The amount reported as deferred outflows of resources resulting from contributions subsequent to the measurement date was recognized as a reduction in the net pension liability for the year ending December 31, 2016.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## NOTE 9 – EMPLOYEE BENEFIT PLANS (cont.)

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### ***BASIC RETIREMENT PLAN*** (cont.)

Amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year Ending June 30	Expense
2017	\$ 3,999
2018	3,999
2019	3,999
2020	3,636
2021	47

***Payable to the Pension Plan.*** At December 31, 2016 and 2015, the employer reported a payable of \$0 for the outstanding amount of contributions to the pension plan required for the years ended December 31, 2016 and 2015, respectively.

The 2016 and 2015 required contributions were determined as part of the January 1, 2016 and January 1, 2015 actuarial valuations, respectively, using the entry age normal cost method. This method seeks to provide a level pattern of cost as a percentage of salary throughout an employee's working lifetime. A level percentage of payroll amortization is used, with an amortization period not to exceed 30 years.

### ***SUPPLEMENTAL RETIREMENT PLAN***

Eligible employees of the District also participate in the District's supplemental retirement plan (the Supplemental Plan). The Supplemental Plan is a defined contribution plan and serves as partial or full replacement of social security for participants, depending upon date of employment. Participants are required to contribute 5% of their compensation on a pre-tax basis. The District wholly matches the contributions. Participants become fully vested in the District's portion of their account after six months of employment. Covered payroll of Participants is the same as under the Basic Retirement Plan. Participants have three investment options, a fund comprised of short-term fixed income money market securities, managed by the District's Treasury Department, a fund comprised primarily of equities, managed by third party investment managers, and a fund comprised of long-term fixed income securities, managed by third party investment managers. The District made contributions to the Supplemental Plan of \$2,091 and \$1,895 for 2016 and 2015, respectively.

### ***HEALTH CARE BENEFITS***

***Plan Description.*** The Retiree Health Program is a single-employer defined benefit healthcare plan. The District provides health care benefits, in accordance with District policy, to qualified retirees and their spouses. The qualification requirements for these benefits are similar to those under the District's retirement plans.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
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(Dollars in Thousands)

## **NOTE 9 – EMPLOYEE BENEFIT PLANS (cont.)**

### **HEALTH CARE BENEFITS (cont.)**

*Funding Policy.* Currently 329 retirees and surviving spouses meet those eligibility requirements. The District contributes the full cost of coverage for employees who retired before 1992; employees who retire in 1992 and thereafter pay a portion of the monthly premium for eligible dependent coverage, and the District pays the remainder of the cost of the plan. Covered retirees are also responsible for personal deductibles and co-payments. The District pays for post-retirement dental and vision care for retirees only to age 65.

*Annual OPEB Cost and Net OPEB Obligation (Asset).* The District contributes at an actuarially determined rate. The annual required contribution was determined in accordance with the projected unit credit actuarial cost method. The actuarial value of assets is based on fair market valuations prepared by a brokerage service. Significant assumptions used to determine the actuarial accrued liabilities as of January 1, 2015, the most recently completed actuarial valuation, include the following, all reflecting annual compounding:

- > Rate of return on the investment of present and future assets of 7.5% per year;
- > Discount rate applied to the pension benefit obligation of 7.5% per year;
- > Salary increases of 3.5% per year; and
- > Projected health care cost increases of 7.5% in 2015 and decreasing by 0.5% each year until 2021 and thereafter when it stays at 4.5%.

The District's annual OPEB cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over thirty years as a percentage of rising covered payroll. The following table illustrates the amount actually contributed to the plan, and changes in the District's net OPEB obligation (asset) (dollar amounts in thousands).

	2016	2015
Annual required contribution	\$ 6,956	\$ 6,982
Interest on net OPEB obligation (asset)	(72)	101
Adjustment to annual required contribution	35	(88)
Annual OPEB cost (expense)	6,919	6,995
Contributions made	9,234	7,968
Increase (decrease) in net OPEB obligation (asset)	(2,315)	(973)
Net OPEB obligation (asset), beginning of period	(606)	367
Net OPEB Obligation (Asset), End of Period	\$ (2,921)	\$ (606)



## MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

### NOTE 9 – EMPLOYEE BENEFIT PLANS (cont.)

#### HEALTH CARE BENEFITS (cont.)

The District's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2016, 2015, and 2014 were as follows:

Fiscal Year Ending	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation (Asset)
12/31/16	\$ 6,956	132.75%	\$ (2,921)
12/31/15	6,995	113.91%	(606)
12/31/14	8,503	96.05%	367

The schedule of funding progress (unaudited) is presented below:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
1/01/15	\$ 35,057	\$ 105,120	\$ 70,063	33.35%	\$ 35,339	198.26%
1/01/13	24,110	107,223	83,113	22.49%	36,124	230.08%
1/01/11	14,997	91,091	76,094	16.46%	32,679	232.85%

Actuarial valuations of an ongoing plan involve estimates for the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

The required schedule of funding progress immediately following the notes to the financial statements presents trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing benefit costs between the employer and plan members to that point. Actuarial calculations reflect a long-term perspective. The methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## NOTE 10 – COMMITMENTS

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The District purchases most of its purchased power from M-S-R (Note 6) and through the following long-term agreements:

### *THE CITY AND COUNTY OF SAN FRANCISCO POWER PURCHASE AGREEMENT*

The City and County of San Francisco (CCSF) Power Purchase Agreement (Agreement) titled the "Amended and Restated Long Term Power Sales Agreement" (ARLTPSA) was amended in 2007 and is now titled the "Long Term Energy Sales Agreement between the City and County of San Francisco and the Modesto Irrigation District" (LTESA). Pursuant to the Raker Act (the 1913 federal law enabling construction of the Hetch Hetchy project in the national park) energy from the Hetch Hetchy project in excess of CCSF's municipal loads (Class One power) must be sold to the District and to the Turlock Irrigation District at cost. Among other things, the LTESA specifies how the Class One power is delivered and how the cost-based pricing is determined.

The current LTESA provides Class One power for the District at a minimum schedule of 40% of the capacity for the month. The District's purchases under the LTESA in 2016 and 2015 totaled \$7,934 and \$4,394, respectively. While the current LTESA expired June 30, 2015, the District expects to continue receiving cost-based Class One power after that time. Total estimated payments to CCSF over the next five years are as follows as of December 31, 2016:

2017	\$	3,964
2018		4,052
2019		4,144
2020		4,237
2021		4,332

### *OTHER ENERGY PURCHASE COMMITMENTS*

The District has a number of other power and natural gas purchase agreements with various entities, which provide for power and fuel deliveries, under various terms and conditions through 2021. Total commitments under these agreements over the next five years are as follows as of December 31, 2016:

2017	\$	73,265
2018		67,151
2019		57,958
2020		56,457
2021		57,193

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## NOTE 11 – CONTINGENCIES

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### *RATE SUBSIDY LITIGATION*

Two class action lawsuits have been filed against the District, Thomas v. Modesto Irrigation District and Hobbs v. Modesto Irrigation District, both of which were filed in March 2016. The basis for these lawsuits stems from Proposition 26, which California voters adopted on November 2, 2010. The lawsuits allege MID uses funds collected from electric customers to subsidize its irrigation and water operations and are illegally taxing electric customers under Propositions 26. Both lawsuits are class action complaints seeking refunds of alleged illegal taxes. In September of 2016, a Judgment was issued by the Court dismissing the Thomas action. The District is currently undertaking preparation of the Administrative Record in the Hobbs action. The District is unable to predict the outcome of the litigation or the extent to which remedies against it may be available if the District is ultimately unsuccessful in the litigation. The District is vigorously defending this matter.

### *GENERAL CONTINGENCIES*

In the normal course of operations, the District is party to various claims, legal actions and complaints. However, the District's counsel and management believe that the ultimate resolution of these matters will not have a significant adverse effect on the financial position or results of operations of the District.

### *OPEN CONTRACTS*

The District has open contracts for approximately \$25,448 for various capital and operating projects. As of December 31, 2016, approximately \$17,309 has been expended.

***Electric Purchase Contracts.*** The District has entered into numerous electric purchase contracts with amounts totaling approximately 491 gigawatt hours (GWh) for the purpose of fixing the rate on the District's electric power purchases. These electric purchase contracts result in the District paying fixed rates ranging from \$29.30 to \$109.50 per MWh. These contracts expire periodically from August 2017 through September 2018. In addition, the District has entered into contracts for power generated by hydroelectric and wind resources where the amount and cost will depend on weather variables. The hydro and wind contracts expire periodically from December 2024 through December 2037.

***Gas Purchase Contracts.*** The District has entered into numerous gas purchase contracts for the purpose of fixing the rate on the District's natural gas purchases for its gas-fueled power plants. These gas purchase contracts result in the District paying fixed rates ranging from \$3.06 to \$5.08 per million British Thermal Units (mmbtu). The amounts total to approximately 7.5 million mmbtu and the contracts expire periodically from January 2017 through December 2025.

# MODESTO IRRIGATION DISTRICT

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

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## NOTE 12 – RISK MANAGEMENT

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The District is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors and omissions; workers compensation; and health care of its employees. These risks are covered through the purchase of commercial insurance. The District is self insured for general and liability claims up to \$1,000. The District also has excess liability insurance for claims over \$1,000. There was no significant decrease in coverage over the prior year. Settled claims have not exceeded insurance coverage in each of the past three years. Claims are paid as they are incurred. Total accrual and payment history is shown below.

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Claims liability – beginning of year	\$ 560	\$ 549	\$ 721
Claims accrued	1,104	431	139
Claims paid/other	<u>(1,156)</u>	<u>(420)</u>	<u>(311)</u>
Claims Liability - End of Year	<u>\$ 508</u>	<u>\$ 560</u>	<u>\$ 549</u>

**REQUIRED SUPPLEMENTARY INFORMATION**

## MODESTO IRRIGATION DISTRICT

### REQUIRED SUPPLEMENTARY INFORMATION (Unaudited)

For the Years Ended December 31, 2016 and 2015  
(Dollars in Thousands)

#### Other Post Employment Benefits (OPEB) Required Supplementary Information

The schedule of funding progress, presented as required supplementary information, present multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

The schedule of funding progress is as follows:

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ([b-a]/c)
1/01/15	\$ 35,057	\$ 105,119	\$ 70,063	33.35%	\$ 35,339	198.26%
1/01/13	24,110	107,223	83,113	22.49%	36,124	230.08%
1/01/11	14,997	91,091	76,094	16.46%	32,679	232.85%

**MODESTO IRRIGATION DISTRICT**

REQUIRED SUPPLEMENTARY INFORMATION

(Unaudited)

As of December 31, 2016

(Dollars in Thousands)

***Schedule of Changes in the Employer's Net Pension Liability and Related Ratios - GASB Statement No. 68***

	<u>2016</u>	<u>2015</u>
<b>Total Pension Liability</b>		
Service cost	\$ 6,460	\$ 5,996
Interest	22,503	21,705
Difference between expected and actual experience	356	-
Benefit payments including employee refunds	<u>(14,508)</u>	<u>(13,448)</u>
<b>Net Change in Total Pension Liability</b>	<u>14,811</u>	<u>14,253</u>
<b>Total Pension Liability beginning</b>	<u>307,348</u>	<u>293,095</u>
<b>Total Pension Liability ending</b>	<u>\$ 322,159</u>	<u>\$ 307,348</u>
 <b>Plan Fiduciary Net Position</b>		
Contributions-employer	\$ 12,120	\$ 13,221
Contributions-employee	465	72
Net Investment income	(237)	14,852
Benefit payments including employee refunds	(14,508)	(13,448)
Administrative expense	<u>(142)</u>	<u>(159)</u>
<b>Net Change in Plan Fiduciary Net Position</b>	<u>(2,302)</u>	<u>14,538</u>
 <b>Plan Fiduciary Net Position beginning</b>	<u>231,014</u>	<u>216,476</u>
<b>Plan Fiduciary Net Position ending</b>	<u>\$ 228,712</u>	<u>\$ 231,014</u>
 <b>Employer Net Pension Liability</b>	<u>\$ 93,447</u>	<u>\$ 76,334</u>
 <b>Plan Fiduciary Net Position as a percentage of the Total Pension Liability</b>	70.99%	75.16%
 <b>Covered Employee Payroll</b>	\$ 38,211	\$ 35,448
<b>Employer's Net Pension Liability as a percentage of covered employee payroll</b>	244.56%	215.34%

**Notes to schedule:**

GASB 68 requires that 10 years of comparative data be shown for all the data presented above. However, as this information is unavailable for the periods preceding 2015, only the data since 2015 is being presented.

**MODESTO IRRIGATION DISTRICT**

**REQUIRED SUPPLEMENTARY INFORMATION**  
(Unaudited)

As of December 31, 2016

(Dollars in Thousands)

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**Schedule of Employer's Contributions - GASB Statement No. 68**

	<u>2016</u>	<u>2015</u>
Actuarial determined contributions *	\$ 11,781	\$ 12,057
Contributions in relation to the actuarially determined contribution	<u>11,854</u>	<u>12,120</u>
Contribution deficiency (excess)	<u>\$ (73)</u>	<u>\$ (63)</u>
Covered employee payroll	\$ 39,112	\$ 38,211
Contributions as a percentage of covered employee payroll	30%	32%

**Notes to Schedule**

Valuation date	Actuarial determined contributions are calculated as of December 31 of the prior year.
Actuarial cost method	Entry Age Normal
Amortization method	30-year rolling, level-dollar
Remaining amortization period	
Asset valuation method	10 year smoothed
Inflation	2.5%
Salary increases	4.0%
Investment rate of return	7.5%
Normal retirement age - tier 1 and tier 2	60
Normal retirement age - tier 3	55
Mortality	RP-2000 Blue Collar Generational Mortality Table

\* Actuarially Determined Contribution is found in the actuarial valuation report on page 2.

GASB 68 requires that 10 years of comparative data be shown for all the data presented above. However, as this information is unavailable for the periods preceding 2015, only the data since 2015 is being presented.

See independent auditors' report.



**SUPPLEMENTARY INFORMATION**

**MODESTO IRRIGATION DISTRICT**

COMBINING STATEMENTS OF FIDUCIARY NET POSITION  
As of December 31, 2016 and 2015

	<i>(Dollars in Thousands)</i>							
	Basic Retirement Plan		Supplemental Retirement Plan		Retiree Medical Plan		Total Fiduciary Funds	
	2016	2015	2016	2015	2016	2015	2016	2015
<b>ASSETS</b>								
<b>CASH AND CASH EQUIVALENTS</b>	\$ 12,883	\$ 5,440	\$ 166	\$ 166	\$ -	\$ 208	\$ 13,049	\$ 5,814
<b>RECEIVABLES</b>								
Accrued interest	256	392	-	-	-	-	256	392
Dividends	29	30	-	-	-	-	29	30
<b>INVESTMENTS AT FAIR VALUE</b>								
Fixed income securities	56,662	57,368	-	-	-	-	56,662	57,368
Publicly traded domestic stocks	111,251	100,305	-	-	-	-	111,251	100,305
Publicly traded international stocks	34,896	32,303	-	-	-	-	34,896	32,303
Real estate investment trust	11,061	11,490	976	982	-	-	12,037	12,472
Stable value	-	-	14,646	8,156	-	-	14,646	8,156
Mutual funds	-	-	85,868	87,353	43,294	37,906	129,162	125,259
Hedge funds	15,649	22,173	-	-	-	-	15,649	22,173
Total Assets	242,687	229,501	101,656	96,657	43,294	38,114	387,637	364,272
<b>LESS: ACCRUED LIABILITIES</b>	773	790	-	-	54	111	827	901
<b>NET POSITION HELD IN TRUST FOR RETIREE BENEFITS</b>	\$ 241,914	\$ 228,711	\$ 101,656	\$ 96,657	\$ 43,240	\$ 38,003	\$ 386,810	\$ 363,371

**MODESTO IRRIGATION DISTRICT**

COMBINING STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION  
As of December 31, 2016 and 2015

	<i>(Dollars in Thousands)</i>							
	Basic Retirement Plan		Supplemental Retirement Plan		Retiree Medical Plan		Total Fiduciary Funds	
	2016	2015	2016	2015	2016	2015	2016	2015
<b>ADDITIONS</b>								
Additions to (reductions from) net position attributed to:								
Investment income (loss):								
Net appreciation (depreciation) of investments	\$ 13,977	\$ (2,327)	\$ 3,426	\$ (4,566)	\$ 2,114	\$ (717)	\$ 19,517	\$ (7,610)
Dividend income	1,486	886	2,880	4,263	788	761	5,154	5,910
Interest income	1,969	2,437	-	-	-	1	1,969	2,438
Investment expenses	<u>(1,106)</u>	<u>(1,234)</u>	-	-	-	-	<u>(1,106)</u>	<u>(1,234)</u>
Net investment income (loss)	16,326	(238)	6,306	(303)	2,902	45	25,534	(496)
Contributions								
Employee contributions	739	465	2,092	1,895	23	21	2,854	2,381
Employer contributions	11,854	12,120	2,091	1,895	7,821	7,187	21,766	21,202
Other contributions	-	-	51	342	-	-	51	342
Total Contributions	<u>12,593</u>	<u>12,585</u>	<u>4,234</u>	<u>4,132</u>	<u>7,844</u>	<u>7,208</u>	<u>24,671</u>	<u>23,925</u>
Total Additions	<u>28,919</u>	<u>12,347</u>	<u>10,540</u>	<u>3,829</u>	<u>10,746</u>	<u>7,253</u>	<u>50,205</u>	<u>23,429</u>
<b>DEDUCTIONS</b>								
Deductions from net position attributed to:								
Distributions to plan members and beneficiaries	15,562	14,508	5,541	4,479	-	-	21,103	18,987
Medical premiums paid	-	-	-	-	5,440	5,061	5,440	5,061
Administrative expenses	119	107	-	-	69	64	188	171
Consultant and professional services expenses	<u>35</u>	<u>35</u>	-	-	-	-	<u>35</u>	<u>35</u>
Total Deductions	<u>15,716</u>	<u>14,650</u>	<u>5,541</u>	<u>4,479</u>	<u>5,509</u>	<u>5,125</u>	<u>26,766</u>	<u>24,254</u>
<b>Net increase in net position held in trust for retiree benefits</b>	13,203	(2,303)	4,999	(650)	5,237	2,128	23,439	(825)
<b>NET POSITION HELD IN TRUST FOR RETIREE BENEFITS</b>								
Beginning of year	<u>228,711</u>	<u>231,014</u>	<u>96,657</u>	<u>97,307</u>	<u>38,003</u>	<u>35,875</u>	<u>363,371</u>	<u>364,196</u>
<b>END OF YEAR</b>	<u>\$ 241,914</u>	<u>\$ 228,711</u>	<u>\$ 101,656</u>	<u>\$ 96,657</u>	<u>\$ 43,240</u>	<u>\$ 38,003</u>	<u>\$ 386,810</u>	<u>\$ 363,371</u>