
Road Commission of Kalamazoo County

(a component unit of the County of Kalamazoo, Michigan)

**Financial Report
with Supplemental Information
December 31, 2018**

Road Commission of Kalamazoo County

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Independent Auditor's Report

To the Board of County Road Commissioners
Road Commission of Kalamazoo County

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and the Road Fund of the Road Commission of Kalamazoo County (the "Road Commission"), a component unit of Kalamazoo County, Michigan, as of and for the year ended December 31, 2018 and the related notes to the financial statements, which collectively comprise the Road Commission of Kalamazoo County's basic financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities and the Road Fund of the Road Commission of Kalamazoo County as of December 31, 2018 and the changes in its financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

To the Board of County Road Commissioners
Road Commission of Kalamazoo County

Other Matters

Required Supplemental Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison schedule - Road Fund, and pension and OPEB system schedules, as identified 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, which 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 supplemental information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Road Commission of Kalamazoo County's basic financial statements. The other supplemental information, as identified in the table of contents, is presented for the purpose of additional analysis and is not a required part of the basic financial statements.

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

Plantz & Moran, PLLC

June 4, 2019

Road Commission of Kalamazoo County

Management's Discussion and Analysis

As management of the Road Commission of Kalamazoo County (the "Road Commission"), we offer readers this narrative overview and analysis of the financial activities for the year ended December 31, 2018.

The Road Commission is a special purpose government engaged in a single government program of road, bridge, and right-of-way maintenance, preservation, and construction for the County of Kalamazoo, Michigan (the "County"). The Road Commission of Kalamazoo County was established by a vote of the citizens of Kalamazoo County in 1909.

The following financial statements are presented in accordance with prescribed methods of accounting. The financial statements related to the governmental fund are prepared in modified accrual format, commonly referred to as governmental fund-level accounting. The full accrual method of accounting focuses on the entity as a whole (the Road Commission's net position) and is referred to as government-wide level accounting. The significant differences between the governmental fund statements and the government-wide statements relate to capital assets (buildings and equipment) and the infrastructure (roads, bridges, and signals). Capital assets and infrastructure costs are expensed when incurred in the governmental fund statements. In the government-wide statements, these costs are capitalized and recognized over their estimated useful lives through depreciation expense.

With respect to the statements of net position and activities, the fund-level financial statements and the government-wide financial statements have been combined and are presented on the same page.

Using this Annual Report

This annual report consists of four parts: management's discussion and analysis (this section), the basic financial statements, required supplemental information, and other supplemental information.

The basic financial statements are the governmental fund balance sheet/statement of net position; statement of governmental fund revenue, expenditures, and changes in fund balance/statement of activities; and notes to the financial statements. The notes to the financial statements are an integral part of the document that explain some of the information in the financial statements and provide more detailed data.

Additional data and schedules that further explain and support the information in the financial statements are provided in both the required supplemental information and the other supplemental information.

Government-wide Overall Financial Analysis

Net position over time may serve as a useful indicator of a government's financial position. In the case of the Road Commission, assets and deferred outflows of resources exceeded liabilities and deferred inflows by \$151,800,184 at the close of the most recent fiscal year.

To assess the overall health of the Road Commission, additional nonfinancial factors need to be considered, such as the condition of the roads in our jurisdiction and changes in the laws related to transportation funding and their distribution.

Road Commission of Kalamazoo County

Management's Discussion and Analysis (Continued)

The following tables provide condensed information about the Road Commission as of December 31, 2018 and 2017 and for the years then ended:

Road Commission's Net Position

| | <u>2018</u> | <u>2017</u> |
|--|-----------------------|-----------------------|
| Assets | | |
| Current and other assets | \$ 15,467,068 | \$ 13,893,968 |
| Capital assets | 139,621,859 | 134,188,660 |
| Total assets | 155,088,927 | 148,082,628 |
| Deferred Outflows of Resources | 2,025,074 | 204,608 |
| Liabilities - Current liabilities | 3,956,856 | 2,792,941 |
| Deferred Inflows of Resources | 1,356,961 | 2,377,792 |
| Net Position | | |
| Net investment in capital assets | 139,621,859 | 134,188,660 |
| Unrestricted | 12,178,325 | 8,927,843 |
| Total net position | <u>\$ 151,800,184</u> | <u>\$ 143,116,503</u> |

The Road Commission's net position increased 6.1 percent from a year ago - increasing from \$143,116,503 to \$151,800,184. This increase primarily relates to the investment of revenue dollars into infrastructure assets to be recognized into expense over a longer period of time, instead of during the year. Other contributing factors include the excess of total revenue over total expenditures, as outlined in Note 3.

Road Commission's Changes in Net Position

| | <u>2018</u> | <u>2017</u> |
|---|-----------------------|-----------------------|
| Revenue | | |
| Intergovernmental | \$ 29,090,104 | \$ 26,393,030 |
| Other revenue: | | |
| Other contributions and service charges | 384,657 | 1,040,050 |
| Other | 185,773 | 137,379 |
| Total revenue | 29,660,534 | 27,570,459 |
| Expenses | | |
| Primary maintenance | 5,405,769 | 6,964,855 |
| Local maintenance | 5,666,530 | 5,485,583 |
| Administrative | 851,689 | 573,170 |
| Equipment rental and other charges | (825,310) | (1,008,303) |
| Depreciation | 9,766,838 | 9,521,710 |
| Nonroad-related projects | 111,337 | 156,716 |
| Total expenses | 20,976,853 | 21,693,731 |
| Change in Net Position | 8,683,681 | 5,876,728 |
| Net Position - Beginning of year | 143,116,503 | 137,239,775 |
| Net Position - End of year | <u>\$ 151,800,184</u> | <u>\$ 143,116,503</u> |

Road Commission of Kalamazoo County

Management's Discussion and Analysis (Continued)

The Road Commission's revenue for the year ended December 31, 2018 increased approximately 7.6 percent from the prior year. This increase was primarily due to a combination of factors effecting intergovernmental revenue, as follows. The Road Commission experienced a 4 percent increase in the Michigan Transportation Fund (MTF) after accounting for the reductions resulting from the unexpected overpayments by the Treasury and the Michigan Department of Transportation (MDOT) to be returned. The Road Commission also received a one-time appropriation of approximately \$1.5 million from the State General Fund - Public Act (PA) 82 of 2018 for 2018 road projects, as well as a one-time appropriation of \$2.7 million from the State General Fund - PA 207 of 2018 for 2019 activities. Total expenses for the year decreased by approximately 3.3 percent primarily in preventive maintenance on primary roads.

Budgetary Highlights

Prior to beginning each year, the Road Commission's budget is prepared based upon certain assumptions and facts available at that time. During the year, the road commission board amends its budget to reflect changes in the original assumptions, facts, and/or economic conditions that were unknown at the time the original budget was adopted.

The Road Commission amended its 2018 budget during the year. The final budget for revenue was approximately \$4 million larger than the original budget, primarily due to the addition of preservation and structural improvement projects utilizing the PA 82 of 2018 funds and the recognition of PA 207 of 2018 funds for 2019. Our actual revenue ended the year lower than expected by approximately \$1.1 million, chiefly due to the notification in 2019 of the unexpected overpayment of MTF during 2018 and a federal grant project not being finalized as expected. The final budget for expenditures was very similar to the original budget. Actual expenditures at the end of the year were approximately \$1,286,000 less than the final amended budget, predominantly due to construction savings.

Capital Assets

The Road Commission ended the year with an increase in net capital assets amounting to \$5,433,199. Infrastructure continues to be the largest asset class and is funded by federal, state, and local government participation, as well as by road commission revenue. Depreciation of capital assets is provided for annually over estimated future lives.

| Capital Assets | Year Ended | |
|---------------------------------|------------------------------|------------------------------|
| | 2018 | 2017 |
| Land | \$ 475,599 | \$ 475,599 |
| Infrastructure land | 22,830,253 | 22,830,253 |
| Buildings and improvements | 4,503,327 | 4,468,104 |
| Land improvements | 402,561 | 402,561 |
| Road equipment | 11,485,449 | 10,789,993 |
| Other equipment | 839,913 | 821,010 |
| Infrastructure and improvements | <u>201,188,853</u> | <u>192,888,306</u> |
| Gross capital assets | 241,725,955 | 232,675,826 |
| Accumulated depreciation | <u>(102,104,096)</u> | <u>(98,487,166)</u> |
| Net capital assets | <u><u>\$ 139,621,859</u></u> | <u><u>\$ 134,188,660</u></u> |

Additional information regarding capital assets is located in Note 6 to the financial statements.

Road Commission of Kalamazoo County

Management's Discussion and Analysis (Continued)

Economic Factors and Next Year's Budget

The Road Commission considers many factors when finalizing the fiscal year budget.

Nationally and in Michigan, economic forecasts assume continued modest growth. Even with this growth, the State of Michigan continues to struggle with a long-term solution to infrastructure investment. The nation's balance in the Highway Trust Fund is on edge without a reduction in the size of surface transportation programs, an increase in revenue, or further general fund transfers (according to the *Congressional Research Service October 24, 2018 Funding and Financing Highways and Public Transportation Report*). More roads continue to deteriorate than can be improved with current funding levels. Other aspects of investment, asset management, and coordination are needed among various public infrastructure assets. Various reports and studies in Michigan are consistent in this message of needed investments for our infrastructure. Most recently those reports include:

- 21st Century Infrastructure Commission Report (2016)*
- 21st Century Michigan Infrastructure Commission (2018) Asset Management Final Report
- Michigan Transportation Asset Management County (2017) Annual Report
- TRIP Report: Modernizing Michigan's Transportation System: Progress and Challenges in Providing Safe, Efficient and Well-Maintained Roads, Highways and Bridges (2019)
- American Society of Civil Engineers, Michigan Section: *2018 Report Card for Michigan's Infrastructure*

Michigan's roads are vital to business and economic development, families and schools, public safety and health care, agriculture and tourism, and every aspect of our lives. Congestion, poor pavement condition, and crashes cost Michigan drivers and business in wasted fuel, lost time and productivity, vehicle maintenance costs, and more. As with many of the county road agencies in Michigan, we use an asset management system to prioritize our resources when it comes to taking care of the infrastructure under our jurisdiction. In most cases, the worst roads are not the same as the highest priority roads under an asset management approach. Michigan's infrastructure investment gap exceeds \$60 billion over the next 20 years, with an annual investment gap of approximately \$4 billion, of which a \$2.7 billion annual investment is necessary for transportation*. Addressing this substantial gap will require a combination of federal, state, local, private, and user-fee investments, as well as financing strategies to meet long-term needs.

The Michigan Transportation Fund is our main source of revenue for operating expenses, repair, and maintenance of the County's roads, bridges, and right of way. MTF funds are based on fuel taxes and vehicle registrations fees. A 2015 legislative transportation funding bill was designed to generate \$1.2 billion in new MTF revenue by 2021. During 2017, the Road Commission saw a 30 percent increase in MTF, and during 2018 a 4 percent increase. Though the increase was beneficial, it does not address the long-term issue of our declining road and infrastructure conditions. Many of the costs associated with critical road maintenance activities, including fuel, asphalt, and equipment, have increased far faster than the consumer rate of inflation, while funding continues to lag behind. The Road Commission has optimized the efficiency of operations under the existing revenue and continues to ensure it is in the process of continuous improvement. It has also invested in experiments and innovations to support further options in maintaining the infrastructure. This Road Commission, as well as across the nation, cannot change the course of road deterioration through efficiencies and innovation alone.

Federal Highway Funding

On December 4, 2015, President Obama signed the Fixing America's Surface Transportation (FAST) Act, which provides funding for transportation programs through 2020. This act includes \$70 billion in new funding to be transferred from the federal General Fund into the Highway Trust Fund through 2020. Michigan expected to see an increase of approximately 5 percent in federal transportation dollars over the following five years. There continues to be indications of further investments in federal funding to rebuild our infrastructure with the President Trump administration; however, there is not a clear forecast as to what that may entail.

Road Commission of Kalamazoo County

Management's Discussion and Analysis (Continued)

The Board of County Road Commissioners of the County of Kalamazoo, Michigan, management, and staff of the Road Commission continue to work diligently to be efficient and keep our expenses low, look for opportunities to partner with other agencies in our area and region, and access all available dollars to maintain the roads and infrastructure within Kalamazoo County. The results of this effort can be seen as you compare the condition of its roads and bridges across the state.

State Transportation Funding

On November 10, 2015, Governor Snyder signed a package of legislative transportation funding bills (Michigan Revenue Package) designed to generate \$1.2 billion in new MTF revenue by 2021. Approximately half of this total will come from increases in fuel taxes (\$400 million) and vehicle registration fees (\$200 million) starting in 2017. Then, beginning in 2019, potentially increasing amounts of General Fund dollars, reaching \$600 million in 2021, will be transferred to the MTF to be further distributed to the various road agencies in the State. Lastly, the fuel taxes will be indexed to inflation, using the Consumer Price Index (CPI), beginning January 1, 2022. It is important to note there is no guarantee with the General Fund dollars in years 2019-2021. As of this report, roads and bridges continue to be at the forefront of our legislators' debate on how to make more investments and fund our infrastructure long term.

Under the Federal Aid Highway Program, Michigan is eligible to use federal funds to improve the condition of highway bridges through replacement, rehabilitation, and preservation activities.

Established in 2004 Public Act 384, an amendment to Act 51, provides financial assistance to local highway authorities for the preservation, improvement, reconstruction of existing bridges, or the construction of bridges to replace existing bridges in whole or part. Revenue is provided from an Act 51 earmark of a half-cent of the gasoline excise tax (approximately \$22 million) and a separate Act 51 earmark (approximately \$5 million) of MTF revenue. Through legislation in 2004, Michigan created a Local Bridge Fund to be administered by the Local Bridge Advisory Board and seven Regional Bridge Councils. Funding from the Local Bridge Fund is allocated to each region based on available funds and weighted ratios provided in the legislation. The recent Michigan Revenue Package, which began in 2017, did not allocate additional funding to the local bridge program.

Local Funding

The financial commitment of township boards and residents through the years has proven invaluable. Although, not required, these partnerships help to provide better service to our joint constituencies and a long-term collaborative effort. For the local road system, the Road Commission establishes road improvement priorities that are developed in conjunction with township governments. Each township works with our designated staff to develop a five-year local road improvement plan supporting asset management for planning purposes and local road preservation. In 2018, Road Commission staff continued to work with townships to develop these plans. The Road Commission maintains a local road participation fund program that provides funds for each township that much be matched on a dollar-for-dollar basis for local road improvement projects. In 2018, the Road Commission applied \$1,700,000 toward this local match program. The Road Commission also shared an additional allocation of dollars to the local road system from Public Act 82 of 2018 for use in 2018. This was a unique, one-time allocation that did not require local township match. The additional allocations of \$300,000 of PA 82 funds to the local program provided a total local road commitment for 2018 of \$2,000,000. These projects include local road preservation-structural improvement, preventive maintenance, and construction projects, such as chip seal, hot mix asphalt (HMA) overlays, and road reconstruction.

Requests for Further Information

This financial report is intended to provide a general overview of the Road Commission's finances and demonstrate the Road Commission's accountability for the money it receives. If you have questions about this report or need additional information, please contact us by mail at Road Commission of Kalamazoo County, 3801 East Kilgore Road, Kalamazoo, MI 49001, or visit our website at www.kalamazooountyroads.com and view our full 2018 annual report.

Road Commission of Kalamazoo County

Governmental Funds Statement of Net Position/Governmental Fund Balance Sheet

December 31, 2018

| | Modified Accrual Basis | | Statement of Net Position |
|---|------------------------|-----------------------|---------------------------|
| | Road Fund | Adjustments | |
| Cash | | | |
| Cash (Note 5) | \$ 8,699,032 | \$ - | \$ 8,699,032 |
| Receivables: | | | |
| Special assessments receivable | 13,116 | - | 13,116 |
| Due from state transportation department | 2,792,552 | - | 2,792,552 |
| Due on county road agreements | 274,094 | - | 274,094 |
| Sundry accounts receivable | 1,271,540 | - | 1,271,540 |
| Inventory | 1,087,321 | - | 1,087,321 |
| Prepaid expenses | 161,685 | - | 161,685 |
| Advances | 184,603 | - | 184,603 |
| Prepaid construction | 31,359 | - | 31,359 |
| Net pension asset (Note 7) | - | 951,766 | 951,766 |
| Capital assets: (Note 6) | | | |
| Assets not subject to depreciation | - | 23,305,852 | 23,305,852 |
| Assets subject to depreciation - Net | - | 116,316,007 | 116,316,007 |
| Total assets | 14,515,302 | 140,573,625 | 155,088,927 |
| Deferred Outflows of Resources | | | |
| Deferred pension costs (Note 7) | - | 1,630,025 | 1,630,025 |
| Deferred OPEB costs (Note 8) | - | 395,049 | 395,049 |
| Total deferred outflows of resources | - | 2,025,074 | 2,025,074 |
| Total cash and deferred outflows of resources | \$ 14,515,302 | 142,598,699 | 157,114,001 |
| Liabilities | | | |
| Accounts payable | \$ 1,680,202 | - | 1,680,202 |
| Accrued liabilities and other | 133,007 | - | 133,007 |
| Advances | 278,993 | - | 278,993 |
| State transportation department overpayment repayable | 505,945 | - | 505,945 |
| Noncurrent liabilities: | | | |
| Due within one year - Compensated absences | - | 151,040 | 151,040 |
| Due in more than one year - Net OPEB liability (Note 8) | - | 1,207,669 | 1,207,669 |
| Total liabilities | 2,598,147 | 1,358,709 | 3,956,856 |
| Deferred Inflows of Resources | | | |
| Unavailable revenue | 13,116 | (13,116) | - |
| Deferred pension cost reductions (Note 7) | - | 791,910 | 791,910 |
| Deferred OPEB cost reductions (Note 8) | - | 565,051 | 565,051 |
| Total deferred inflows of resources | 13,116 | 1,343,845 | 1,356,961 |
| Equity | | | |
| Fund balance: | | | |
| Nonspendable | 1,280,365 | (1,280,365) | - |
| Unassigned | 10,623,674 | (10,623,674) | - |
| Total fund balance | 11,904,039 | (11,904,039) | - |
| Total liabilities, deferred inflows of resources, and fund balance | \$ 14,515,302 | | |
| Net Position | | | |
| Net investment in capital assets (Note 6) | | 139,621,859 | 139,621,859 |
| Unrestricted | | 12,178,325 | 12,178,325 |
| Total net position | | \$ 151,800,184 | \$ 151,800,184 |

Road Commission of Kalamazoo County

Governmental Funds Statement of Activities/Governmental Fund Revenue, Expenditures, and Changes in Fund Balance

Year Ended December 31, 2018

| | Modified Accrual Basis | | Statement of Activities |
|--|---------------------------|-----------------------|----------------------------|
| | Road Fund | Adjustments | |
| Revenue | | | |
| Intergovernmental: | | | |
| Federal grants | \$ 1,098,028 | \$ - | \$ 1,098,028 |
| State-shared revenue and grants: | | | |
| General state aid | 4,280,045 | - | 4,280,045 |
| Michigan Transportation Fund | 19,336,647 | - | 19,336,647 |
| Township and other governmental contributions | 4,375,384 | - | 4,375,384 |
| Other revenue: | | | |
| Other contributions and service charges | 384,657 | - | 384,657 |
| Miscellaneous | 200,308 | (14,535) | 185,773 |
| Total revenue | <u>29,675,069</u> | <u>(14,535)</u> | <u>29,660,534</u> |
| Expenditures | | | |
| Preservation/Structural improvements: | | | |
| Roads | 9,052,103 | (9,052,103) | - |
| Structures | 5,087,153 | (5,087,153) | - |
| Routine and preventive maintenance: | | | |
| Roads | 5,405,769 | - | 5,405,769 |
| Structures | 5,666,530 | - | 5,666,530 |
| Administrative | 1,262,709 | (411,020) | 851,689 |
| Equipment - Net | (825,310) | - | (825,310) |
| Capital outlay - Net | 1,060,781 | (1,060,781) | - |
| Depreciation expense | - | 9,766,838 | 9,766,838 |
| Work performed for other governmental units | 111,337 | - | 111,337 |
| Total expenditures/expenses | <u>26,821,072</u> | <u>(5,844,219)</u> | <u>20,976,853</u> |
| Net Change In Fund Balance/Net Position | 2,853,997 | 5,829,684 | 8,683,681 |
| Fund Balance/Net Position - Beginning of year | 9,050,042 | 134,066,461 | 143,116,503 |
| Fund Balance/Net Position - End of year | <u>\$ 11,904,039</u> | <u>\$ 139,896,145</u> | <u>\$ 151,800,184</u> |

Note 1 - Nature of Business

The Road Commission of Kalamazoo County (the "Road Commission") is a special purpose governmental agency engaged in a single government program of road and bridge maintenance, preservation, and construction for the County of Kalamazoo, Michigan (the "County"). The Road Commission is the jurisdictional authority over all public roads lying outside the incorporated cities and villages within the County exclusive of any Michigan Department of Transportation (MDOT) state trunkline highways. The Road Commission is governed by a five-member Board of County Road Commissioners appointed by the Kalamazoo County Board of Commissioners. The Road Commission's financial statements will be included in the basic financial statements of the County as a discretely presented component unit for financial reporting purposes only.

Note 2 - Significant Accounting Policies

Accounting and Reporting Principles

The Road Commission follows accounting principles generally accepted in the United States of America (U.S. GAAP), as applicable to governmental units. Accounting and financial reporting pronouncements are promulgated by the Governmental Accounting Standards Board. The following is a summary of the significant accounting policies used by the Road Commission:

Report Presentation

Governmental accounting principles require that financial reports include two different perspectives - the government-wide perspective and the fund-based perspective. The individual Road Fund column presents the activity on the modified accrual basis of accounting, as discussed above, which demonstrates accountability for how the current resources have been spent. The government-wide column is presented on the economic resources measurement focus and the full accrual basis of accounting in order to measure the cost of providing government services and the extent to which constituents have paid the full cost of government services.

On the full accrual basis of accounting, revenue is recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Fund Accounting

The Road Commission accounts for its activities in one major governmental fund, the Road Fund. The Road Fund is used to account for all activities of the Road Commission.

Basis of Accounting

The Road Fund uses the current financial resources measurement focus and the modified accrual basis of accounting. This basis of accounting is intended to better demonstrate accountability for how the Road Commission has spent its resources.

Expenditures are reported when the goods are received or the services are rendered. Capital outlays are reported as expenditures (rather than as capital assets) because they reduce the ability to spend resources in the future; conversely, employee benefit costs that will be funded in the future (such as pension and retiree healthcare-related costs or sick and vacation pay) are not counted until they come due for payment. In addition, debt service expenditures, claims, and judgments are recorded only when payment is due.

Revenue is not recognized until it is collected or collected soon enough after the end of the year that it is available to pay for obligations outstanding at the end of the year. For this purpose, the Road Commission considers amounts collected within 60 days of year end to be available for recognition. The following major revenue sources meet the availability criterion: state gas and weight tax revenue and revenue related to construction projects and inspection work orders. Conversely, special assessments will be collected after the period of availability; receivables have been recorded for these, along with a "deferred inflow."

Note 2 - Significant Accounting Policies (Continued)

Specific Balances and Transactions

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, demand deposits, and short-term investments with a maturity of three months or less when acquired.

Due from State Transportation Department and Due on County Road Agreements

Due from state transportation department consists of amounts due from the Michigan Transportation Fund (MTF) for state-shared revenue. Due on county road agreements consists of receivables from townships, cities, and villages for their share of construction projects.

Inventories and Prepaid Items

Inventories are valued at cost on a weighted-average basis. Inventories consist principally of road material, salt, signs, and equipment maintenance materials. Inventories of governmental funds are recorded as expenditures when consumed rather than when purchased. Certain payments to vendors reflect costs applicable to future fiscal years and are recorded as prepaid items in both government-wide and fund financial statements.

Prepaid Construction

Prepaid construction results when progress payments made to MDOT are in excess of the total expenses incurred for projects on a percentage of completion basis. The payments will be applied to projects in future years as costs are incurred.

Capital Assets

Capital assets, which include property, buildings, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the government-wide financial statements. Capital assets are defined by the Road Commission as assets with an initial individual cost of more than \$2,500 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated acquisition value at the date of donation, with the related revenue recorded as other contributions.

Land is not subject to depreciation, road equipment is depreciated using the "sum of the years' digits" method, and all other capital asset classes are depreciated using the straight-line method over the following useful lives:

| <u>Capital Asset Class</u> | <u>Depreciable Life - Years</u> |
|----------------------------|-------------------------------------|
| Infrastructure | 5-50 |
| Buildings | 25-50 |
| Road equipment | 5-8 |
| Other equipment | 4-20 |

Deferred Outflows/Inflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element represents a consumption of net position that applies to a future period and will not be recognized as an outflow of resources (expense/expenditure) until then. The Road Commission reports a deferred outflow of resources related to the defined benefit pension plan and the retiree healthcare plan, which is only reported in the government-wide financial statements.

Note 2 - Significant Accounting Policies (Continued)

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element represents an acquisition of net position that applies to a future period and will not be recognized as an inflow of resources (revenue) until that time. The Road Commission reports a deferred inflow of resources related to unavailable revenue from special assessments and is only reported in the governmental fund balance sheet. This amount is deferred and recognized as an inflow of resources in the period that the amount becomes available. The Road Commission also reports deferred inflows of resources related to the defined benefit pension plan and the retiree healthcare plan, which are only reported in the government-wide financial statements.

Net Position

Net position of the Road Commission is classified in three components. Net investment in capital assets - net of related debt consists of capital assets net of accumulated depreciation and is reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. Restricted net position is further classified as expendable and nonexpendable. Expendable restricted net position has been limited for use by donors and is held in trust for various uses. Nonexpendable restricted net position has been restricted by donors to be maintained in perpetuity. The Road Commission does not have restricted net position. Unrestricted net position is the remaining net position that does not meet the definition of invested in capital or restricted.

Net Position Flow Assumption

The Road Commission will sometimes fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted net position and unrestricted net position in the government-wide financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the government's policy to consider restricted net position to have been depleted before unrestricted net position is applied.

Fund Balance Flow Assumptions

The Road Commission will sometimes fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the government's policy to consider restricted fund balance to have been depleted before using any of the components of unrestricted fund balance. Furthermore, when the components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first followed by assigned fund balance. Unassigned fund balance is applied last.

Fund Balance Policies

Fund balance of governmental funds is reported in various categories based on the nature of any limitations requiring the use of resources for specific purposes. The government itself can establish limitations on the use of resources through either a commitment (committed fund balance) or an assignment (assigned fund balance).

The committed fund balance classification includes amounts that can be used only for the specific purposes determined by a formal action of the government's highest level of decision-making authority. The Board of County Road Commissioners is the highest level of decision-making authority for the government that can, by adoption of a resolution prior to the end of the fiscal year, commit fund balance. Once adopted, the limitation imposed by the resolution remains in place until a similar action is taken (the adoption of another resolution) to remove or revise the limitation.

Note 2 - Significant Accounting Policies (Continued)

Amounts in the assigned fund balance classification are intended to be used by the government for specific purposes but do not meet the criteria to be classified as committed. The Road Commission has, by resolution, authorized the finance director to assign fund balance. The Board of County Road Commissioners may also assign fund balance as it does when appropriating fund balance to cover a gap between estimated revenue and appropriations in the subsequent year's appropriated budget. Unlike commitments, assignments generally only exist temporarily. In other words, an additional action does not normally have to be taken for the removal of an assignment. Conversely, as discussed above, an additional action is essential to either remove or revise a commitment.

Beginning in January 2014 and continued in 2018, the Road Commission set a goal to maintain a minimum fund balance of 30 - 40 percent of MTF revenue in the Road Fund. This is deemed to be the prudent amount to maintain the Road Commission's ability to meet obligations as they come due throughout the year and for emergency issues that may arise.

Pension

The Road Commission offers a defined benefit pension plan to its employees through the Kalamazoo County Employees' Retirement System. The Road Commission records a net pension asset for its proportionate share of the aggregate net pension asset. For the purpose of measuring the net pension asset, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Road Commission's portion of the Kalamazoo County Employees' Retirement System and additions to/deductions from the pension plan's fiduciary net position have been determined on the same basis as they are reported by the pension plan. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Other Postemployment Benefit Costs (OPEB)

The Road Commission offers retiree healthcare benefits to retirees. The Road Commission records a net OPEB liability for the difference between the total OPEB liability calculated by the actuary and the OPEB plan's fiduciary net position. For the purpose of measuring the net OPEB liability, deferred outflows of resources and deferred inflows of resources related to OPEB, and OPEB expense, information about the fiduciary net position of the OPEB plan and additions to/deductions from the OPEB plan's fiduciary net position have been determined on the same basis as they are reported by the OPEB plan. For this purpose, benefit payments are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value, except for money market investments and participating interest-earning investment contracts that have a maturity at the time of purchase of one year or less, which are reported at cost.

Compensated Absences (Vacation and Sick Leave)

It is the Road Commission's policy to permit employees to accumulate earned but unused sick and vacation pay benefits. There is no liability for unpaid accumulated sick leave since the Road Commission does not have a policy to pay any amounts when employees separate from service with the Road Commission, except at retirement for nonbargaining employees. All vacation pay is accrued when incurred in the government-wide financial statements. A liability for these amounts is reported in the Road Fund only for employee terminations as of year end.

Use of Estimates

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

Note 2 - Significant Accounting Policies (Continued)

Upcoming Accounting Pronouncements

In November 2016, the Governmental Accounting Standards Board (GASB) issued Statement No. 83, *Certain Asset Retirement Obligations*, which establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for asset retirement obligations. The Road Commission is currently evaluating the impact this standard will have on the financial statements when adopted. The provisions of this statement are effective for the Road Commission's financial statements for the year ending December 31, 2019.

In June 2017, the GASB issued Statement No. 87, *Leases*, which improves accounting and financial reporting for leases by governments. This statement requires recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources. The Road Commission is currently evaluating the impact this standard will have on the financial statements when adopted. The provisions of this statement are effective for the Road Commission's financial statements for the year ending December 31, 2020.

Note 3 - Reconciliation of Individual Fund Columns of the Statement of Net Position/Statement of Activities

Net position reported in the statement of net position column is different than the fund balance reported in the Road Fund column because of the different measurement focus and basis of accounting, as discussed in Note 2. Below is a reconciliation of the differences:

| | |
|---|-----------------------|
| Fund Balance Reported in Governmental Funds | \$ 11,904,039 |
| Amounts reported for governmental activities in the statement of net position are different because: | |
| Capital assets used in governmental activities are not financial resources and are not reported in the funds | 139,621,859 |
| Special assessment and state funding receivables that are not collected soon after year end are not available to pay for current period expenditures and, therefore, are reported as unavailable revenue in the funds | 13,116 |
| Some employee fringe benefits are payable over a long period of years and do not represent a claim on current financial resources; therefore, they are not reported in the funds: | |
| Employee compensated absences | (151,040) |
| Pension benefits | 1,789,881 |
| Retiree healthcare benefits | (1,377,671) |
| Net Position of Governmental Activities | \$ 151,800,184 |

December 31, 2018

Note 3 - Reconciliation of Individual Fund Columns of the Statement of Net Position/Statement of Activities (Continued)

The change in net position reported in the statement of activities column is different than the change in fund balance reported in the Road Fund column because of the different measurements focus and basis of accounting, as discussed in Note 2. Below is a reconciliation of the differences:

| | |
|--|---------------------|
| Net Change in Fund Balance Reported in Governmental Funds | \$ 2,853,997 |
| Amounts reported for governmental activities in the statement of activities are different because: | |
| Governmental funds report capital outlays as expenditures; however, in the statement of activities, these costs are allocated over their estimated useful lives as depreciation: | |
| Capital outlay | 15,200,037 |
| Depreciation expense | (9,766,838) |
| Revenue in the statement of activities that does not provide current financial resources is not reported as revenue in the funds until it is available | (14,535) |
| Some employee costs (pension, OPEB, and compensated absences) do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental funds | 411,020 |
| Change in Net Position of Governmental Activities | \$ 8,683,681 |

Note 4 - Stewardship, Compliance, and Accountability

Budgetary Information

The Road Commission is legally subject to the budgetary control requirements of State of Michigan Public Act (PA) 621 of 1978 (the "Uniform Budgeting Act"). The following is a summary of the requirements of this act according to the state treasurer's Bulletin for Audits of Local Units of Government in Michigan, dated April 1982, as amended by PA 493 of 2000:

- Budgeted expenditures cannot exceed budgeted revenue and fund balance.
- The budgets must be amended when necessary.
- Public hearings must be held before budget adoption.
- Expenditures cannot exceed budget appropriations.
- Expenditures must be authorized by a budget before being incurred.

Pursuant to this requirement, the Road Commission follows these procedures:

- The managing director submits a proposed operating budget for the fiscal year to the Board of County Road Commissioners before the beginning of the fiscal year. The budget includes proposed expenditures and the means of providing them.
- A public hearing is held to obtain comments.
- Prior to the beginning of the year, the budget and appropriations are legally adopted by the Board of County Road Commissioners.
- Comparison of budget-to-actual activity is used as a management control device throughout the year.
- Budgets are prepared using the modified accrual basis of accounting.
- The budgetary information presented may be amended throughout the year by an official action of the Board of County Road Commissioners.

Note 4 - Stewardship, Compliance, and Accountability (Continued)

Excess of Expenditures Over Appropriations in Budgeted Funds

The law requires budget amendments as needed to prevent actual expenditures from exceeding those provided in the budget. During the year ended December 31, 2018, the Road Commission had expenditure budget overruns as listed in the chart below. These overruns were due to minor timing differences.

| | Budget | Actual |
|--|--------------|--------------|
| Preservation and structural improvements - Local road system | \$ 6,526,000 | \$ 6,580,768 |
| Work performed for others | 95,000 | 111,337 |

Note 5 - Deposits and Investments

Michigan Compiled Laws Section 129.91 (Public Act 20 of 1943, as amended) authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The law also allows investments outside the state of Michigan when fully insured. The local unit is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States; repurchase agreements; bankers' acceptances of United States banks; commercial paper rated within the two highest classifications, which matures not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions, which are rated as investment grade; and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan.

The Road Commission has designated two banks for the deposit of its funds. The investment policy adopted by the board in accordance with Public Act 196 of 1997 has authorized investment in bonds and securities of the United States government and bank accounts and CDs, but not the remainder of state statutory authority, as listed above. The Road Commission's investments comply with all required laws and regulations.

The Road Commission's cash and investments are subject to several types of risk, which are examined in more detail below:

Custodial Credit Risk of Bank Deposits

Custodial credit risk is the risk that, in the event of a bank failure, the Road Commission's deposits may not be returned to it. The Road Commission does not have a deposit policy for custodial credit risk. At year end, the Road Commission had no bank deposits (certificates of deposit and checking and savings accounts) that were uninsured and uncollateralized. The Road Commission believes that, due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, the Road Commission evaluates each financial institution with which it deposits funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

In addition, at December 31, 2018, the Road Commission had approximately \$8,700,000 of bank deposits that were held by the County's treasurer on its behalf. Of this amount, \$250,000 was insured. The remaining amount is insured up to the \$250,000 limit, but is based on the combined amount of all county accounts. Therefore, the specific insured amount for the Road Commission is unknown.

Note 6 - Capital Assets

Capital asset activity of the Road Commission's governmental activities was as follows:

| | Balance January 1, 2018 | Additions and Depreciation | Disposals and Adjustments | Balance December 31, 2018 |
|--|-------------------------------|-------------------------------|------------------------------|---------------------------------|
| Capital assets not being depreciated: | | | | |
| Land | \$ 475,599 | \$ - | \$ - | \$ 475,599 |
| Infrastructure land | 22,830,253 | - | - | 22,830,253 |
| Subtotal | 23,305,852 | - | - | 23,305,852 |
| Capital assets being depreciated: | | | | |
| Buildings and improvements | 4,468,104 | 35,223 | - | 4,503,327 |
| Land improvements | 402,561 | - | - | 402,561 |
| Road equipment | 10,789,993 | 1,004,015 | (308,559) | 11,485,449 |
| Other equipment | 821,010 | 21,544 | (2,641) | 839,913 |
| Infrastructure and improvements | 192,888,306 | 14,139,255 | (5,838,708) | 201,188,853 |
| Subtotal | 209,369,974 | 15,200,037 | (6,149,908) | 218,420,103 |
| Accumulated depreciation: | | | | |
| Buildings and improvements | 2,738,795 | 88,542 | - | 2,827,337 |
| Land improvements | 192,907 | 57,478 | - | 250,385 |
| Road equipment | 8,371,563 | 976,633 | (308,559) | 9,039,637 |
| Other equipment | 660,949 | 52,414 | (2,641) | 710,722 |
| Infrastructure and improvements | 86,522,952 | 8,591,771 | (5,838,708) | 89,276,015 |
| Subtotal | 98,487,166 | 9,766,838 | (6,149,908) | 102,104,096 |
| Net capital assets being depreciated | 110,882,808 | 5,433,199 | - | 116,316,007 |
| Net governmental activities capital assets | <u>\$ 134,188,660</u> | <u>\$ 5,433,199</u> | <u>\$ -</u> | <u>\$ 139,621,859</u> |

Note 7 - Defined Benefit Pension Plan

Plan Description

The Road Commission participates in the Kalamazoo County Employees' Retirement System (the "System"). The System is a single-employer, defined benefit pension plan that provides retirement and disability benefits to eligible plan members and beneficiaries. The System was established by the County of Kalamazoo Board of Commissioners and is administered by the Office of Finance of the County of Kalamazoo, Michigan. Accordingly, it is included as a pension trust fund in the County's Comprehensive Annual Financial Report. The County, the Road Commission, and Kalamazoo Community Mental Health and Substance Abuse Services (the "Authority") are participating employers of the System.

The pension system issues a publicly available financial report that can be obtained at by writing to the System at 201 W. Kalamazoo Avenue, Kalamazoo, MI 49007 or by calling (269) 384-8111.

Benefits Provided

The Kalamazoo County Employees' Retirement Plan System provides retirement, disability, and death benefits to the members and their beneficiaries.

Retirement benefits for employees are calculated as a percent of the employee's final average salary (FAS) times the employee's years of service, 2.1 percent for nonunion and 2.2 percent for Teamsters State County and Municipal Workers Local 214. The FAS is calculated using the highest five consecutive years out of the last 10 years, some lump sums included. Normal retirement age is 60 with eight or more years of service or age 55 with 25 or more years of service. For members retiring after age 60 with at least eight years of service, the amount will be calculated using the greater of (a) the benefit based on service, FAS, and multiplier, or (b) the actuarial equivalent of the benefit accrued at age 60. The maximum employer-financed portion is 75 percent of FAS.

Note 7 - Defined Benefit Pension Plan (Continued)

Early retirement age is 55 with eight or more years of service. The amount is then computed as a regular retirement, but reduced 4/10 of 1 percent (0.004) for each month of age preceding age 60.

Employees are eligible for nonduty disability benefits after 10 or more years of service and for duty-related disability benefits upon hire. Disability retirement benefits are determined in the same manner as retirement benefits, but with a minimum benefit of 15 percent of FAS.

Employees are eligible for death benefits after 10 or more years of service or age 60 with eight years of service. The amount is computed as a regular retirement, but actuarially reduced in accordance with a 100 percent joint and survivor election.

Benefit terms are established and amended by authority of the Board of County Road Commissioners.

Contributions

State law requires public employers to make pension contributions in accordance with an actuarial valuation. The Kalamazoo County Employees' Retirement Plan System hires an independent actuary for this purpose and annually contributes the amount determined to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The Road Commission's required contribution is determined after consideration of the required contribution rate of employees. For the year ended December 31, 2018, no contribution was required in the current year. Plan members are currently not required to contribute to the System.

Net Pension Asset

At December 31, 2018, the Road Commission reported an asset of \$951,766 for its proportionate share of the net pension asset. The System's net pension asset was measured as of December 31, 2018, and the total pension liability, used to calculate the net pension asset, was determined by an actuarial valuation as of December 31, 2017, which used updated procedures to roll forward the estimated liability to December 31, 2018. The Road Commission followed the allocation methodology directed by the County to the actuary, and, as such, the Road Commission's proportionate share of the System's net pension asset was determined based on the Road Commission's relative percentage of the present value of the future benefits for its participants in relation to the present value of the future benefits for the System as a whole. Based on its separately issued actuarial funding valuation as of the same date, the Road Commission's overfunded accrued liability (excess assets at market value) is \$4,906,323 as of December 31, 2018 and \$7,480,294 as of December 31, 2017.

Pension Expense and Deferrals

For the year ended December 31, 2018, the Road Commission recognized pension recovery of \$259,658.

At December 31, 2018, the Road Commission reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

| | Deferred Outflows of Resources | Deferred Inflows of Resources |
|--|--------------------------------------|-------------------------------------|
| Difference between expected and actual experience | \$ 127,924 | \$ 59,862 |
| Changes in assumptions | 323,944 | - |
| Net difference between projected and actual earnings on pension plan investments | 1,126,878 | - |
| Changes in proportionate share or difference between amount contributed and proportionate share of contributions | 51,279 | 732,048 |
| Total | <u>\$ 1,630,025</u> | <u>\$ 791,910</u> |

Note 7 - Defined Benefit Pension Plan (Continued)

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

| Years Ending December 31 | Amount |
|-----------------------------|-------------------|
| 2019 | \$ (127,498) |
| 2020 | 149,525 |
| 2021 | 299,428 |
| 2022 | 516,660 |
| Total | <u>\$ 838,115</u> |

Actuarial Assumptions

The total pension liability in the December 31, 2017 actuarial valuation was determined using an inflation assumption ranging from 2.75 to 3.5 percent; assumed salary increases (including inflation) ranging from 3.5 to 7.23 percent; an investment rate of return (net of investment expenses) of 7.25 percent; and the RP-2000 mortality tables, projected 20 years with U.S. Projection Scale BB.

The investment rate of return decreased from 7.50 to 7.25 for the December 31, 2018 actuarial valuation.

Discount Rate

The discount rate used to measure the total pension liability was 7.25 percent.

Projected Cash Flows

Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make 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 asset.

Investment Rate of Return

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return as of December 31, 2018 for each major asset class are summarized in the following table:

| Asset Class | Target Allocation | Long-term Expected Real Rate of Return |
|--------------------------------|-------------------|--|
| U.S. small cap (Manager 1) | 5.00 % | 5.34 % |
| U.S. small cap (Manager 2) | 10.00 | 5.34 |
| International developed equity | 10.00 | 7.34 |
| U.S. large cap (Manager 1) | 30.00 | 5.04 |
| U.S. large cap (Manager 2) | 5.00 | 5.04 |
| Emerging markets | 10.00 | 6.84 |
| Domestic fixed income | 25.00 | 1.34 |
| Real estate (Manager 1) | 2.50 | 3.94 |
| Real estate (Manager 2) | 2.50 | 3.94 |

Note 7 - Defined Benefit Pension Plan (Continued)

Sensitivity of the Net Pension Asset to Changes in the Discount Rate

The following presents the net pension asset of the Road Commission, calculated using the discount rate of 7.25 percent, as well as what the Road Commission's net pension (liability) asset would be if it were calculated using a discount rate that is 1 percentage point lower or 1 percentage point higher than the current rate:

| | 1 Percent Decrease (6.25%) | Current Discount Rate (7.25%) | 1 Percent Increase (8.25%) |
|-------------------------------|----------------------------------|-------------------------------------|----------------------------------|
| Net pension (liability) asset | \$ (747,000) | \$ 951,766 | \$ 2,372,729 |

Pension Plan Fiduciary Net Position

Detailed information about the plan's fiduciary net position is available in the separately issued financial report. For the purpose of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pension, and pension expense, information about the plan's fiduciary net position and additions to/deductions from fiduciary net position have been determined on the same basis as they are reported by the plan. The plan uses the economic resources measurement focus and the full accrual basis of accounting. Investments are stated at fair value. Contribution revenue is recorded as contributions are due, pursuant to legal requirements. Benefit payments and refunds of employee contributions are recognized as expense when due and payable in accordance with the benefit terms.

Note 8 - Other Postemployment Benefit Plan

Plan Description

The Road Commission provides retiree medical benefits for all employees who meet eligibility requirements. The benefits are provided through the Kalamazoo County Retiree Medical Benefits Plan (the "Plan"), a single-employer plan established by the County Board of Commissioners and administered by the Office of Finance of the County. Kalamazoo County Retiree Medical Benefits Plan issues a publicly available financial report that can be obtained at 201 W. Kalamazoo Avenue, Kalamazoo, MI 49007 or by calling (269) 384-8111.

Benefits Provided

The Plan provides healthcare, dental, and vision benefits for retirees and their dependents. Benefits are provided to nonunion members hired on or before December 31, 2012 and union members hired on or before December 31, 2016, age 55 with 25 years of service or age 60 with eight years of service. Nonunion members hired on or after January 1, 2013 and union members hired on or after January 1, 2017 are not eligible for retiree healthcare benefits.

Benefits are established and can be amended by the Board of Road Commissioners.

Contributions

The County of Kalamazoo, Michigan establishes contribution rates based on an actuarially determined rate per a funding valuation. The Plan hires an independent actuary for this purpose and annually contributes the amount determined. Retirees will contribute 20 percent of the premium cost annually. Retirees pay the full cost of vision and dental coverage. The Road Commission's contractually determined contributions for the year ended December 31, 2018 was \$125,066. Actual contributions to the plan from the Road Commission were \$211,297 for the year ended December 31, 2018.

Note 8 - Other Postemployment Benefit Plan (Continued)

Net OPEB Liability

At December 31, 2018, the Road Commission reported a liability of \$1,207,669 for its proportionate share of the net OPEB liability. The net OPEB liability was measured as of December 31, 2018, and the total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of December 31, 2017, which used updated procedures to roll forward the estimated liability to December 31, 2018. The Road Commission's proportion of the net OPEB liability was based on the Road Commission's actuarially determined contribution for the year ended December 31, 2017 relative to all other contributing employers. At December 31, 2017, the Road Commission's proportion was 2.903 percent.

OPEB Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB

For the year ended December 31, 2018, the Road Commission recognized OPEB expense of \$62,586 and OPEB contributions of \$211,297.

At December 31, 2018, the Road Commission reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

| | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|--------------------------------------|-------------------------------------|
| Difference between expected and actual experience | \$ - | \$ 565,051 |
| Changes in assumptions | 213,032 | - |
| Net difference between projected and actual earnings on OPEB plan investments | 182,017 | - |
| Total | \$ 395,049 | \$ 565,051 |

Amounts reported as deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows:

| Years Ending December 31 | Amount |
|-----------------------------|--------------|
| 2019 | \$ (90,576) |
| 2020 | (90,576) |
| 2021 | (46,932) |
| 2022 | 58,082 |
| Total | \$ (170,002) |

Actuarial Assumptions

The total OPEB liability in the December 31, 2017 actuarial valuation was determined using an inflation assumption of 3.5 percent, assumed salary increases (including inflation) from 3.5 to 7.23 percent, an investment rate of return (net of investment expenses) of 7.25 percent, a healthcare cost trend rate of 9.0 percent decreasing to 3.5 percent, and using the RP-2000 Mortality Combined Healthy Tables, projected 20 years with U.S. Projection Scale BB. These assumptions were applied to all periods included in the measurement.

The investment rate of return decreased from 7.50 to 7.25 for the December 31, 2018 actuarial valuation.

The actuarial assumptions used in the December 31, 2017 valuation were based on the results of an actuarial experience study for the five-year period ended December 31, 2013.

Note 8 - Other Postemployment Benefit Plan (Continued)

Discount Rate

The discount rate used to measure the total OPEB liability was 7.25 percent. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that Road Commission contributions will be made at rates equal to the difference between actuarially determined contribution rates and the employee rate.

Based on those assumptions, the OPEB plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on OPEB plan investments was applied to all periods of projected benefit payments to determine the total OPEB liability.

Investment Rate of Return

The long-term expected rate of return on OPEB plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of OPEB plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and adding expected inflation. Best estimates of arithmetic real rates of return as of the December 31, 2018 measurement date for each major asset class included in the OPEB plan's target asset allocation, as disclosed in the investment footnote, are summarized in the following tables:

| Asset Class | Target Allocation | Long-term Expected Real Rate of Return |
|--------------------------------|-------------------|--|
| U.S. small cap (Manager 1) | 5.00 % | 5.34 % |
| U.S. small cap (Manager 2) | 10.00 | 5.34 |
| International developed equity | 10.00 | 7.34 |
| U.S. large cap (Manager 1) | 30.00 | 5.04 |
| U.S. large cap (Manager 2) | 5.00 | 5.04 |
| Emerging markets | 10.00 | 6.84 |
| Domestic fixed income | 25.00 | 1.34 |
| Real estate (Manager 1) | 2.50 | 3.94 |
| Real estate (Manager 2) | 2.50 | 3.94 |

Sensitivity of the Net OPEB Liability to Changes in the Discount Rate

The following presents the net OPEB liability of the Road Commission, calculated using the discount rate of 7.25 percent, as well as what the Road Commission's net OPEB liability would be if it were calculated using a discount rate that is 1 percentage point lower or 1 percentage point higher than the current rate:

| | 1 Percent Decrease (6.25%) | Current Discount Rate (7.25%) | 1 Percent Increase (8.25%) |
|---|----------------------------------|-------------------------------------|----------------------------------|
| Net OPEB liability of the Road Commission | \$ 1,526,199 | \$ 1,207,669 | \$ 935,252 |

Note 8 - Other Postemployment Benefit Plan (Continued)

Sensitivity of the Net OPEB Liability to Changes in the Healthcare Cost Trend Rate

The following presents the net OPEB liability of the Road Commission, calculated using the healthcare cost trend rate of 9.0 percent decreasing to 3.5 percent, as well as what the Road Commission's net OPEB liability would be if it were calculated using a healthcare cost trend rate that is 1 percentage point lower or 1 percentage point higher than the current rate:

| | 1 Percent Decrease (8.0%) decreasing to 2.5%) | Current Healthcare Cost Trend Rate (9.0%) decreasing to 3.5%) | 1 Percent Increase (10.0%) decreasing to 4.5%) |
|---|---|--|--|
| Net OPEB liability of the Road Commission | \$ 917,541 | \$ 1,207,669 | \$ 1,539,494 |

OPEB Plan Fiduciary Net Position

Detailed information about the plan's fiduciary net position is available in the separately issued financial report. For the purpose of measuring the net OPEB liability, deferred outflows of resources and deferred inflows of resources related to OPEB, and OPEB expense, information about the plan's fiduciary net position and additions to/deductions from fiduciary net position have been determined on the same basis as they are reported by the plan. The plan uses the economic resources measurement focus and the full accrual basis of accounting. Investments are stated at fair value. Contribution revenue is recorded as contributions are due, pursuant to legal requirements. Benefit payments and refunds of employee contributions are recognized as expense when due and payable in accordance with the benefit terms.

Note 9 - Risk Management

The Road Commission is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The Road Commission participates in the Michigan County Road Commission Self-insurance Pool (MCRCSIP) for claims relating to property loss, torts, errors, and omissions. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three fiscal years.

MCRCSIP operates as a common risk-sharing management program for road commissions in Michigan; member premiums are used to purchase commercial excess insurance coverage and to pay member claims in excess of deductible amounts.

The Road Commission is a member of the County Road Association Self-insurance Fund (CRASIF) for workers' compensation claims. Member premiums are used to purchase workers' compensation insurance. As a member of CRASIF, the Road Commission is fully insured for workers' compensation claims incurred.

The Road Commission continues to carry commercial insurance for other risks of loss, including employee health and accident insurance.

The Road Commission offers a high-deductible health insurance plan with a Health Reimbursement Account (HRA). The HRA reimburses a certain level of medical expenses not covered by the high-deductible plan. The Road Commission is responsible for expenses up to the specified HRA plan limits.

Required Supplemental Information

Road Commission of Kalamazoo County

Required Supplemental Information Budgetary Comparison Schedule Road Fund

Year Ended December 31, 2018

| | Original Budget | Final Budget | Actual | Over (Under) Final Budget |
|---|---------------------|----------------------|----------------------|------------------------------|
| Revenue | | | | |
| Michigan Transportation Funds: | | | | |
| Primary Road Fund | \$ 14,896,000 | \$ 15,200,000 | \$ 14,610,994 | \$ (589,006) |
| Local Road Fund | 4,704,000 | 4,800,000 | 4,725,653 | (74,347) |
| Federal, state, and enhancement | 1,949,000 | 1,471,000 | 1,181,176 | (289,824) |
| State general fund: | | | | |
| PA 207 of 2018 | - | 2,980,800 | 2,741,670 | (239,130) |
| PA 82 of 2018 | - | 1,455,000 | 1,455,227 | 227 |
| Township projects | 4,912,000 | 4,367,000 | 4,283,164 | (83,836) |
| Township special assessments | 15,000 | 14,000 | 14,535 | 535 |
| Cities and other governmental | 10,000 | 90,000 | 92,220 | 2,220 |
| Interest | 12,000 | 104,000 | 109,946 | 5,946 |
| Other | 250,000 | 330,000 | 453,458 | 123,458 |
| Total revenue | 26,748,000 | 30,811,800 | 29,668,043 | (1,143,757) |
| Expenditures | | | | |
| Preservation and structural improvements: | | | | |
| Primary road system | 8,782,500 | 9,550,000 | 9,060,197 | 489,803 |
| Local road system | 6,485,000 | 6,526,000 | 6,580,768 | (54,768) |
| Routine and preventive maintenance: | | | | |
| Primary road system | 5,891,000 | 5,797,000 | 5,397,675 | 399,325 |
| Local road system | 3,772,000 | 4,403,000 | 4,172,915 | 230,085 |
| Administrative | 1,302,000 | 1,307,000 | 1,255,683 | 51,317 |
| Less equipment rental and other charges to other expenditures | (931,500) | (729,000) | (825,310) | 96,310 |
| Capital outlay - Net | 1,348,500 | 1,151,000 | 1,060,781 | 90,219 |
| Work performed for other governmental units | 227,000 | 95,000 | 111,337 | (16,337) |
| Total expenditures | 26,876,500 | 28,100,000 | 26,814,046 | 1,285,954 |
| Net Change in Fund Balance | (128,500) | 2,711,800 | 2,853,997 | 142,197 |
| Fund Balance - Beginning of year | 9,050,042 | 9,050,042 | 9,050,042 | - |
| Fund Balance - End of year | \$ 8,921,542 | \$ 11,761,842 | \$ 11,904,039 | \$ 142,197 |

Road Commission of Kalamazoo County

Required Supplemental Information
 Schedule of the Road Commission's Proportionate Share of the Net Pension Liability
 Kalamazoo County Employees' Retirement Plan

| | Last Five Fiscal Years | | | | |
|---|-------------------------------------|--------------|--------------|--------------|--------------|
| | Plan Years Ended December 31 | | | | |
| | <u>2018</u> | <u>2017</u> | <u>2016</u> | <u>2015</u> | <u>2014</u> |
| Road Commission's proportion of the net pension asset | 7.14700 % | 6.91000 % | 7.06200 % | 7.20000 % | - % |
| Road Commission's proportionate share of the net pension asset | \$ 951,766 | \$ 3,583,731 | \$ 2,542,616 | \$ 1,875,773 | - |
| Road Commission's covered payroll | \$ 2,897,844 | \$ 2,700,098 | \$ 2,459,213 | \$ 2,137,399 | \$ 2,074,153 |
| Road Commission's proportionate share of the net pension asset as a percentage of its covered payroll | 32.84 % | 132.73 % | 103.39 % | 87.76 % | - % |
| Plan fiduciary net position as a percentage of total pension liability | 106.99 % | 129.41 % | 121.00 % | 115.70 % | - % |

*Note: GASB No. 68 was implemented in 2015. This schedule is being built prospectively. Ultimately, 10 years of data will be presented.

Road Commission of Kalamazoo County

Required Supplemental Information
Schedule of Pension Contributions
Kalamazoo County Employees' Retirement Plan

**Last Ten Fiscal Years
Years Ended December 31**

| | 2018 | 2017 | 2016 | 2015 | 2014 | 2013 | 2012 | 2011 | 2010 | 2009 |
|--|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Contractually required contribution | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - |
| Contributions in relation to the contractually required contribution | - | - | - | - | - | - | - | - | - | - |
| Contribution Deficiency | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - | \$ - |
| Road Commission's Covered Payroll | \$ 2,897,844 | \$ 2,700,098 | \$ 2,459,213 | \$ 2,137,399 | \$ 2,074,153 | \$ 2,222,722 | \$ 2,379,843 | \$ 2,699,115 | \$ 2,747,330 | \$ 2,842,241 |
| Contributions as a Percentage of Covered Payroll | - % | - % | - % | - % | - % | - % | - % | - % | - % | - % |

*Historically, contributions have not been required due to the Road Commission's portion of the Plan being overfunded.

Road Commission of Kalamazoo County

Required Supplemental Information
Schedule of the Road Commission's Proportionate Share of the
Net OPEB Liability
Kalamazoo County Retiree Medical Benefits Plan

| | Last Two Fiscal Years | |
|--|-------------------------------------|--------------|
| | Plan Years Ended December 31 | |
| | <u>2018</u> | <u>2017</u> |
| Road Commission's proportion of the net OPEB liability | 2.90300 % | 3.05700 % |
| Road Commission's proportionate share of the net OPEB liability | \$ 1,207,669 | \$ 1,406,706 |
| Road Commission's covered payroll | \$ 1,663,500 | \$ 1,921,362 |
| Road Commission's proportionate share of the net OPEB liability as a percentage of its covered payroll | 72.60 % | 73.21 % |
| Plan fiduciary net position as a percentage of total OPEB liability | 31.39 % | 58.68 % |

*Note: GASB No. 75 was implemented in 2017. This schedule is being built prospectively. Ultimately, 10 years of data will be presented.

Road Commission of Kalamazoo County

Required Supplemental Information Schedule of OPEB Contributions

Last Ten Fiscal Years Years Ended December 31

| | 2018 | 2017 | 2016 | 2015 | 2014 | 2013 | 2012 | 2011 | 2010 | 2009 |
|--|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Actuarially determined contribution | \$ 125,066 | \$ 179,423 | \$ 181,088 | \$ 182,295 | \$ 182,851 | \$ 222,630 | \$ 217,684 | \$ 306,789 | \$ 293,578 | \$ 345,825 |
| Contributions in relation to the actuarially determined contribution | 211,297 | 297,957 | 241,142 | 215,529 | 175,031 | 169,453 | 178,064 | 237,476 | 267,258 | 313,676 |
| Contribution Excess (Deficiency) | \$ 86,231 | \$ 118,534 | \$ 60,054 | \$ 33,234 | \$ (7,820) | \$ (53,177) | \$ (39,620) | \$ (69,313) | \$ (26,320) | \$ (32,149) |
| Covered Payroll | \$ 1,663,500 | \$ 1,921,362 | \$ 1,883,924 | \$ 1,702,440 | \$ 1,880,109 | \$ 2,200,685 | \$ 2,285,799 | \$ 2,403,603 | \$ 2,705,045 | \$ 2,950,857 |
| Contributions as a Percentage of Covered Payroll | 12.70 % | 15.51 % | 12.80 % | 12.66 % | 9.31 % | 7.70 % | 7.79 % | 9.88 % | 9.88 % | 10.63 % |

Notes to Schedule of Contributions

Actuarial valuation information relative to the determination of contributions:

Valuation date Actuarially determined contribution rates are calculated as of December 31, which is 24 months prior to the beginning of the fiscal year in which contributions are reported.

Methods and assumptions used to determine contribution rates:

| | |
|-------------------------------|---|
| Actuarial cost method | Entry age normal |
| Amortization method | Level dollar, closed period |
| Remaining amortization period | 26 years |
| Asset valuation method | Market value assets |
| Inflation | 3.5 percent |
| Healthcare cost trend rates | Initial trend of 9.00 percent gradually decreasing to 3.50 percent |
| Salary increase | 3.50 to 7.23 percent |
| Investment rate of return | 7.50 percent, net of OPEB plan investment expenses |
| Excise tax | No load was applied in connection with the "Cadillac" tax. |
| Mortality | RP-2000 mortality combined healthy tables, projected 20 years with U.S. Projection Scale BB |
| Aging factors | Based on an internal actuary study using several pricing manuals from National Health Care Consultant Groups and incorporating analysis and data from a Society of Actuaries survey regarding aging practices used in healthcare valuations |

Road Commission of Kalamazoo County

Note to Required Supplemental Information

December 31, 2018

Budgetary Information

The budgetary comparison schedule for the Road Fund is presented on the same basis of accounting used in preparing the adopted budget. The following is a reconciliation of the budgetary comparison schedule to the Road Fund (statement of governmental fund revenue, expenditures, and changes in fund balance):

| | <u>Total Revenue</u> | <u>Total Expenditures</u> |
|---|--------------------------|-------------------------------|
| Amounts per operating statement | \$ 29,675,069 | \$ 26,821,072 |
| Specific revenue accounts budgeted for against expenditures | <u>(7,026)</u> | <u>(7,026)</u> |
| Amounts per budget statement | <u>\$ 29,668,043</u> | <u>\$ 26,814,046</u> |

During the year, the Road Commission of Kalamazoo County incurred significant expenditures that were in excess of the amounts budgeted, as follows:

| | <u>Budget</u> | <u>Actual</u> | <u>Variance</u> |
|--|---------------|---------------|-----------------|
| Preservation and structural improvements - Local road system | \$ 6,526,000 | \$ 6,580,768 | \$ (54,768) |
| Work performed for others | 95,000 | 111,337 | (16,337) |

Other Supplemental Information

Road Commission of Kalamazoo County

Other Supplemental Information Analysis of Changes in Road Fund Balances

Year Ended December 31, 2018

| | Primary Road | Local Road | County Road Commission | Total Road Fund |
|---|---------------------|--------------------|---------------------------|----------------------|
| Revenue | | | | |
| Michigan Transportation Fund: | | | | |
| Engineering | \$ 7,542 | \$ 2,458 | \$ - | \$ 10,000 |
| Snow removal | 1,537 | 2,827 | - | 4,364 |
| Urban road | 2,512,697 | 780,958 | - | 3,293,655 |
| Allocation | 12,089,218 | 3,939,410 | - | 16,028,628 |
| Other governmental funding: | | | | |
| Federal sources | 1,098,028 | - | - | 1,098,028 |
| Other state sources: | | | | |
| General state aid | 3,165,140 | 1,031,757 | - | 4,196,897 |
| Local bridge | 3,492 | - | - | 3,492 |
| Economic Development Fund | 79,656 | - | - | 79,656 |
| Township and other governmental contributions | 3,090 | 4,288,850 | 77,943 | 4,369,883 |
| Charges for services - Other contributions and charges for services | 179,392 | 34,830 | 142,606 | 356,828 |
| Licenses and permits - Other licenses and permits | 10,889 | 22,441 | - | 33,330 |
| Other: | | | | |
| Other | - | - | (2,894) | (2,894) |
| Interest earned | 77,741 | 1,636 | 30,569 | 109,946 |
| Special assessments | - | 14,535 | - | 14,535 |
| Gain on equipment disposals | 15,396 | - | 56,299 | 71,695 |
| Total revenue | 19,243,818 | 10,119,702 | 304,523 | 29,668,043 |
| Expenditures | | | | |
| Preservation and structural improvements: | | | | |
| Primary road system | 9,052,103 | - | - | 9,052,103 |
| Local road system | - | 5,087,153 | - | 5,087,153 |
| Routine and preventive maintenance: | | | | |
| Primary road system | 5,405,769 | - | - | 5,405,769 |
| Local road system | - | 5,666,531 | - | 5,666,531 |
| Administrative | 720,087 | 535,596 | - | 1,255,683 |
| Equipment - Net | 149,303 | 176,305 | 24,148 | 349,756 |
| Capital outlay - Net | (265,761) | - | 151,475 | (114,286) |
| Work performed for other governmental units | - | - | 111,337 | 111,337 |
| Total expenditures | 15,061,501 | 11,465,585 | 286,960 | 26,814,046 |
| Excess of Revenue Over (Under) Expenditures | 4,182,317 | (1,345,883) | 17,563 | 2,853,997 |
| Optional Transfers | (1,345,883) | 1,345,883 | - | - |
| Net Change in Fund Balances | 2,836,434 | - | 17,563 | 2,853,997 |
| Fund Balances - Beginning of year | 6,495,808 | - | 2,554,234 | 9,050,042 |
| Fund Balances - End of year | \$ 9,332,242 | \$ - | \$ 2,571,797 | \$ 11,904,039 |

Road Commission of Kalamazoo County

Note to Other Supplemental Information

December 31, 2018

A reconciliation of the analysis of changes in Road Fund balances to the statement of governmental fund revenue, expenditures, and changes in fund balance is as follows:

| | <u>Total Revenue</u> | <u>Total Expenditures</u> |
|--|--------------------------|-------------------------------|
| Amounts per operating statement | \$ 29,675,069 | \$ 26,821,072 |
| Specific revenue accounts applied against expenditures | <u>(7,026)</u> | <u>(7,026)</u> |
| Amounts per analysis of changes in Road Fund balances | <u>\$ 29,668,043</u> | <u>\$ 26,814,046</u> |