

**SAN JOSE – SANTA CLARA  
CLEAN WATER FINANCING AUTHORITY**  
(A Component Unit of the  
City of San José, California)

Independent Auditor's Reports,  
Management's Discussion and Analysis,  
and Basic Financial Statements

For the Year Ended June 30, 2019



Certified  
Public  
Accountants

**SAN JOSE – SANTA CLARA  
CLEAN WATER FINANCING AUTHORITY**  
(A Component Unit of the City of San José, California)  
For the Year Ended June 30, 2019

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## Independent Auditor's Report

The Board of Directors  
San José – Santa Clara Clean Water Financing Authority  
San José, California

### Report on the Financial Statements

We have audited the accompanying financial statements of the San José – Santa Clara Clean Water Financing Authority (the Authority), a component unit of the City of San José (the City), California, as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

### *Management's Responsibility for the Financial Statements*

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

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 opinion.

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of June 30, 2019, and the changes in its financial position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

***Other Matters***

***Required Supplementary Information***

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

***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated October 25, 2019, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Authority's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.



Walnut Creek, California  
October 25, 2019

**SAN JOSE - SANTA CLARA**  
**CLEAN WATER FINANCING AUTHORITY**  
Management's Discussion and Analysis (Unaudited)  
For the Year Ended June 30, 2019

The following discussion and analysis of the San José - Santa Clara Clean Water Financing Authority's (the Authority) financial performance provides an overview of its financial activities for the year ended June 30, 2019. The City of San José's Finance Department prepared this discussion and analysis. Please read it in conjunction with the Authority's basic financial statements, which begin on page 5. Responsibility for both the accuracy of the data, and the completeness and fairness of the presentation, including all disclosures, rest solely with management of the Authority. To the best of our actual knowledge and belief, the basic financial statements, as presented, are accurate in all material respects.

***Financial Statements***

The Authority's financial statements are those of a special-purpose government engaged only in providing debt financing for the acquisition and construction of additions and improvements to the existing wastewater treatment plant and related facilities, known as the San José - Santa Clara Water Pollution Control Plant (the Plant). Under Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, public entities like the Authority that have only business-type activities may present only enterprise fund financial statements as follows: (1) statement of net position (deficit); (2) statement of revenues, expenses, and changes in net position; (3) statement of cash flows; and (4) notes to basic financial statements.

The Authority's basic financial statements are prepared on an accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (GAAP). The Authority is reported as a single enterprise fund.

The following table indicates the net position at June 30, 2019 and 2018:

	<u>2019</u>	<u>2018</u>	<u>Dollar Change</u>
Assets	\$ 5,548,860	\$ 5,387,826	\$ 161,034
Current liabilities	5,358,681	5,170,403	188,278
Noncurrent liabilities	<u>7,596,142</u>	<u>12,895,851</u>	<u>(5,299,709)</u>
Total liabilities	<u>12,954,823</u>	<u>18,066,254</u>	<u>(5,111,431)</u>
Net deficit	<u>\$ (7,405,963)</u>	<u>\$ (12,678,428)</u>	<u>\$ 5,272,465</u>

**Statement of Net Deficit**

Total liabilities decreased by \$5.1 million for the year ended June 30, 2019. The decrease is primarily the result of the Authority's scheduled bond principal payment of \$5.0 million.

**SAN JOSE - SANTA CLARA  
CLEAN WATER FINANCING AUTHORITY**  
Management's Discussion and Analysis (Unaudited)  
For the Year Ended June 30, 2019

The Authority's net position at June 30, 2019 was a deficit of \$7.4 million. The Authority has issued debt for the acquisition and construction of additions and improvements to the Plant. The Authority does not have title to the Plant land or any capital improvements to the Plant, and capital assets acquired under the Joint Exercise of Powers Agreement (the CWFA Agreement) are conveyed to the City of San José and the City of Santa Clara (Cities) in accordance with the provisions of the CWFA Agreement. Since assets are conveyed to the Cities while the debt remains on the Authority's books, the Authority has a net deficit at June 30, 2019, which is expected to be eliminated in future years through the receipt of base payments and additional payments from the City of San José.

The following table indicates the changes in net deficit for the years ended June 30, 2019 and 2018

	2019	2018	Dollar Change
Operating revenues	\$ 5,638,190	\$ 5,749,461	\$ (111,271)
Operating expenses	(2,650)	(1,750)	(900)
Operating income	5,635,540	5,747,711	(112,171)
Nonoperating revenues (expenses):			
Investment income	49,156	25,680	23,476
Bond interest expense	(412,231)	(588,369)	176,138
Total nonoperating expenses, net	(363,075)	(562,689)	199,614
Change in net position	5,272,465	5,185,022	87,443
Net deficit, beginning of year	(12,678,428)	(17,863,450)	5,185,022
Net deficit, end of year	\$ (7,405,963)	\$ (12,678,428)	\$ 5,272,465

**Statement of Revenues, Expenses, and Changes in Net Deficit**

The Statement of Revenues, Expenses, and Changes in Net Deficit identified various revenue and expense items, which impact the change in net position. The Authority's operating revenues were comprised of base payments and additional payments to the Authority from Net System Revenues of the sewer system operated by the City of San José for principal and interest on the Authority's outstanding bonds. Operating expenses were comprised of administrative expenses including trustee charges.

***Long-Term Debt***

Long-term debt of the Authority was \$10.8 million, which was comprised of \$10.6 million of outstanding principal and \$0.2 million of unamortized premium. During the year ended June 30, 2019, the Authority made a scheduled bond principal payment of \$5.0 million on the Series 2009A sewer revenue refunding bonds. Additional information in the Authority's long-term debt can be found in Note 5 to the basic financial statements.

***Request for Information***

Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Director of Finance, 200 E. Santa Clara Street, San José, CA 95113.

**SAN JOSE - SANTA CLARA**  
**CLEAN WATER FINANCING AUTHORITY**  
(A Component Unit of the City of San José, California)  
Statement of Net Deficit  
June 30, 2019

Assets

Current assets:

Restricted cash and cash equivalents (Note 4)	\$ 2,255,513
Base payment receivable	<u>3,293,347</u>
Total assets	<u>5,548,860</u>

Liabilities

Current liabilities:

Bond interest payable	58,972
Bonds payable - current, net (Note 5)	<u>5,299,709</u>
Total current liabilities	<u>5,358,681</u>

Noncurrent liabilities:

Advance from the City of San José (Note 6)	2,139,375
Bonds payable - noncurrent, net (Note 5)	<u>5,456,767</u>
Total noncurrent liabilities	<u>7,596,142</u>

Total liabilities	<u>12,954,823</u>
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Net deficit

Unrestricted deficit	<u><u>\$ (7,405,963)</u></u>
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See accompanying notes to basic financial statements.

**SAN JOSE - SANTA CLARA**  
**CLEAN WATER FINANCING AUTHORITY**  
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Statement of Revenues, Expenses, and Changes in Net Deficit  
For the Year Ended June 30, 2019

Operating revenues:	
Base payments from the City of San José	\$ 5,633,190
Additional payments from the City of San José	<u>5,000</u>
Total operating revenues	<u>5,638,190</u>
Operating expenses:	
Administrative and other costs	<u>2,650</u>
Operating income	<u>5,635,540</u>
Nonoperating revenues (expenses):	
Investment income	49,156
Bond interest expense	<u>(412,231)</u>
Total nonoperating expenses, net	<u>(363,075)</u>
Change in net deficit	<u>5,272,465</u>
Net deficit, beginning of year	<u>(12,678,428)</u>
Net deficit, end of year	<u><u>\$ (7,405,963)</u></u>

See accompanying notes to basic financial statements.



**SAN JOSE - SANTA CLARA**  
**CLEAN WATER FINANCING AUTHORITY**  
(A Component Unit of the City of San José, California)  
Statement of Cash Flows  
For the Year Ended June 30, 2019

Cash flows from operating activities:	
Cash received from the City of San José, principal portion	\$ 4,965,000
Cash received from the City of San José, interest portion	558,662
Cash received for general expenses	5,000
Cash payments for general expenses	<u>(2,650)</u>
Net cash provided by operating activities	<u>5,526,012</u>
Cash flows from noncapital financing activities:	
Cash paid for principal on bonds	(4,965,000)
Cash paid for interest on bonds	<u>(558,662)</u>
Net cash used in noncapital financing activities	<u>(5,523,662)</u>
Cash flows from investing activities:	
Investment earnings received	<u>49,156</u>
Net change in cash and cash equivalents	51,506
Cash and cash equivalents:	
Beginning of year	<u>2,204,007</u>
End of year	<u>\$ 2,255,513</u>
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ 5,635,540
Adjustments to reconcile operating income to net cash provided by operating activities:	
Decrease in base payment receivable	(109,528)
Net cash provided by operating activities	<u>\$ 5,526,012</u>
Noncash noncapital financing and investing activities:	
Amortization of bond premium	\$ 124,709

See accompanying notes to basic financial statements.

**SAN JOSE – SANTA CLARA  
CLEAN WATER FINANCING AUTHORITY**  
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Notes to Basic Financial Statements  
For the Year Ended June 30, 2019

**NOTE 1 – REPORTING ENTITY**

The San José - Santa Clara Clean Water Financing Authority (the Authority), a component unit of the City of San José, California, was created pursuant to the Joint Exercise of Powers Agreement (the CWFA Agreement) on March 1, 1981, as amended, between the City of San José and the City of Santa Clara (the Cities) to operate and finance the acquisition and construction of additions and improvements to the existing wastewater treatment plant and related facilities, known as the San José - Santa Clara Water Pollution Control Plant (the Plant).

The Authority and the Cities entered into an Improvement Agreement on July 1, 1982, as amended, under which Base Payments are made by the City of San José from Net System Revenues of the sewer system operated by San José. Such payments have been adjusted under the amendments to be at least equal to 1.15 times the annual debt service required by Sewer Revenue Bonds issued through the Authority, and are solely secured by a pledge of the sewer system's Net System Revenues.

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

***Basis of Presentation***

The fiscal agent, as trustee for the bondholders, is required to maintain separate funds for specified activities. The accompanying financial statements reflect the transactions executed by the fiscal agent and the Authority for financing activities and are presented in accordance with accounting principles generally accepted in the United States (GAAP).

***Basis of Accounting***

The accounts of the Authority are organized on the basis of a proprietary fund type, specifically an enterprise fund. The activities of this fund are accounted for with a separate set of self-balancing accounts that comprise the Authority's assets, deferred outflows of resources, liabilities, deferred inflows of resources, net position (deficit), revenues, and expenses. Enterprise funds are used to account for activities that are financed with debt that is secured solely by a pledge of the net revenues from fees and charges for the activities.

The accounting and financial reporting treatment applied to the Authority is determined by its measurement focus. The transactions of the Authority are accounted for using the flow of economic resources measurement focus. With this measurement focus, all assets, deferred outflows of resources, liabilities, and deferred inflows of resources associated with the operations are included on the statement of net position (deficit). Revenues are recorded when earned, and expenses are recorded when the related liabilities are incurred.

Enterprise funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services in connection with the fund's principal ongoing operations. The principal operating revenue of the Authority is Base Payments from the City of San José. Operating expenses for the Authority include administrative and other costs. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2019

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

The City of San José, as the administering agent of the Authority, has established certain funds to account for its sewer collections and plant operations, which are integral to the Authority, including the South Bay Water Recycling Fund, which was established to account for construction activity partially financed through the Authority, and the Clean Water Financing Authority Payment Fund, which is used to collect funds to be transferred to the Authority as Base Payments.

***Restricted Cash and Cash Equivalents***

Cash and cash equivalents are restricted and held by a fiscal agent. Investments are accounted for in accordance with the provisions of GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools* and GASB Statement No. 72, *Fair Value Measurement and Application*, which requires governmental entities to report certain investments at fair value and recognize the corresponding change in fair value of investments in the year in which the change occurred. The Authority reports its investments at fair value. The fair value is based on quoted market information obtained from the fiscal agent or other sources.

For purposes of the accompanying statement of cash flows, the Authority considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

***Donated Services***

As the agent for the Authority, the City of San José incurs certain administrative costs on behalf of the Authority. The City of San José has not charged the Authority for any of these costs incurred through June 30, 2019. Any such charges would be substantially offset by Additional Payments for administrative costs by the City of San José under the Improvement Agreement. The net effect of the donated services is not material and has not been reflected in the accompanying basic financial statements.

***Original Issue Premiums and Loss on Refunding of Debt***

Original issue premiums are amortized using the straight-line method over the life of the bonds. Bonds payable are reported net of the applicable bond premium. Loss on refunding of debt are reported as deferred outflows of resources and amortized over the shorter of the life of the refunded debt or refunding debt. Amortization of these balances is reported as a component of interest expense. There are no loss on refunding of debt for the fiscal year ended June 30, 2019.

***Prepaid Insurance Costs***

Prepaid insurance costs are amortized using the straight-line method over the life of the bonds. Amortization of these balances is reported as a component of operating expenses. There are no prepaid insurance costs for the fiscal year ended June 30, 2019.

**SAN JOSE – SANTA CLARA**  
**CLEAN WATER FINANCING AUTHORITY**  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2019

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

*Capital Assets*

The Authority does not have title to the Plant land or any capital improvements to the Plant, and capital assets acquired under the CWFA agreement are conveyed to the Cities in accordance with the provisions of the CWFA Agreement.

*Use of Estimates*

The preparation of basic financial statements in conformity with U.S. GAAP requires management to make certain estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results may differ from those estimates.

*Effects of New Accounting Pronouncement*

During the year ended June 30, 2019, the Authority implemented Governmental Accounting Standards Board Statement No. 88, Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements. The objective of this statement is to improve the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. It also clarifies which liabilities governments should include when disclosing information related to debt. Implementation of this statement did not have a significant impact on the Authority's financial statements for the year ended June 30, 2019.

**NOTE 3 – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY**

At June 30, 2019, the Authority has a net deficit of \$7,405,963, which is expected to be eliminated in future years through the receipt of Base Payments from the City of San José.

**SAN JOSE – SANTA CLARA  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2019

**NOTE 4 – RESTRICTED CASH AND CASH EQUIVALENTS**

Certain bond resolutions require that amounts be held by a fiscal agent (a trust department of a qualifying financial institution) as trustee for the bondholders. The Authority's bond indenture authorizes the Authority to invest in the following, under applicable State of California laws (including the San José Investment Policy):

<u>Authorized Investment Type</u>	<u>Maximum Maturity</u>	<u>Credit Rating Limits</u>
Federal securities	None	None
Federal agencies and instrumentalities	None	None
Securities or receipts evidencing ownership interest in obligations or specified portions of federal obligations	None	None
Obligations of any state or territory of the United States or any agency or political subdivisions thereof	None	At least as high as each series of the Authority's bonds
Time certificates of deposit	None	Aa or AA for the issuers
Repurchase agreements	None	None
Investment agreements	None	None
State of California Local Agency Investment Fund	None	None
Government money market portfolios or money market funds restricted to obligations issued or guaranteed by the United States	None	Aa or AA
City of San José Investment Portfolio	None	None
Other investments consistent with the City of San José's Investment Policy	None	None

**Interest Rate Risk** – Pursuant to the Authority's bond indenture, investments shall mature not later than such times as necessary to provide money when reasonably expected to be needed for payments. At June 30, 2019, the Authority invested \$2,255,513 in JP Morgan 100% U.S. Treasury money market funds with a weighted average maturity of 33 days.

**Credit Risk** – The Authority's investment in money market fund is rated Aaa-mf by Moody's Investors Service and AAAM by Standard & Poor's.

**Fair Value Hierarchy**

The Authority 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 assets. Level 1 inputs are quoted prices in an active market for identical assets; Level 2 input are significant other observable inputs; and Level 3 inputs are significant unobservable inputs. The inputs and techniques used for valuing securities are not necessarily an indication of risk associated with investing in those securities. The Authority's investment in JP Morgan 100% U.S. Treasury money market funds are measured using level 1 inputs.

**SAN JOSE – SANTA CLARA  
CLEAN WATER FINANCING AUTHORITY**  
(A Component Unit of the City of San José, California)  
Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2019

**NOTE 5 - BONDS PAYABLE**

*Series 2009A Bonds*

On January 29, 2009, the Authority issued \$21,420,000 of Series 2009A sewer revenue refunding bonds with fixed interest rates ranging from 3.00% to 5.00% maturing from November 15, 2016 through November 15, 2020. The proceeds of the Series 2009A bonds were used to refund the Authority's Series 2005B variable rate sewer revenue refunding bonds, which were used to refund the Authority's Series 1995B sewer revenue bonds. The 1995 Bonds were issued to pay for a project to recycle treated wastewater from the San José - Santa Clara Water Pollution Control Plant for irrigation and industrial uses in San José, Santa Clara and Milpitas. Debt service is payable from the Authority's revenue, which consists of payments to the Authority from Net System Revenues of the sewer system operated by the City of San José.

Changes in long-term debt during the year ended June 30, 2019, were as follows:

	Balance June 30, 2018	Retirements	Balance June 30, 2019	Balance due within one year
Sewer Revenue Bonds				
2009 Series A	\$ 15,550,000	\$ (4,965,000)	\$ 10,585,000	\$ 5,175,000
Unamortized Premium	296,185	(124,709)	171,476	124,709
Total	<u>\$ 15,846,185</u>	<u>\$ (5,089,709)</u>	<u>\$ 10,756,476</u>	<u>\$ 5,299,709</u>

Annual future bond principal and interest repayments as of June 30, 2019, are as follows:

Year Ending June 30,	Principal	Interest	Total
2020	\$ 5,175,000	\$ 352,087	\$ 5,527,087
2021	5,410,000	116,200	5,526,200
Total	<u>\$ 10,585,000</u>	<u>\$ 468,287</u>	<u>\$ 11,053,287</u>

*Revenues Pledged for Future Debt Service*

The City of San José has pledged, as security for bonds issued by the Authority, a portion of the Net System Revenues of the sewer system operated by the City of San José that is restricted for purposes of irrigation and industrial uses in San José, Santa Clara, and Milpitas in the recycle treated wastewater from the San José - Santa Clara Water Pollution Control Plant. The bonds issued by the Authority in 2009 in the amount of \$21,420,000, to provide financing for various

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**CLEAN WATER FINANCING AUTHORITY**  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2019

**NOTE 5 - BONDS PAYABLE (Continued)**

capital projects of the Authority, are payable through 2021. The City of San José has committed to appropriate each year, from the Net System Revenues, amounts sufficient to cover the principal and interest requirements on the Authority's debt. The Authority has pledged, as the sole security for the bonds, the annual appropriations from the City of San José. Total principal and interest remaining on the debt is \$11,053,287 with annual requirements of \$5,526,200 and \$5,527,087 through 2021. For the year ended June 30, 2019, debt services paid by the Authority and the Base Payments made from City of San José Net System Revenues is \$5,523,662.

***Events of Default and Acceleration Clauses***

The Authority has one series of bonds outstanding as of June 30, 2019, the Series 2009A Bonds. The Authority issued the Series 2009A Bonds pursuant to a Master Indenture as supplemented and amended ("Master Indenture") with a trustee bank ("Trustee"). The source of repayment of the Series 2009A Bonds consists of Revenues (defined below) paid under the Improvement Agreement by and among the City, the City of Santa Clara and the Authority as supplemented and amended ("Improvement Agreement). For purposes of the Series 2009A Bonds, Revenues consist of payments made under the Improvement Agreement solely by the City from Net System Revenues (as defined in the Improvement Agreement) derived from the operation of the City's sewer and wastewater treatment system.

There are events of default under both the Master Indenture and the Improvement Agreement. Generally, the events of default under the Master Indenture are: (i) failure to pay debt service when due; (ii) failure to comply with covenants and conditions of the Master Indenture and such default shall have continued for a specified period of days following the Authority's receipt from the Trustee, or the owners of at least 10% of the aggregate principal amount of the Series 2009A Bonds outstanding, of written notice of the occurrence of such default, provided that such period may be extended as specified in the Master Indenture; (iii) bankruptcy or similar debtor relief proceedings; or (iv) an event of default by the City under the Improvement Agreement. The Master Indenture does not provide for acceleration of payment of the Series 2009A Bonds. The Master Indenture, however, provides for application of Revenues upon an event of default in the order of priority set forth in the Master Indenture.

Generally, the events of default under the Improvement Agreement are: (i) failure to make a payment when due; (ii) failure to comply with covenants and conditions of the Improvement Agreement and such default shall have continued for a period of 30 days following the City's receipt of written notice of the occurrence of such default from the Authority, provided that such period may be extended as specified in the Improvement Agreement; or (iii) bankruptcy or similar debtor relief proceedings. Following an event of default under the Improvement Agreement, the Authority or the Trustee may pursue its rights and remedies at law or in equity. With respect to payment defaults, the Trustee may demand payment of amounts past due with interest, to the extent permitted by law, at the effective rate of interest on the Series 2009A Bonds until such amount has been paid.

Document Summaries. All summaries of documents contained in the notes to the financial statements are made subject to the provisions of such documents and do not purport to be complete

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**CLEAN WATER FINANCING AUTHORITY**  
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Notes to Basic Financial Statements (Continued)  
For the Year Ended June 30, 2019

**NOTE 5 - BONDS PAYABLE (Continued)**

statements of any or all such provisions. Each reference is qualified in its entirety by reference to such document, which is on file with or may be obtained from the City's Director of Finance.

**NOTE 6 – ADVANCE FROM THE CITY OF SAN JOSE**

During the year ended June 30, 2017, the City of San José's Wastewater Treatment System enterprise fund advanced \$2,139,375 to the Authority. The Authority deposited the funds received into the 2009A Bonds reserve accounts in order to satisfy the Debt Service Reserve Requirement pursuant to the bond indenture. The advance bears no interest and will be repaid to the City of San José when the Debt Service Reserve Requirement is met through the surety policy issued by Financial Security Assurance, Inc. or when no bonds remain outstanding. At June 30, 2019, the balance of the advance from the City of San José is \$2,139,375.





**Independent Auditor’s Report on Internal Control Over Financial Reporting and on  
Compliance and Other Matters Based on an Audit of Financial Statements  
Performed in Accordance with *Government Auditing Standards***

The Board of Directors  
San José – Santa Clara Clean Water Financing Authority  
San José, California

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the San José – Santa Clara Clean Water Financing Authority (the Authority), a component unit of the City of San José (the City), California, as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the Authority’s basic financial statements, and have issued our report thereon dated October 25, 2019.

***Internal Control Over Financial Reporting***

In planning and performing our audit of the financial statements, we considered the Authority’s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority’s internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority’s internal control.

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

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

***Compliance and Other Matters***

As part of obtaining reasonable assurance about whether the Authority’s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express

such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

***Purpose of this Report***

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

*Macias Gini & O'Connell LLP*

Walnut Creek, California  
October 25, 2019