



**Special District Reinsurance Group  
Annual Financial Report  
For the Fiscal Year Ended June 30, 2023  
(With Comparative Amounts for June 30, 2022)**

**NIGRO & NIGRO<sup>PC</sup>**

**SPECIAL DISTRICT REINSURANCE GROUP**

*Board of Directors*

*As of June 30, 2023*

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**PRESIDENT**

**Brian Kelley, MBA, ARM**  
Chief Executive Officer, SDRMA

**CHAIRMAN**

**Mike Scheafer**  
Costa Mesa Sanitary District

**VICE-CHAIRMAN**

**Robert Swan**  
Groveland Community Services District

**SECRETARY**

**Brent Andrewsen**  
Holland & Hart, LLP

**TREASURER**

**Timothy Unruh, CSDM**  
Kern County Cemetery District #1

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**Matt Clutterbuck, CPA**  
Chief Financial Officer

**SPECIAL DISTRICT REINSURANCE GROUP**

*For the Fiscal Year Ended June 30, 2023*

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***Financial Section***

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## INDEPENDENT AUDITORS' REPORT

Board of Directors  
Special District Reinsurance Group  
Sacramento, California

### Opinion

We have audited the accompanying financial statements of the Special District Reinsurance Group (Captive) which comprise the balance sheet as of June 30, 2023, the related statements of revenue, expenses, and changes in net position, and cash flows for the year then ended, and related notes to the financial statements, as listed in the table of contents.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Captive as of June 30, 2023 and the changes in its financial position and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### Basis for Opinion

We conducted our audits 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. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report.

We are required to be independent of the Captive and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Captive's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

## **Auditor's Responsibilities for the Audit of the Financial Statements**

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Captive's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Captive's ability to continue as a going concern for a reasonable period of time.
- We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

## **Other Information**

Management is responsible for the other information included in the annual report. The other information comprises the claims development information but does not include the basic financial statements and our auditor's report thereon. Our opinions on the basic financial statements do not cover the other information, and we do not express an opinion or any form of assurance thereon.

In connection with our audit of the basic financial statements, our responsibility is to read the other information and consider whether a material inconsistency exists between the other information and the basic financial statements, or the other information otherwise appears to be materially misstated. If, based on the work performed, we conclude that an uncorrected material misstatement of the other information exists, we are required to describe it in our report.

### **Prior-Year Comparative Information**

The financial statements include partial prior-year comparative information. Such information does not include sufficient detail to constitute a presentation in accordance with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the District's financial statements for the year ended June 30, 2022, from which such partial information was derived.

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

In accordance with *Government Auditing Standards*, we have also issued a separate report dated November 30, 2023, on our consideration of the Captive'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 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 Captive'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 Captive's internal control over financial reporting and compliance.



Murrieta, California  
November 30, 2023

## **SPECIAL DISTRICT REINSURANCE GROUP**

### *Management's Discussion and Analysis (Unaudited) For the Fiscal Year Ended June 30, 2023*

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Management's Discussion and Analysis (MD&A) offers readers of Special District Reinsurance Group's financial statements a narrative overview of the Captive's financial activities for the fiscal years ended June 30, 2023. This MD&A presents financial highlights, an overview of the accompanying financial statements, an analysis of net position and results of operations, a current-to prior year analysis, a discussion on restrictions, commitments and limitations, and a discussion of significant activity involving capital assets and long-term debt. Please read in conjunction with the financial statements, which follow this section.

#### **FINANCIAL HIGHLIGHTS**

- The Captive's net position increased by 14.33% or \$1,018,701, from the prior year.
- The Captive had 2023 operating revenue of \$11,620,000 as compared to 2022 operating revenue of \$11,049,000 from increased member premium contributions in 2023.
- In fiscal year 2023, total expenses increased \$1,998,823 from \$10,631,170 in 2022 to \$12,629,993 in 2023 due primarily to an increase of \$1,955,089 in claims expenses.

#### **OVERVIEW OF THE FINANCIAL STATEMENTS**

This MD&A serves as an introduction to the Captive's financial statements. The Captive's basic financial statements reflect the combined results of the operating and capital programs and include four components: (1) Balance Sheet; (2) Statement of Revenues, Expenses and Changes in Net Position; (3) Statement of Cash Flows; and (4) Notes to the Financial Statements.

The financial statements accompanying this MD&A present the net position and results of operations during the fiscal year ending June 30, 2023. These financial statements have been prepared using the accrual basis of accounting, which is similar to the accounting basis used by for-profit entities. Each financial statement is identified and defined in this section, and analyzed in subsequent sections of this MD&A.

#### **REQUIRED FINANCIAL STATEMENTS**

##### **Balance Sheet**

The Balance Sheet presents information on the Captive's assets and liabilities the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Captive is improving or deteriorating. However, other factors such as changes in economic conditions, population growth, zoning, and new or changed legislation or regulations also need to be considered when evaluating financial position. Assets exceed liabilities, resulting in a net position of \$8,126,097 as of June 30, 2023.

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

The Statement of Revenues, Expenses and Changes in Net Position presents information showing how the Captive's net position changed during the fiscal year. All of the year's revenues and expenses are accounted for in this statement. This statement measures the results of the Captive's operations for the year and can be used to determine if the Captive has successfully recovered all of its costs through fees and charges. Operating revenues and expenses are related to the Captive's core activities. Non-operating revenues and expenses are not directly related to the core activities of the Captive. For the fiscal year ended June 30, 2023 net position increased by 14.33% or \$1,018,701.



**SPECIAL DISTRICT REINSURANCE GROUP**  
*Management's Discussion and Analysis (Unaudited)*  
*For the Fiscal Years Ended June 30, 2023*

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**FINANCIAL ANALYSIS AND CONDENSED FINANCIAL INFORMATION**

**Analysis of Net Position**

**Table A-1: Condensed Balance Sheet**

	<u>June 30, 2023</u>	<u>June 30, 2022</u>	<u>Change</u>
<b>Assets:</b>			
Current assets	\$ 1,250,419	\$ 1,497,248	\$ (246,829)
Non-current assets	28,635,790	15,379,877	13,255,913
<b>Total assets</b>	<u>\$ 29,886,209</u>	<u>\$ 16,877,125</u>	<u>\$ 13,009,084</u>
<b>Liabilities:</b>			
Current liabilities	\$ 10,015,307	\$ 2,108,296	\$ 7,907,011
Non-current liabilities	11,744,805	7,661,433	4,083,372
<b>Total liabilities</b>	<u>21,760,112</u>	<u>9,769,729</u>	<u>11,990,383</u>
<b>Net position:</b>			
Paid-in-capital	8,833,000	8,833,000	-
Unrestricted	(706,903)	(1,725,604)	1,018,701
<b>Total net position</b>	<u>8,126,097</u>	<u>7,107,396</u>	<u>1,018,701</u>
<b>Total liabilities and net position</b>	<u>\$ 29,886,209</u>	<u>\$ 16,877,125</u>	<u>\$ 13,009,084</u>

At June 30, 2023, the Captive showed a negative (deficit) balance in its unrestricted net position of \$706,903, due to the \$8,833,000 of paid-in-capital.

**Analysis of Revenues and Expenses**

**Table A-2: Condensed Statement of Revenues, Expenses and Changes in Net Position**

	<u>June 30, 2023</u>	<u>June 30, 2022</u>	<u>Change</u>
Operating revenues	\$ 11,620,000	\$ 11,409,000	\$ 211,000
Operating expenses	(12,629,993)	(10,631,170)	(1,998,823)
<b>Operating income(loss)</b>	(1,009,993)	777,830	(1,787,823)
Non-operating revenues(expenses), net	2,028,694	(2,503,434)	4,532,128
<b>Change in net position</b>	1,018,701	(1,725,604)	2,744,305
Net position:			
<b>Beginning of year</b>	7,107,396	3,833,000	3,274,396
<b>Paid-in-capital</b>	-	5,000,000	(5,000,000)
<b>End of year</b>	<u>\$ 8,126,097</u>	<u>\$ 7,107,396</u>	<u>\$ 1,018,701</u>

SDRG's net position increased by approximately 14.33% or \$1,018,701 compared to the prior year.

## SPECIAL DISTRICT REINSURANCE GROUP

### Management's Discussion and Analysis (Unaudited)

For the Fiscal Years Ended June 30, 2023

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#### Analysis of Revenues and Expenses

While the Statement of Net Position shows the change in financial position, the Statement of Revenues, Expenses and Changes in Net Position provides answers to the nature and source of these changes. The main factor in the change in net position is due to the following:

**Table A-3: Total Revenues**

	<u>June 30, 2023</u>	<u>June 30, 2022</u>	<u>Increase (Decrease)</u>
<b>Operating revenues:</b>			
Members' contributions	\$ 11,620,000	\$ 11,409,000	\$ 211,000
<b>Total operating revenues</b>	<u>11,620,000</u>	<u>11,409,000</u>	<u>211,000</u>
<b>Non-operating:</b>			
Investment earnings	2,028,694	(2,503,434)	4,532,128
<b>Total non-operating</b>	<u>2,028,694</u>	<u>(2,503,434)</u>	<u>4,532,128</u>
<b>Total revenues</b>	<u>\$ 13,648,694</u>	<u>\$ 8,905,566</u>	<u>\$ 4,743,128</u>

The operating revenues of the Captive consist of premium contributions from members. The Captive had 2023 operating revenue of \$11,620,000 as compared to 2022 operating revenue of \$11,409,000 due to increased member contributions in 2023. The Captive experienced \$2,028,694 in investment income in fiscal year 2022-23 due to increases in prevailing interest rates and mark-to-market adjustments to the Captive's fixed income holdings and equities.

**Table A-4: Total Expenses**

	<u>June 30, 2023</u>	<u>June 30, 2022</u>	<u>Increase (Decrease)</u>
<b>Operating expenses:</b>			
Claims expense	\$ 12,475,089	\$ 10,520,000	\$ 1,955,089
General and administrative	154,904	111,170	43,734
<b>Total operating expenses</b>	<u>12,629,993</u>	<u>10,631,170</u>	<u>1,998,823</u>
<b>Total expenses</b>	<u>\$ 12,629,993</u>	<u>\$ 10,631,170</u>	<u>\$ 1,998,823</u>

In fiscal year 2023, total expenses increased \$1,998,823 from \$10,631,170 in 2022 to \$12,629,993 in 2023 due primarily to an increase of \$1,955,089 in claims expenses.

**SPECIAL DISTRICT REINSURANCE GROUP**  
*Management's Discussion and Analysis (Unaudited)*  
*For the Fiscal Years Ended June 30, 2023*

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**FINANCIAL ANALYSIS AND CONDENSED FINANCIAL INFORMATION (continued)**

**FACTORS AFFECTING CURRENT FINANCIAL POSITION**

**Insurance Market Condition and Outlook**

The excess workers' compensation coverage market continues to remain relatively stable. However, the investment markets will influence premium increases: Little to no gains in investment income will have an adverse impact on premiums. As a result, we expect percentage rate increases to be roughly 20% conservatively.

**CONTACTING THE CAPTIVE'S FINANCIAL MANAGEMENT**

This financial report is designed to provide the Captives funding sources, customers, stakeholders and other interested parties with an overview of the Captive's financial operations and financial condition. Should the reader have questions regarding the information included in this report or wish to request additional financial information, please contact the Captive's Finance Department, 1112 I Street, Suite 300, Sacramento, CA 95814.

## SPECIAL DISTRICT REINSURANCE GROUP

### Balance Sheets

June 30, 2023 (With Comparative Amounts as of June 30, 2022)

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<b><u>ASSETS</u></b>	<b><u>2023</u></b>	<b><u>2022</u></b>
<b>Current assets:</b>		
Cash and cash equivalents (Note 2)	\$ 1,242,899	\$ 1,490,873
Prepaid expenses	7,520	6,375
<b>Total current assets</b>	<b>1,250,419</b>	<b>1,497,248</b>
<b>Non-current assets:</b>		
Investments (Note 2)	28,635,790	15,379,877
<b>Total non-current assets</b>	<b>28,635,790</b>	<b>15,379,877</b>
<b>Total assets</b>	<b>\$ 29,886,209</b>	<b>\$ 16,877,125</b>
<b><u>LIABILITIES AND NET POSITION</u></b>		
<b>Current liabilities:</b>		
Accounts payable and accrued expenses	\$ 31,363	\$ 450,462
Due to SDRMA	4,983,944	157,834
Long-term liabilities – due within one year: Claim-related payables (Note 3)	5,000,000	1,500,000
<b>Total current liabilities</b>	<b>10,015,307</b>	<b>2,108,296</b>
<b>Non-current liabilities:</b>		
Long-term liabilities – due in more than one year: Claim-related payables (Note 3)	11,744,805	7,661,433
<b>Total non-current liabilities</b>	<b>11,744,805</b>	<b>7,661,433</b>
<b>Total liabilities</b>	<b>21,760,112</b>	<b>9,769,729</b>
<b>Net position:</b>		
Contributed capital	8,833,000	8,833,000
Unrestricted	(706,903)	(1,725,604)
<b>Total net position</b>	<b>8,126,097</b>	<b>7,107,396</b>
<b>Total liabilities and net position</b>	<b>\$ 29,886,209</b>	<b>\$ 16,877,125</b>

**SPECIAL DISTRICT REINSURANCE GROUP***Statements of Revenues Expenses and Changes in Net Position**For the Fiscal Year Ended June 30, 2023**(With Comparative Amounts for the Fiscal Year Ended June 30, 2022)*

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	<u>2023</u>	<u>2022</u>
<b>Operating revenues:</b>		
Members' contributions	\$ 11,620,000	\$ 11,409,000
<b>Total operating revenues</b>	<u>11,620,000</u>	<u>11,409,000</u>
<b>Operating expenses:</b>		
Claims expense	12,475,089	10,520,000
General and administrative	154,904	111,170
<b>Total operating expenses</b>	<u>12,629,993</u>	<u>10,631,170</u>
<b>Operating income(loss)</b>	<u>(1,009,993)</u>	<u>777,830</u>
<b>Non-operating revenues(expenses):</b>		
Investment earnings	<u>2,028,694</u>	<u>(2,503,434)</u>
<b>Total non-operating revenue, net</b>	<u>2,028,694</u>	<u>(2,503,434)</u>
<b>Change in net position</b>	1,018,701	(1,725,604)
<b>Net position:</b>		
Beginning of year	7,107,396	3,833,000
Paid-in-capital	-	5,000,000
End of year	<u>\$ 8,126,097</u>	<u>\$ 7,107,396</u>

## SPECIAL DISTRICT REINSURANCE GROUP

### Statements of Cash Flows

For the Fiscal Year Ended June 30, 2023

(With Comparative Amounts for the Fiscal Year Ended June 30, 2022)

	<u>2023</u>	<u>2022</u>
<b>Cash flows from operating activities:</b>		
Cash receipts from members	\$ 11,620,000	\$ 11,409,000
Cash paid for administration expenses	(154,904)	(111,170)
Cash paid to members and vendors for claims and premiums	(485,851)	(756,646)
<b>Net cash provided by operating activities</b>	<u>10,979,245</u>	<u>10,541,184</u>
<b>Cash flows from investing activities:</b>		
Purchase of investments, net	(12,051,551)	(13,369,465)
Investment earnings	824,332	486,154
<b>Net cash used in investing activities</b>	<u>(11,227,219)</u>	<u>(12,883,311)</u>
<b>Net decrease in cash and cash equivalents</b>	(247,974)	(2,342,127)
<b>Cash and cash equivalents:</b>		
Beginning of year	1,490,873	3,833,000
End of year	<u>\$ 1,242,899</u>	<u>\$ 1,490,873</u>
<b>Reconciliation of cash and cash equivalents to the balance sheet:</b>		
Cash and cash equivalents	\$ 1,242,899	\$ 1,490,873
Restricted – cash and cash equivalents	-	-
<b>Total cash and cash equivalents</b>	<u>\$ 1,242,899</u>	<u>\$ 1,490,873</u>
	<u>2023</u>	<u>2022</u>
<b>Reconciliation of operating income(loss) to net cash provided by operating activities:</b>		
Operating income(loss)	\$ (1,009,993)	\$ 777,830
<b>Adjustments to reconcile operating income(loss) to net cash provided by operating activities:</b>		
<b>Change in assets – (increase)decrease:</b>		
Prepaid expenses	(1,145)	(6,375)
<b>Change in liabilities – increase(decrease):</b>		
Accounts payable and accrued expenses	(419,099)	608,297
Due to SDRMA	4,826,110	157,834
Claim-related liabilities	7,583,372	9,003,598
<b>Total adjustments</b>	<u>11,989,238</u>	<u>9,763,354</u>
<b>Net cash provided by operating activities</b>	<u>\$ 10,979,245</u>	<u>\$ 10,541,184</u>
<b>Noncash investing, capital and financing transactions</b>		
Change in fair-value of investments	<u>\$ 1,204,362</u>	<u>\$ (2,989,588)</u>

## **SPECIAL DISTRICT REINSURANCE GROUP**

*Notes to Financial Statements*

*June 30, 2023*

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### **NOTE 1 – DESCRIPTION OF ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES**

#### **Organization and Operations of the Reporting Entity**

The Special District Reinsurance Group (the Captive) is a captive insurance company regulated by the Utah Insurance Department. The Captive is reported as a blended component unit of the Special District Risk Management Authority (the Authority), which is a California governmental Joint Powers Authority. Only the risks of the Authority, its parent company, are transferred to the Captive. The Captive, a component unit of the Authority, provides insurance coverage to the Authority. As part of the Authority, the assets, liabilities, revenues, expenses, and changes in net position of the Captive are included in the consolidated financial statements of the Authority. The Captive is a not-for-profit corporation formed on July 1, 2021 under the State of Utah rules for nonprofit entities and is governed by its Board of Directors and regulated by the Utah Insurance Department.

The Authority is the sole member of the Captive. Beginning in program year 2021/2022, the Captive provided assumed reinsurance coverage for the Authority's workers' compensation claims up to the program's self-insured retention (SIR) of \$750,000 per occurrence for claims occurring after July 1, 2021. All claims occurring prior to July 1, 2021 will remain with the Authority.

Effective for the year ended June 30, 2022, the unallocated loss adjustment expense (ULAE) component of the outstanding liability estimate is included in the Authority's workers' compensation claims liability, as those expenses are not ceded to the Captive.

#### **Basis of Accounting and Measurement Focus**

The Captive reports its activities as an enterprise fund, which is used to account for operations that are financed and operated in a manner similar to a private business enterprise, where the intent of the Captive is that the costs of providing services be financed or recovered primarily through member charges. Revenues and expenses are recognized on the full accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred, regardless of when the related cash flows take place.

#### **Financial Reporting**

The Captive's basic financial statements have been prepared in conformity with accounting principles generally accepted in the United States Board (GAAP), as applied to enterprise funds. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Captive solely operates as a special-purpose government which means it is only engaged in business-type activities; accordingly, activities are reported in the Captive's proprietary fund.

Operating revenues and expenses result from exchange transactions associated with the principal activity of the Captive. Exchange transactions are those in which each party receives and gives up essentially equal values. Management administration and depreciation expenses are also considered operating expenses. Other revenues and expenses not included in the above categories are reported as non-operating revenues and expenses.

#### **Cash and Cash Equivalents**

For purposes of the statement of cash flows, the Captive considers all highly liquid investments with a maturity of three months or less, when purchased, to be cash equivalents. Cash deposits are reported at carrying amount, which reasonably estimates fair value.

## **SPECIAL DISTRICT REINSURANCE GROUP**

*Notes to Financial Statements*

*June 30, 2023*

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### **NOTE 1 – DESCRIPTION OF ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)**

#### **Investments**

Investments are reported at fair value except for short-term investments, which are reported at cost, which approximates fair value. Cash deposits are reported at carrying amount, which reasonably estimates fair value. Investments in governmental investment pools are reported at fair value based on the fair value per share of the pool's underlying portfolio.

In accordance with fair value measurements, the Captive categorizes its assets and liabilities measured at fair value into a three-level hierarchy based on the priority of the inputs to the valuation technique used to determine fair value. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used in the determination of the fair value measurement fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement.

Financial assets and liabilities recorded on the balance sheet are categorized based on the inputs to the valuation techniques as follows:

*Level 1* – Inputs that reflect unadjusted quoted prices in active markets for identical investments, such as stocks, corporate and government bonds. The Captive has the ability to access the holding and quoted prices as of the measurement date.

*Level 2* – Inputs, other than quoted prices, that are observable for the asset or liability either directly or indirectly, including inputs from markets that are not considered to be active.

*Level 3* – Inputs that are unobservable. Unobservable inputs reflect the Captive's own assumptions about the factors market participants would use in pricing an investment and is based on the best information available in the circumstances.

#### **Prepaid Expenses**

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items.

#### **Claim Related Liabilities (Claims Payable, Claims Incurred but Not Reported, and Liability for Unallocated Loss Adjustment Expenses).**

The Captive establishes claims liabilities based on estimates of the ultimate cost of claims (including future claim adjustment expenses) that have been reported but not settled, and of claims that have been incurred but not reported (IBNR). The length of time for which such costs must be estimated varies by the coverage involved. Estimated amounts of salvage and subrogation and excess insurance recoverable on unpaid claims are deducted from the liability for unpaid claims. Because actual claims costs depend on such complex factors as inflation, changes in doctrines of legal liability, and damage awards, the process used in computing claims liabilities does not necessarily result in an exact amount, particularly for coverage such as general liability.

Claims liabilities are re-computed periodically using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, claim frequency, and other economic and social factors. A provision for inflation in the calculation of estimated future claims costs is implicit in the calculation because reliance is placed both on actual historical data that reflects past inflation and on other factors that are considered to be appropriate modifiers of past experience. Adjustments to claims liabilities are charged or credited to expense in the period in which they are made.



## **SPECIAL DISTRICT REINSURANCE GROUP**

*Notes to Financial Statements*

*June 30, 2023*

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### **NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

#### **Net Position**

The financial statements utilize a net position presentation. Net position is categorized as follows:

**Paid-in capital** - This component of net position consists of the full amount of cash that shareholders (SDRMA) have paid into the Captive in exchange for equity.

**Unrestricted** – This component of net position is the net amount of the assets less liabilities that are not included in the paid-in capital component of net position.

#### **Member Contributions**

Enterprise fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as subsidies and investment earnings, result from non-exchange transactions or ancillary activities.

Revenues mainly consist of premium contributions from members. Contribution development is performed by actuaries and the Board of Directors based on the particular characteristics of the members. Contribution income consists of payments from members that are planned to match the expense of insurance premiums for coverage in excess of self-insured amounts, estimated payments resulting from self-insurance programs, and operating expenses. The activities of the Authority consist solely of risk management programs and claims management activities related to the coverages described above.

The reporting entity does not include any other component units with the criterion prescribed by GAAP. Member contributions are recognized as revenues in the period for which coverage protection is provided. If the Board of Directors determines that the funds for a program are insufficient to pay losses, the Authority may impose a supplemental assessment on all participating members. Anticipated investment income is not considered in determining supplemental assessments. Supplemental assessments are recognized as income in the period assessed.

#### **Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (“U.S. GAAP”) requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from these estimates.

## SPECIAL DISTRICT REINSURANCE GROUP

### Notes to Financial Statements

June 30, 2023

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#### NOTE 2 – CASH AND INVESTMENTS

Cash and investments at June 30, 2023, are classified on the balance sheet as follows:

Description	June 30, 2023
Cash and cash equivalents	\$ 1,242,899
Investments	28,635,790
<b>Total cash and investments</b>	<b>\$ 29,878,689</b>

Cash and investments at June 30, 2023, consisted of the following:

Description	June 30, 2023
Demand deposits held with financial institutions	\$ 1,055,958
Money market mutual fund	186,941
Investments	28,635,790
<b>Total cash and investments</b>	<b>\$ 29,878,689</b>

#### Demand Deposits with Financial Institutions

At June 30, 2023 the carrying amount of the Captive's demand deposits was \$1,055,958, and the financial institution's balance was \$1,062,010. The net difference represents outstanding checks, deposits-in-transit and/or other reconciling items between the financial institution's balance and the Captive's balance for the year.

#### Custodial Credit Risk – Deposits

Custodial credit risk is the risk that in the event of a bank failure, the Captive's deposits may not be returned to it. The Captive does not have a policy for custodial credit risk for deposits. Cash balances held in banks are insured up to \$250,000 by the Federal Depository Insurance Corporation (FDIC) and are collateralized by the respective financial institutions. In addition, the California Government Code requires that a financial institution secure deposits made by State or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under State law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110 percent of the total amount deposited by the public agencies. California law also allows financial institutions to secure public deposits by pledging first trust deed mortgage notes having a value of 150 percent of the secured public deposits and letters of credit issued by the Federal Home Loan Bank of San Francisco having a value of 105 percent of the secured deposits.

#### Money-Market Funds

Money-market funds are an investment whose objective is to earn modest investment earnings while maintaining a net asset value (NAV) of \$1 per share (which is the funds main goal – preservation of principal). A money-market fund's portfolio is typically comprised of short-term, or less than one year, securities representing high-quality, liquid debt and monetary instruments with minimal credit risk. Money-market funds are Level 1 investments (with quoted prices in active markets for identical assets) that are Not Rated under the current credit risk ratings format. For financial reporting purposes, the District considers money market funds a cash equivalent due to their highly liquid nature and NAV of \$1 per share. As of June 30, 2023 the Captive held \$186,941, in money market funds.

## SPECIAL DISTRICT REINSURANCE GROUP

Notes to Financial Statements

June 30, 2023

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### NOTE 2 – CASH AND INVESTMENTS (continued)

#### Investments

The Captive's investments as of June 30, 2023 were as follows:

	<u>Total</u> <u>Fair Value</u>	<u>% of Portfolio</u>
<b>Exchange traded Funds:</b>		
Equity	\$ 12,582,834	44%
Fixed Income	2,760,687	10%
<b>Mutual Funds:</b>		
Equity	1,949,012	6%
Fixed Income	<u>11,343,257</u>	40%
<b>Total investments</b>	<u>\$ 28,635,790</u>	

Mutual funds and exchange traded funds (ETF) are valued using quoted market prices (Level 1 Input).

#### Fair Value Measurement Input

The Captive categorizes its fair value measurement inputs within the fair value hierarchy established by generally accepted accounting principles. The Captive has presented its measurement inputs as noted in the previous table.

#### Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization.

#### Concentration of Credit Risk

The Captives investment policy places long-term asset allocation targets as follows:

<u>Asset Class</u>	<u>Allocation</u>
Equities	50%
Fixed Income	50%

1. The equity allocation limitation is specific to the surplus funds of the Captive.
2. The asset manager will be responsible for determining the asset allocation within the targets and rebalance as necessary.
3. The fixed income allocation includes the liquidity portion to meet short-term cash flow requirements. The liquidity portfolio will maintain cash and cash equivalents of \$250,000 as required by the Utah Insurance Department.

As of June 30, 2023, the investments in the Captive's portfolio conform to the guidelines.

## SPECIAL DISTRICT REINSURANCE GROUP

Notes to Financial Statements

June 30, 2023

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### NOTE 2 – CASH AND INVESTMENTS (continued)

#### Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the fair values of investments with longer maturities have greater sensitivity to changes in market interest rates. The Captive has elected to use the segmented time distribution method of disclosure for the maturities of its investments as related to interest rate risk as noted in the previous table.

#### Custodial Credit Risk – Investments

The custodial credit risk for *investments* is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The Captive's investment policy contains legal and policy requirements that would limit the exposure to custodial credit risk for investments. With respect to investments, custodial credit risk generally applies only to direct investments in marketable securities. Custodial credit risk does not apply to a local government's indirect investment in securities through the use of mutual funds or government investment pools.

### NOTE 3 – UNPAID CLAIM LIABILITIES

The Captive establishes a liability for both reported and unreported insured events, which includes estimates of both future payments of losses and related claims adjustment expenses. The following represents changes in those aggregate liabilities for all programs during the year ended June 30:

	<u>2023</u>	<u>2022</u>
Unpaid claims and claim adjustment expenses at beginning of year	\$ 9,161,433	\$ -
<b>Incurring claims and claim adjustment expenses:</b>		
Provision for insured events of the current year	12,872,000	10,520,000
Increase (decrease) in provision of insured events of prior years	<u>(396,911)</u>	<u>-</u>
<b>Total incurred claims and claim adjustment expenses</b>	<u>12,475,089</u>	<u>10,520,000</u>
<b>Payments:</b>		
Claim and claim adjustment expenses attributable to insured events of current year	2,334,738	1,358,567
Claim and claim adjustment expenses attributable to insured events of prior years	<u>2,556,979</u>	<u>-</u>
<b>Total payments</b>	<u>4,891,717</u>	<u>1,358,567</u>
<b>Total unpaid claims and claims adjustment expenses</b>	<u>\$ 16,744,805</u>	<u>\$ 9,161,433</u>
<b>Detail of claim related Liabilities:</b>		
Claims payable	\$ 8,173,340	\$ 3,036,727
Claims incurred but not reported	<u>8,571,465</u>	<u>6,124,706</u>
<b>Total</b>	<u>\$ 16,744,805</u>	<u>\$ 9,161,433</u>
Current portion	\$ 5,000,000	\$ 1,500,000
Non-current portion	<u>11,744,805</u>	<u>7,661,433</u>
<b>Total</b>	<u>\$ 16,744,805</u>	<u>\$ 9,161,433</u>

## **SPECIAL DISTRICT REINSURANCE GROUP**

*Notes to Financial Statements*

*June 30, 2023*

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### **NOTE 4 – COMMITMENTS AND CONTINGENCIES**

#### **Litigation**

The Captive is involved in routine litigation incidental to its business and may be subject to claims and litigation from outside parties. After consultation with legal counsel, management believes the ultimate outcome of such matters, if any, will not materially affect its financial condition.

### **NOTE 5 – SUBSEQUENT EVENTS**

The Captive has evaluated subsequent events through November 30, 2023, the date which the financial statements were available to be issued.

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***Other Information***

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**SPECIAL DISTRICT REINSURANCE GROUP**  
*Claims Development Information*  
*For the Fiscal Years Ended June 30, 2022 to 2023*

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	<b>Fiscal and Policy Year</b>	
	<b>Ended June 30</b>	
	<b>2022</b>	<b>2023</b>
Total Required Contribution and Investment Revenue Ceded	\$ 8,905,566	\$ 13,648,694
1 Net Earned Required Contribution and Investment Revenues	8,905,566	13,648,694
2 Unallocated Expenses	111,171	154,902
3 Estimated Incurred Claims and Expense		
Year End	10,520,000	12,872,000
Ceded	-	-
Net	10,520,000	12,872,000
4 Paid (Cumulative)		
Year End	1,358,567	2,334,738
One Year Later	4,401,456	
5 Reestimated Ceded Claims and Experience	-	-
6 Reestimated Ceded Claims and Experience		
End of Year	10,520,000	12,872,000
One Year Later	10,609,000	-
7 Increase (Decrease in Estimated Incurred Claims Expense from End of Policy Year	89,000	-

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***Other Independent Auditors' Reports***

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

Board of Directors  
Special Captive Reinsurance Group  
Sacramento, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the Special Captive Reinsurance Group (Captive) which comprise the balance sheet as of June 30, 2023, and the related statements of revenues, expenses, and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, which collectively comprise the Captive's basic financial statements, and have issued our report thereon dated November 30, 2023.

**Internal Control Over Financial Reporting**

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

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Captive'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 or significant deficiencies may exist that have not been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Captive's financial statements are free of 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 financial statements. 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 Captive'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 Captive's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Murrieta, California  
November 30, 2023