

**UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)**

ANNUAL FINANCIAL REPORT

Year Ended December 31, 2016



Certified Public Accountants and Business Consultants

INTRODUCTORY SECTION

**UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)**

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YEAR ENDED DECEMBER 31, 2016

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FINANCIAL SECTION

Independent Auditors' Report

To the Board of Directors
Upper Merion Municipal Utility Authority
King of Prussia, Pennsylvania

We have audited the accompanying financial statements of the Upper Merion Municipal Utility Authority (a component unit of Upper Merion Township), which comprise the statement of net position as of December 31, 2016, 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.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion 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 auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the 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.

To the Board of Directors
Upper Merion Municipal Utility Authority
King of Prussia, Pennsylvania

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Upper Merion Municipal Utility Authority as of December 31, 2016, 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 (GAAP).

Emphasis of Matter

For the year ended December 31, 2016, the Upper Merion Municipal Utility Authority adopted new accounting guidance, implementing Governmental Accounting Standards Board Statements No. 72, *Fair Value Measurement and Application* and No. 79 *Certain External Investment Pools and Pool Participants*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 4 through 7 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 evidence sufficient to express an opinion or provide any assurance.

Maillie LLP

Oaks, Pennsylvania
June 7, 2017

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
MANAGEMENT'S DISCUSSION AND ANALYSIS (Unaudited)
YEAR ENDED DECEMBER 31, 2016

Our discussion and analysis of the Upper Merion Municipal Utility Authority's (a component unit of Upper Merion Township) financial performance provides an overview of the Authority's financial activities for the fiscal year ended December 31, 2016. Please read it in conjunction with the Authority's financial statements, which begin with the statement of net position.

OVERVIEW OF THE FINANCIAL STATEMENTS

The Authority's annual financial report consists of several sections. Taken together, they provide a comprehensive financial look at the Authority. The components of the report include the independent auditors' report, management's discussion and analysis, financial statements and notes to the basic financial statements.

The independent auditors' report briefly describes the audit engagement and also renders an opinion as to the material components of the Authority's financial position.

Management's discussion and analysis (MD&A), prepared by Authority/Township management, provides a narrative introduction and overview that users of the financial statements need to interpret the basic financial statements. The MD&A also provides analysis of some key data that is presented in the basic financial statements. It also addresses any other currently known facts, decisions, or conditions that are expected to have a significant effect on financial position or results of operations.

The basic financial statements include the statement of net position, statement of revenues, expenses and changes in net position, statement of cash flows and the notes to the basic financial statements.

- The *statement of net position* shows the financial condition of the Authority at the end of the fiscal period or a specific snapshot in time.
- The *statement of revenues, expenses and changes in net position* measures the results of operations of the Authority during the fiscal period.
- The *statement of cash flows* measures the resources provided during the fiscal period and the uses to which they are put.
- The *notes to the basic financial statements* provide additional disclosures required by governmental accounting standards and provide information to assist the reader in understanding the Authority's financial condition.

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
MANAGEMENT'S DISCUSSION AND ANALYSIS (Unaudited)
YEAR ENDED DECEMBER 31, 2016

The analysis below focuses on the net position (Table 1) and changes in net position (Table 2) of the Authority.

Table 1
Condensed Statements of Net Position
December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
ASSETS		
Cash and investments	\$ 3,709,631	\$ 2,695,074
Capital assets, net of accumulated depreciation	<u>17,289,028</u>	<u>18,053,138</u>
TOTAL ASSETS	<u>20,998,659</u>	<u>20,748,212</u>
LIABILITIES		
Other liabilities	<u>144,530</u>	<u>88,507</u>
NET POSITION		
Net investment in capital assets	17,289,028	18,053,138
Unrestricted	<u>3,565,101</u>	<u>2,606,567</u>
TOTAL NET POSITION	<u>\$ 20,854,129</u>	<u>\$ 20,659,705</u>

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
MANAGEMENT'S DISCUSSION AND ANALYSIS (Unaudited)
YEAR ENDED DECEMBER 31, 2016

Table 2
Condensed Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2016 and 2015

	2016	2015
REVENUES		
Tapping fees	\$ 676,060	\$ 367,455
Lease payments	960,000	960,000
Investment income	13,599	11,009
TOTAL REVENUES	1,649,659	1,338,464
EXPENSES		
Administrative	7,518	5,427
Professional fees	52,136	45,863
Depreciation	1,268,448	1,248,850
Reimbursement to Township	127,133	125,500
Road construction	-	611
Interest on long-term debt	-	105,971
TOTAL EXPENSES	1,455,235	1,532,222
CHANGE IN NET POSITION	194,424	(193,758)
NET POSITION, BEGINNING	20,659,705	20,853,463
NET POSITION, ENDING	\$ 20,854,129	\$ 20,659,705

REPORTING

The Upper Merion Municipal Utility Authority was established in 1986 to finance the Township's sewage collection and treatment facilities. A five-member board, appointed by the Township's Board of Supervisors, governs the Authority. Although legally separate, the Authority is considered a component unit of the Township because the Township is financially accountable for it. The major function of the Authority is to provide financing for capital construction of the Township's sewage collection and treatment facilities. The Authority owns two waste treatment plants, 12 pumping stations and 125 miles of sewer lines. The Township has the responsibility for daily operations through a leaseback arrangement with the Authority.

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
MANAGEMENT'S DISCUSSION AND ANALYSIS (Unaudited)
YEAR ENDED DECEMBER 31, 2016

Cash and investments represent 18.0% of the Authority's total assets. By far the largest portion of the Authority's assets, 82.0%, reflects its investment in capital assets (e.g., property and equipment). Accumulated depreciation reflects 68.9% of total capital assets.

The Authority developed a program of advance payments for individuals, developers and businesses to purchase non-allocated and future capacity in the sanitary sewer system. The program was launched due to the need to construct and upgrade sewage treatment capacity. The program is called Upper Merion Sewer Access Rights (UMSAR) and is the primary revenue source for the Authority. It has provided increased sewer capacity for new customers but at the same time has minimized cost increases to present customers. The fee structure is based on the sale of Equivalent Dwelling Units (EDU). Each EDU represents approximately 225 gallons of sewage capacity. The current cost of one EDU is equal to \$6,800. The 2016 collection of UMSAR totals \$676,060. UMSAR revenues from the program's inception to December 31, 2016, equate to \$23,205,779.

The revenue obtained from the sale of sewer capacity is expended to fund continued expansions and upgrades to the two plants and collection system. This arrangement follows an agreement with the Pennsylvania Department of Environmental Protection, which assisted in planning for future improvements. At December 31, 2016, the Authority's investments had an approximate fair value of \$958,159. Please see Note B to the financial statements for additional information on the Authority's investments.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the Authority's finances and to show the Authority's accountability for the funds it receives and disburses. If you have questions about this report or need additional information, please contact the Director of Finance and Administration at 175 West Valley Forge Road, King of Prussia, PA 19406-1802.

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
STATEMENT OF NET POSITION
DECEMBER 31, 2016

ASSETS

CURRENT ASSETS

Cash	\$ 2,751,472
Investments	<u>958,159</u>
TOTAL CURRENT ASSETS	<u>3,709,631</u>

NONCURRENT ASSETS

Capital assets	
Building and improvements	55,670,979
Accumulated depreciation	<u>(38,381,951)</u>
TOTAL CAPITAL ASSETS	<u>17,289,028</u>

TOTAL ASSETS	<u>20,998,659</u>
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LIABILITIES

CURRENT LIABILITIES

Accounts payable	17,807
Due to Upper Merion Township	<u>126,723</u>
TOTAL LIABILITIES	<u>144,530</u>

NET POSITION

Net investments in capital assets	17,289,028
Unrestricted	<u>3,565,101</u>
TOTAL NET POSITION	<u>\$ 20,854,129</u>

See accompanying notes to the basic financial statements.

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
STATEMENT OF REVENUES, EXPENSES AND
CHANGES IN NET POSITION
YEAR ENDED DECEMBER 31, 2016

OPERATING REVENUES	
Lease payments	\$ <u>960,000</u>
OPERATING EXPENSES	
Administrative	7,518
Professional fees	52,136
Depreciation	1,268,448
Reimbursement to Upper Merion Township	127,133
TOTAL OPERATING EXPENSES	<u>1,455,235</u>
OPERATING LOSS	<u>(495,235)</u>
NONOPERATING REVENUES	
Investment income	13,599
Tapping fees	676,060
TOTAL NONOPERATING REVENUES	<u>689,659</u>
CHANGE IN NET POSITION	194,424
NET POSITION AT BEGINNING OF YEAR	<u>20,659,705</u>
NET POSITION AT END OF YEAR	<u>\$ <u>20,854,129</u></u>

See accompanying notes to the basic financial statements.

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)

STATEMENT OF CASH FLOWS
YEAR ENDED DECEMBER 31, 2016

CASH FLOWS FROM OPERATING ACTIVITIES	
Cash received from lease payments	\$ 960,000
Cash payments to suppliers for services	(53,851)
Cash payments to other governments	<u>(127,133)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>779,016</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Capital acquisitions	(504,338)
Tapping fees	<u>676,060</u>
NET CASH PROVIDED BY CAPITAL AND RELATED FINANCING ACTIVITIES	<u>171,722</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Investment income	13,599
Maturities of investments, net	<u>566,672</u>
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>580,271</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
Due from Upper Merion Township	<u>50,220</u>
NET INCREASE IN CASH	1,581,229
CASH AT BEGINNING OF YEAR	<u>1,170,243</u>
CASH AT END OF YEAR	<u>\$ 2,751,472</u>
RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES	
Operating loss	\$ (495,235)
Adjustments to reconcile operating loss to net cash provided by operating activities	
Depreciation	1,268,448
Changes in assets and liabilities	
Accounts payable	<u>5,803</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 779,016</u>

See accompanying notes to the basic financial statements.

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Purpose of the Authority

Upper Merion Municipal Utility Authority (the "Authority") is a separate legal entity (incorporated August 6, 1986), which is primarily responsible for bonds issued to finance the expansion of the Matsunk Sewer Treatment Plant and system and the Trout Run Sewer Plant in the Township.

Basis of Presentation

The financial statements of the Authority include all accounts of Upper Merion Township (the "Township") which relate to the Authority. The Authority is a component unit of the Township because of its role in financing and constructing Township facilities.

Basis of Accounting

The measurement focus is on the flow of economic resources and the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recorded when incurred.

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, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will *not* be recognized as an outflow of resources (expense/expenditure) until then. The Authority has no items that qualify for reporting in this category.

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, *deferred inflows of resources*, represents an acquisition of net position that applies to a future period(s) and so will *not* be recognized as an inflow of resources (revenue) until that time. The Authority has no items that qualify for reporting in this category.

Net Position Flow Assumption

Sometimes the Authority will 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 Proprietary Fund financial statements, a flow assumption must be made about the order in which the resources are considered to be applied. It is the Authority's policy to consider restricted net position to have been depleted before unrestricted net position is applied.

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investments

The Authority has adopted GASB Statements No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, No. 72, *Fair Value Measurement and Application* and No. 79 *Certain External Investment Pools and Pool Participants*. In accordance with these Statements, investments in marketable securities with readily determinable fair value and all investments in debt securities are reported at their fair values. Investments in qualifying external investment pools are reported at amortized cost basis.

Property and Equipment

Property consists of sewer treatment plants and improvements and sewer equipment recorded at cost and depreciated using the straight-line method over estimated useful lives ranging from 10 to 40 years.

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 certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Sewer Access Rights

Sewer access rights consist of advance payments made to the Authority to reserve capacity in the sewage system. Income is recognized as occupancy permits are approved.

NOTE B - CASH AND INVESTMENTS

Deposits

Custodial Credit Risk - Custodial credit risk is the risk that, in the event of a bank failure, the Authority's deposits may not be returned to it. Deposits are insured under Act 72 of the 1971 Session of the Pennsylvania General Assembly, whereby financial institutions were granted the authority to secure deposits of public bodies by pledging a pool of assets, as defined in the Act, to cover all public funds deposited in excess of FDIC limits. As of December 31, 2016, \$911,783 of the Authority's \$2,751,626 bank balance is uninsured and collateralized with securities held by the pledging bank's trust department not in the Authority's name, \$500,000 was insured by FDIC and \$1,339,843 is uninsured and uncollateralized.

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE B - CASH AND INVESTMENTS (Continued)

Investments

As of December 31, 2016, the Authority had the following investments and maturities:

<u>Investment Type</u>	<u>Amortized Cost</u>	<u>Investment Maturities Less Than One Year</u>
State investment pools	\$ 215,102	\$ 215,102
Certificates of Deposit	<u>743,057</u>	<u>743,057</u>
	<u>\$ 958,159</u>	<u>\$ 958,159</u>

A portion of the Township’s investments is in the PLGIT program, of which are funds similar to mutual funds. GASB Statement No. 3, Paragraph 69, provides that certain types of cash and investments, such as cash investments in a State Treasurer’s investment pool or mutual fund, cannot be assigned a credit risk category because the government does not own specific securities. Therefore, the PLGIT cash investments included in these statements will not be assigned a credit risk category. The carrying amount of these investments at December 31, 2016, is \$215,102. These assets maintain a stable net asset value of \$1 per share. All investments are monitored weekly by Standard & Poor’s and are subject to an independent audit on an annual basis.

Investments held with qualifying external state investment pools are valued at amortized costs in accordance with GASB Statement No. 79.

Certificates of deposit held by banks of \$743,057 are stated at cost plus interest earned.

Investments of the Authority covered by the investment policy are limited to the following investment instruments:

1. All obligations of the U.S. Government or its agencies.
2. Certificates of deposit of U.S. commercial banks insured by the FDIC up to \$250,000. Certificates of deposit in excess of \$250,000 must be secured by a pledge of government securities.
3. Money market funds and other diversified pools of short and intermediate fixed income securities. Only those “dollar denominated” funds that invest only in high quality short- and intermediate-term government securities, essentially as described above.

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE B - CASH AND INVESTMENTS (Continued)

Interest Rate Risk - The Authority's investment policy limits investment maturities to remain sufficiently liquid to meet all operating requirements that are reasonably anticipated as a means of managing its exposure to fair value losses arising from increasing interest rates. No issues may be purchased with more than five years to maturity.

Fair Value Measurement - 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 asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are those that lack significant observable inputs. The Authority did not have any recurring fair value measurements as of December 31, 2016.

Credit Risk - Only debt issues that meet or exceed a credit rating of A from Standard & Poor's and/or an A rating from Moody's may be purchased. As of December 31, 2016, the Authority's investment in the state investment pool was rated AAAM by Standard & Poor's.

Although not registered with the Securities and Exchange Commission and not subject to formal regulatory oversight, the state investment pool is subject to an independent annual audit. The fair value in the external investment pool is equivalent to the value of the pool shares.

Concentration of Credit Risk - Investments in securities of a single issuer (with the exception of the U.S. Government and its agencies) must not exceed 5% of the value (10% if rated AAA). No more than 10% of the securities' par value (excluding issues of the U.S. Government and its agencies) may be invested in the securities of any one issuer or 5% in any one issue (10% if rated AAA).

NOTE C - CAPITAL ASSETS

The following is a summary of changes in capital assets during the year:

	Balance January 1, 2016	Additions	Deletions	Balance December 31, 2016
Treatment plant and improvements	\$ 55,166,641	\$ 504,338	\$ -	\$ 55,670,979
Accumulated depreciation	<u>(37,113,503)</u>	<u>(1,268,448)</u>	<u>-</u>	<u>(38,381,951)</u>
	<u>\$ 18,053,138</u>	<u>\$ (764,110)</u>	<u>\$ -</u>	<u>\$ 17,289,028</u>

UPPER MERION MUNICIPAL UTILITY AUTHORITY
(A Component Unit of Upper Merion Township)
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2016

NOTE D - COMMITMENTS AND CONTINGENCIES

Lease Management Agreement

During 1986, the Authority entered into a lease management agreement with the Township to manage and operate the Matsunk Sewer Treatment Plant and collection lines and to perform other functions on behalf of the Authority. The Township makes an annual lease payment of \$960,000 to the Authority.

NOTE E - SUBSEQUENT EVENTS

The Upper Merion Municipal Utility Authority changed its name to the Upper Merion Sanitary and Stormwater Authority effective April 13, 2017. The Authority's purpose has also been expanded, under the authority of Act 22 of 2001, to include but not limited to the planning, management, and implementation of stormwater systems and the assessment of any fee.