

NOTE 8: CLAIMS, JUDGMENTS and RISK MANAGEMENT

Pima County is a defendant in a number of court actions. In the opinion of County management, the final disposition of these actions, if unfavorable, will not have a material effect upon the County's financial statements.

Wastewater Management

On March 5, 1999, the City of Tucson ("Tucson") filed a complaint in state court (the "Wastewater Litigation") against the County, alleging material breaches of a June 29, 1979 Intergovernmental Agreement (the "1979 IGA") between the County and Tucson. Under the 1979 IGA, Tucson deeded to the County its sewage collection and treatment facilities, thus creating the metropolitan sewer system (the "System") owned and operated by the County.

In its complaint, Tucson requests that the County be ordered to cure its alleged breaches under the IGA and to pay monetary damages, currently less than \$700. The County has filed an answer to the complaint, defending against Tucson's claims, and a counterclaim alleging material breaches of the 1979 IGA by Tucson.

The 1979 IGA and associated documents contain provisions for termination of the 1979 IGA and for the reversion to Tucson of the Tucson portion of the System, which may be exercised by either Tucson or the County upon the occurrence of certain breaches thereunder. Neither Tucson's nor the County's pleadings to date in the Wastewater Litigation seek termination of the 1979 IGA or the return of the Tucson portion of the System. However, if a breach under the 1979 IGA were determined to exist, either party could terminate the 1979 IGA and trigger a return to Tucson of the Tucson portion of the System.

The County cannot currently determine the eventual outcome of the Wastewater Litigation, nor determine what effect, if any, a reversion to Tucson of the Tucson portion of the System might have on the operations or financial condition of the System.

Metropolitan Domestic Water Improvement District

On December 17, 1997, Metropolitan Domestic Water Improvement District (MDWID) and the City of Tucson entered into a settlement agreement to resolve the issues raised in the litigation, which originated on August 16, 1995. On January 26, 1998, the parties entered into an amended and restated settlement agreement, which superseded the original December agreement. On February 9, 1998, the parties adopted a first amendment to the amended and restated settlement agreement, which replaced or modified some provisions of the restated agreement, while leaving the rest intact.

Under the terms of the parties' agreements, as presently constituted, MDWID and Oro Valley together were obligated to make an initial payment to a trustee in the aggregate amount of \$800 within 30 days of the entry of a court order tentatively approving the settlement. That payment was timely made on March 25, 1998. Thereafter, MDWID and Oro Valley are obligated to make 42 semi-annual installment payments to the trustee, U.S. Bank Trust. All payments have been made timely to date. Each of the first 30 installments is in the total amount of \$375; MDWID's share is \$350. Each of the final 12 installments is in the total amount of \$820; MDWID's share is \$765. MDWID may prepay the installment payments at their option.

The settlement also provides for the assignment by the City of Tucson to MDWID a total of 8,858 acre feet of entitlement to Central Arizona Project (CAP) water. The entitlements will be held in trust until the installment payments are paid in full. However, in the interim, MDWID will have complete access to the CAP water covered by those entitlements, so long as they are not in default under the agreements. In addition to the installment payments described above, the agreements obligate MDWID to assume certain payment obligations in connection with the purchase of CAP water pursuant to the entitlements to CAP water being transferred to them.

The assignment of the CAP water entitlements required approval by the Central Arizona Water Conservation District (CAWCD), the Arizona Department of Water Resources (ADWR) and the United States Bureau of

Reclamation (USBR). All of these approvals have been obtained. The agreement received judicial validation in December 1998.

MDWID's CAP water payment obligation includes prorated capital charges plus operations, maintenance, and replacement (OM&R) charges on water actually ordered. The assignments, MDWID will assume all payment obligations to CAWCD for the 8,858 acre feet being assigned, including capital charges and OM&R. The amounts of these payments will vary over the lifetime of the agreements. By way of illustration, current capital charges for CAP water equal \$48 per acre foot. Current OM&R charges for CAP water equal \$63 per acre foot, if and when a subcontractor schedules the delivery of CAP water.

In the event of a default by MDWID, the defaulting district's right to a CAP entitlement will be terminated and the remaining sums owed to the City under the agreements will be accelerated by operation of a judgment.

The agreement further obligates MDWID to set their rates, fees and charges for water sales and water services at sufficient levels to create net revenues available for payment of all their bonds and all of their obligations under the settlement agreements.

Finally, the agreement gives MDWID the option to purchase treated CAP water or the treatment of CAP water in quantities and at prices to be agreed upon when the occasion arises.

This summary describes the financial aspects of the settlement agreements only. While every effort has been made to describe the financial aspects accurately, any discrepancy between this summary and the actual agreements is, of course, governed by the agreements.

Legal expenses of \$8 related to the litigation have been classified in the Statement of Revenues, Expenses and Changes in Fund Equity as operating expenses for the year ended June 30, 1999.

Other

Unvested accumulated sick leave of County employees at June 30, 1999 totaled \$19,292. This unvested accumulated sick leave is not payable to County employees upon termination of employment. Vested sick leave is accrued and payable to County employees upon termination of employment.

The County is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; medical malpractice; environmental claims; and natural disasters. Claims against the County are accounted for in the Self Insurance Trust Fund, an internal service fund. Annually, an actuarial evaluation is performed to determine the County's anticipated losses except for environmental losses. Environmental losses are based on reported claims and the County risk manager's knowledge and experience. Losses accounted for include reported and paid, reported but unpaid, and incurred but not reported. All liabilities of the Self Insurance Trust Fund except for environmental losses are reported at their present value using an expected future investment yield assumption of four percent. The County purchases commercial insurance for claims in excess of coverage provided by the Fund and for some other risks of loss. Settled claims have not exceeded insurance coverage in any of the last three fiscal years.

All funds of the County participate in the Fund. With the exception of environmental losses, payments to the Fund are based on actuarial estimates of the amounts needed to pay prior and current-year claims and to establish some reserve for catastrophe losses. That reserve was estimated to be \$500 at June 30, 1999, and is a designation of the Self Insurance Trust Fund retained earnings. Payments to the Fund for environmental losses are based on historical experience, since an actuarial basis is not available.

The claims liability of \$27,700 reported in the Fund at June 30, 1999 is based on estimates of the ultimate cost of claims that have been reported but not settled, and of claims that have been incurred but not reported. The ultimate cost of claims includes incremental claim adjustment expenses that have been allocated to specific claims, as well as salvage and subrogation. No other claim adjustment expenses have been included.

Changes in the Fund's claims liability amount for the fiscal years ended June 30, 1999 and 1998 are as follows:

	<u>1999</u>	<u>1998</u>
Claims liability balance - beginning	\$ 26,775	\$ 23,990
Current year claims and changes in estimates	10,430	8,993
Claim payments	<u>(9,505)</u>	<u>(6,208)</u>
Claims liability balance - ending	<u>\$ 27,700</u>	<u>\$ 26,775</u>