

CITY OF MILWAUKEE – WATER WORKS

Basic Financial Statements

December 31, 2016 and 2015

(With Independent Auditors' Report Thereon)

CITY OF MILWAUKEE – WATER WORKS

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INDEPENDENT AUDITORS' REPORT

Common Council
City of Milwaukee, Wisconsin – Milwaukee Water Works
Milwaukee, Wisconsin

Report on the Financial Statements

We have audited the accompanying financial statements of the City of Milwaukee – Water Works, an enterprise fund of the City of Milwaukee, Wisconsin, as of and for the years ended December 31, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the entity'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.

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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the City of Milwaukee – Water Works as of December 31, 2016 and 2015, and the respective changes in financial position and its cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis-of-Matters

As discussed in Note 1, the financial statements present of the City of Milwaukee – Water Works do not purport to, and do not, present fairly the financial position of the City of Milwaukee, Wisconsin, as of December 31, 2016 and 2015, and the changes in its financial position and cash flows, where applicable, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Management has omitted the Schedule of Funding Progress Other – Postemployment Benefits that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing 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 the financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Accounting principles generally accepted in the United States of America require that the management's discussion on pages 3 – 12 and the Pension Schedules on page 44 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.



CliftonLarsonAllen LLP

Milwaukee, Wisconsin

September 5, 2017

CITY OF MILWAUKEE – WATER WORKS

Management’s Discussion and Analysis

December 31, 2016 and 2015

(Unaudited)

The management of the City of Milwaukee – Water Works (Water Works) offers readers of the organization’s basic financial statements this narrative overview and analysis of the Water Works’ basic financial statements for the fiscal years ended December 31, 2016 and 2015. Readers are encouraged to consider the information presented here in conjunction with the financial information.

The mission of the Water Works is to provide safe, reliable, and aesthetically pleasing drinking water to the City of Milwaukee and customers in suburban communities.

Financial Highlights

Year ended December 31, 2016

- Total revenues increased by 1.4% in 2016, from \$96.9 million in 2015 to \$98.2 million in 2016.
- Total expenses increased by 2.2% in 2016, from \$72.0 million in 2015 to \$73.6 million in 2016.
- As of December 31, 2016, the Water Works’ outstanding debt consisted of \$25.5 million in revenue bonds, through a combination of the State of Wisconsin Safe Drinking Water Loan Program and a conventional revenue bond that Milwaukee Water Works issued in late 2016, and \$28.7 million in general obligation bonds for a total of \$54.2 million.
- The Water Works is an enterprise fund within the primary government of the City of Milwaukee and as such is not subject to property taxes. In place of property taxes, the Water Works contributes to the City’s tax levy by making a payment in lieu of taxes (PILOT). The PILOT was \$12.8 million in 2016 and \$12.9 million in 2015 and is reported in the accompanying Statement of Revenues, Expenses, and Changes in Fund Net Position as transfers out.

Year ended December 31, 2015

- Total revenues increased by 9.7% in 2015, from \$88.3 million in 2014 to \$96.9 million in 2015.
- Total expenses decreased by 0.7% in 2015, from \$72.5 million in 2014 to \$72.0 million in 2015.
- As of December 31, 2015, the Water Works’ outstanding debt consisted of \$16.1 million in revenue bonds through the State of Wisconsin Safe Drinking Water Loan Program, \$10.2 million in general obligation bonds and \$10.0 million in extendable municipal commercial paper for a total of \$36.3 million.
- The PILOT was \$12.9 million in 2015 and \$12.4 million in 2014.

This discussion and analysis is intended to serve as an introduction to the basic financial statements of the Water Works. The basic financial statements include two components: 1) the basic financial statements and 2) notes to the basic financial statements, which explain in more detail some of the information in the basic financial statements.

Required Basic Financial Statements

The basic financial statements report information about the Water Works using accounting methods similar to those used by private sector companies. These statements provide both long-term and short-term information about the Water Works’ overall financial status.

CITY OF MILWAUKEE – WATER WORKS

Management's Discussion and Analysis

December 31, 2016 and 2015

(Unaudited)

The statement of net position presents information on all of the Water Works' assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference reported as net position. This statement provides information about the nature and the amounts of investments in resources (assets and deferred outflows of resources) and the obligations to Water Works' creditors (liabilities and deferred inflows of resources). It provides one way to measure financial health by providing the basis for evaluating the capital structure and assessing the liquidity and financial flexibility of the Water Works. However, one will need to consider other nonfinancial factors, such as changes in economic conditions, population and industrial/commercial customer growth, and new or changed government legislation.

All of the current year's revenues and expenses are accounted for in the statement of revenues, expenses, and changes in fund net position. This statement measures the results of operations over the past year and can be used to determine whether the Water Works has successfully recovered all of its costs through user fees and other charges.

The final required financial statement is the statement of cash flows. This statement reports cash receipts, cash payments, and net changes in cash resulting from operations, capital financing and non-capital financing, and investing activities. This statement identifies sources and uses of cash, as well as the change in the cash balance during the reporting period.

CITY OF MILWAUKEE – WATER WORKS

Management’s Discussion and Analysis

December 31, 2016 and 2015

(Unaudited)

Financial Analysis of the Water Works

Statement of Net Position

A summary of assets, liabilities, and net position as of December 31, 2016, 2015, and 2014 is as follows:

Table A-1

Condensed Summary of Net Position

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Assets:			
Current assets	\$ 56,971,960	55,114,606	50,169,201
Net capital assets	454,715,271	441,968,070	428,758,744
Total assets	<u>511,687,231</u>	<u>497,082,676</u>	<u>478,927,945</u>
Deferred outflows of resources	<u>8,445,000</u>	<u>3,750,095</u>	<u>—</u>
Liabilities:			
Current liabilities	17,250,028	47,813,626	47,220,554
Noncurrent liabilities	65,695,736	31,029,345	24,806,002
Total liabilities	<u>82,945,764</u>	<u>78,842,971</u>	<u>72,026,556</u>
Deferred inflows of resources	<u>557,000</u>	<u>10,000</u>	<u>—</u>
Net Position:			
Net investment in capital assets	400,511,980	405,660,514	405,166,630
Restricted for debt service	1,229,225	1,173,915	929,903
Unrestricted net position	34,888,262	15,145,371	804,856
Total net position	<u>\$ 436,629,467</u>	<u>421,979,800</u>	<u>406,901,389</u>

Net position may, over time, serve as a useful indicator of an entity’s financial position. In the case of the Water Works, assets exceeded liabilities by \$436.6 million and \$422.0 million at December 31, 2016 and 2015, respectively, showing a 3.9% increase from 2015.

In Table A-1, it can be seen that the largest portion of the Water Works’ net position, 92% and 96% as of December 31, 2016 and 2015, respectively, reflects the net investment in capital assets (e.g., water mains, buildings, machinery, and equipment). Also, as shown in Table A-3, the Water Works’ water main system makes up approximately 53% and 55% of the capital assets as of December 31, 2016 and December 31, 2015, respectively. The Water Works uses these capital assets to provide safe, reliable, and aesthetically pleasing drinking water to its 864,000 customer base that lives in the City of Milwaukee and surrounding communities.

CITY OF MILWAUKEE – WATER WORKS

Management’s Discussion and Analysis

December 31, 2016 and 2015

(Unaudited)

The Water Works’ net investment in capital assets is reported net of related debt. The resources to repay this debt must be provided from operating and nonoperating activities as the capital assets themselves are not intended to be used to liquidate these liabilities.

Unrestricted net position of the Water Works represents current assets such as cash on hand for operation, cash held in local government investment pool, accounts receivable and inventory of materials. Unrestricted net position increased to 8.0% of total net position in 2016, up from 3.6% in 2015.

As can be seen in Table A-1, net investment in capital assets decreased by \$5.1 million and increased by \$494,000 during the years ended December 31, 2016 and 2015, respectively. The decrease in net investment in capital assets in 2016 is mainly due to a large increase in debt, from \$36.3 million in 2015 to \$54.2 million in 2016, offset by a \$12.7 million net increase in capital assets. Ramped up water main replacement program to meet the PSC’s mandate constitutes a significant portion of the increase in capital assets in 2016. The increase in net investment in capital assets in 2015 is attributable to completion and capitalization of three major capital projects for a total of approximately \$14.3 million, offset by an increase of \$12.7 million in total debt. The amounts of contributed capital were \$2.8 million in 2016 and \$1.3 million in 2015. In 2016, the Water Works received \$415,000 in local grants and in 2015 received \$951,000 and \$332,000 in federal and state capital grants respectively.

Statement of Revenues, Expenses, and Changes in Net Position

While the summary of net position (Table A-1) shows the amount of net position, as of the end of each respective year, the summary of revenues, expenses, and changes in fund net position (Table A-2) exhibits the nature and source of the changes.

CITY OF MILWAUKEE – WATER WORKS

Management’s Discussion and Analysis

December 31, 2016 and 2015

(Unaudited)

Table A-2

Condensed Summary of Revenues, Expenses, and Changes in Fund Net Position

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Operating revenue	\$ 97,849,702	96,686,959	88,012,611
Nonoperating revenue	389,231	221,756	293,795
Total revenues	<u>98,238,933</u>	<u>96,908,715</u>	<u>88,306,406</u>
Depreciation expense	18,217,743	17,485,221	16,864,383
Other operating expenses	55,229,187	54,516,209	54,769,000
Nonoperating expenses	173,225	709	907,524
Total expenses	<u>73,620,155</u>	<u>72,002,139</u>	<u>72,540,907</u>
Income before capital contributions and transfers	24,618,778	24,906,576	15,765,499
Capital contributions	2,798,060	1,276,094	383,727
Transfers to the City of Milwaukee	<u>(12,767,171)</u>	<u>(12,880,259)</u>	<u>(12,397,198)</u>
Changes in net position	14,649,667	13,302,411	3,752,028
Net position – beginning of year	<u>421,979,800</u>	<u>408,677,389</u>	<u>403,149,361</u>
Net position – end of year	\$ <u>436,629,467</u>	<u>421,979,800</u>	<u>406,901,389</u>

Year ended December 31, 2016

A review of Table A-2 shows that total revenues increased by \$1.3 million, or 1.4% in 2016 and total expenses increased by \$1.6 million, or 2.3%. These results may be explained as follows:

Revenues

- Operating revenues increased by \$1.2 million in 2016. This moderate increase in revenue reflects the impact of a 3% Simplified Rate Increase that was effective September 2016, despite a continuing trend of drop in water sales or consumption in 2016. Table A-4 shows the sale of water (in billion gallons) for the last five years. According to this table, the total sale of water to all customer classes had dropped by 3.5 billion gallons or 10.6% from 2012. The decline in sale to some customer classes may show slight fluctuations over the years but the overall trend is a decline in consumption thereby affecting operating revenue.

CITY OF MILWAUKEE – WATER WORKS

Management’s Discussion and Analysis

December 31, 2016 and 2015

(Unaudited)

- Nonoperating revenues mainly consist of rental income from antenna contracts, and also include miscellaneous fees for service and branch tapping, interest income and other revenues such as from sale of nonutility properties. Miscellaneous nonoperating revenues for 2016 increased by \$167,000 or 75.5% over 2015. This increase is the result of a loss on the sale of capital assets recognized in 2015 that decreased nonoperating revenue for that year and, by comparison, increasing that of 2016. There has been no significant change in interest income in relation to total nonoperating revenue.

Expenses

- Operating expenses, excluding depreciation, increased by 1.3% to \$55.2 million in 2016, from \$54.5 million in 2015. This was mainly due to a combination of increases in administrative and general expenses and transmission and distribution expenses and decreases in pumping and water treatment expenses. Transmission and distribution expenses increased by 10.5%, whereas administration and general expenses increased by 15.4%. Increase in transmission and distribution expenses was a net result of expenses for painting the Lincoln storage tank and lead service line replacements, offset by a decrease in water main expenses. Increase in administrative and general expenses was mainly due to pension expenses recognized in compliance with GASB 68. Pumping and treatment expenses decreased by 6.3% and 16.5% respectively. Pumping expenses decreased partly because Plants Operations implemented observing “peak” for pump operations at Texas and Howard facilities that in turn was believed to have lowered electrical charges. Treatment expenses decreased due to a decrease in cost of chemicals used in treatment and due to having Linnwood Plant to Riverside tunnel inspection done in 2015 and having no similar expenses in 2016.
- Nonoperating expenses, which is made up of mainly interest expense, increased by \$173,000 in 2016. This increase was the result of increase in debt service and related interest expense.

Year ended December 31, 2015

A review of Table A-2 shows that total revenues increased by \$8.6 million, or 9.7% in 2015 and total expenses decreased by \$539,000, or 0.7%. These results may be explained as follows:

Revenues

- Operating revenues increased by \$8.7 million in 2015. This increase in revenue reflects the full year impact of an 11.4% rate increase implemented in November 2014, despite a continuing trend of drop in water sales or consumption in 2015. Table A-4 shows the sale of water (in billion gallons) for the last five years. According to this table, the sale of water for most customer classes has consistently dropped from year to year since 2011. It should also be noted that 2015 sales represents the lowest figures for residential, public authority, and industrial customer category and total consumption. The sale of water for these three customer categories dropped by 0.6 billion gallons, whereas sale to commercial and wholesale customers increased by 0.3 billion gallons resulting in a net decrease in total water sale of 0.3 billion gallons from 2014 to 2015.

CITY OF MILWAUKEE – WATER WORKS

Management’s Discussion and Analysis

December 31, 2016 and 2015

(Unaudited)

- Miscellaneous nonoperating revenues for 2015 decreased by \$72,000 or 24.5% over 2014. This decrease is the result of a loss on the sale of capital assets and increase in other non-utility property expenses, off-set in part by increase in other revenues.

Expenses

- Operating expenses, excluding depreciation, decreased by 0.5% to \$54.5 in 2015 from \$54.8 million in 2014. This was a combination of decreases in transmission and distribution expenses and increases in administration and general expenses and water treatment expenses. Transmission and distribution expenses decreased by 10.3%, whereas administration and general expenses and treatment expenses increased by 10.6% and 8.1% respectively. Decrease in distribution expenses was mainly due to decrease in water main breaks to 430 in 2015 from 930 in 2014 and other expenses incurred in 2014 due to an extremely harsh winter. Increase in administrative and general expenses was due to installation of new AVAYA phone system for MWW Customer Service unit, increases in network support, GASB 45 OPEB expenses, and increases in Pension expenses, in part offset by a decrease in PSC expenses due to the 2014 rate case. Increase in treatment expenses was a combination of expenses related to the tunnel inspection work done from the Linnwood Plant to Riverside pumping station partially offset by a decrease in cost of chemicals
- Nonoperating expenses decreased by \$907,000 in 2015 or by 99.9%. This decrease was the result of the capitalization of the majority of interest expense to on-going capital improvement projects.

Capital Assets and Debt Administration

Capital Assets

The Water Works calculates depreciation based on composite groups of assets within a given category and the average useful life. These categories are building and improvements, transmission and distribution system, and machinery and equipment. Each group’s depreciation is then calculated using a rate authorized by the latest Public Services Commission of Wisconsin (PSC) rate order.

As of December 31, 2016, the Water Works investment in capital assets, net of accumulated depreciation, increased by \$12.7 million or 2.9% to \$454.7 million. Transmission and distribution system assets and machinery and equipment increased by \$6.6 million and \$7.7 million, respectively, and construction in progress increased by \$11.5 million. The increase in transmission and distribution system assets was mainly due to installation of water mains. The increase in machinery and equipment reflects a combination of increases in Automated Meter Reading (AMR) equipment, hydrants installed and completion of clearwell roof project at Linnwood. The increase in construction in progress was due to the ramping up of water main replacement program per PSC mandate and main replacement contracts in 2015 and 2016 that are not completed yet. There was a minor reclassification of non-utility property to utility property in the amount of \$18,100 in 2016.

CITY OF MILWAUKEE – WATER WORKS

Management’s Discussion and Analysis

December 31, 2016 and 2015

(Unaudited)

As of December 31, 2015, the Water Works investment in capital assets, net of accumulated depreciation, increased by \$13.2 million or 3.1% to \$442.0 million. Transmission and distribution system assets and machinery and equipment increased by \$5.2 million and \$15.9 million, respectively, and construction in progress increased by \$2.6 million. The increase in transmission and distribution system assets was mainly due to installation of water mains. The increase in machinery and equipment reflects a combination of increases in Automated Meter Reading (AMR) equipment, Linnwood backup power project, Linnwood ozone project and hydrants. The increase in construction in progress was due to the undertaking of several projects in 2015, offset by the completion of the projects noted above. Some of the projects that contributed to the increase were the Linnwood buried south filtered reservoir project (\$1.7 million), Lincoln Station painting project (\$1.2) and new water mains (\$9.7 million). There was no change in nonutility property from 2014.

**Table A-3
Capital Assets**

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Capital assets:			
Land	\$ 1,415,398	1,397,298	1,410,560
Buildings	28,992,766	28,514,399	29,055,664
Transmission and distribution system	381,681,201	375,130,721	369,921,899
Machinery and equipment	259,604,970	251,944,886	236,061,456
Construction in progress	37,506,698	25,993,329	23,376,435
Nonutility property	<u>4,293,160</u>	<u>4,308,994</u>	<u>4,308,994</u>
Total capital assets	713,494,193	687,289,627	664,135,008
Less accumulated depreciation	<u>(258,778,922)</u>	<u>(245,321,557)</u>	<u>(235,376,264)</u>
Net capital assets	<u>\$ 454,715,271</u>	<u>441,968,070</u>	<u>428,758,744</u>

Investment Administration

As an enterprise fund within the primary government of the City of Milwaukee, the Water Works does not have a direct investment plan. As such, cash not in use for day-to-day operation is invested through the City of Milwaukee, primarily in the State of Wisconsin’s LGIP and/or other types of investment instruments as determined by the City Treasurer. As of December 31, 2016 and 2015, the City Treasurer held cash and cash equivalents of \$18.3 million and \$16.6 million, respectively, on behalf of the Water Works that consisted of LGIP investments and cash accounts.

Debt Administration

Debt service is administered by the Public Debt Commission and can only be initiated through Council resolution with approval from the Commissioner of Public Works (or his designee, the Superintendent of Water Works).

The Water Works continues to make its regularly scheduled payments on its bonds per the amortization schedule for each bond.

CITY OF MILWAUKEE – WATER WORKS

Management’s Discussion and Analysis

December 31, 2016 and 2015

(Unaudited)

As of December 31, 2016 and 2015, the Water Works debt consisted of \$25.5 million and \$16.1 million, respectively, in revenue bonds through the State of Wisconsin Safe Drinking Water Loan program and a conventional revenue bond that the Milwaukee Water Works issued in 2016. In addition, Milwaukee Water Works had \$8.7 million and \$10.2 million, respectively, in general obligation bonds and \$20.0 million line of credit (2016) and \$10.0 million of extendable municipal commercial paper (2015) for a total indebtedness of \$54.2 million and \$36.3 million, as of December 31, 2016 and 2015, respectively.

Economic Factors

Volume of water sold decreased by 0.3 billion gallons and 0.2 billion gallons in 2016 and 2015, respectively. As shown in Table A-4, volume of water sold to industrial and public authority customer categories stayed the same, from 2015 to 2016, at 3.2 billion gallons and 1.7 billion gallons respectively. A decrease of 0.2 billion gallons was experienced in wholesale customer category in 2016. A sharper decline of 26.4% was recognized in the commercial customer category whereas there was an 18.4% increase in residential customer category. The decrease and increase in these two respective customer categories are mainly due to a reclassification of customer accounts in 2016. Some multi-family customer accounts were reclassified from commercial to residential category per a PSC mandate. It should also be noted that volume of water sold to all customers dropped by 10.6% over the last five years, including 2016. Table A-5 shows, graphically, the volume of water sold to different categories of customers over the last 20 years. As can be observed in the graph, even though there had been a continuing decline in the sale of water to all customer categories over the 20-year period, it seems to have leveled out, especially for industrial, public authority and wholesale customer categories the last three years.

Table A-4

Sale of Water

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
	(In billion of gallons)				
Customer class:					
Residential	11.6	9.8	10.1	10.3	11.0
Commercial	5.3	7.2	7.0	7.5	7.9
Industrial	3.2	3.2	3.4	3.3	3.6
Public authority	1.7	1.7	1.8	2.0	2.0
Subtotal	21.8	21.9	22.3	23.1	24.5
Wholesale	7.6	7.8	7.6	7.4	8.4
Total	29.4	29.7	29.9	30.5	32.9

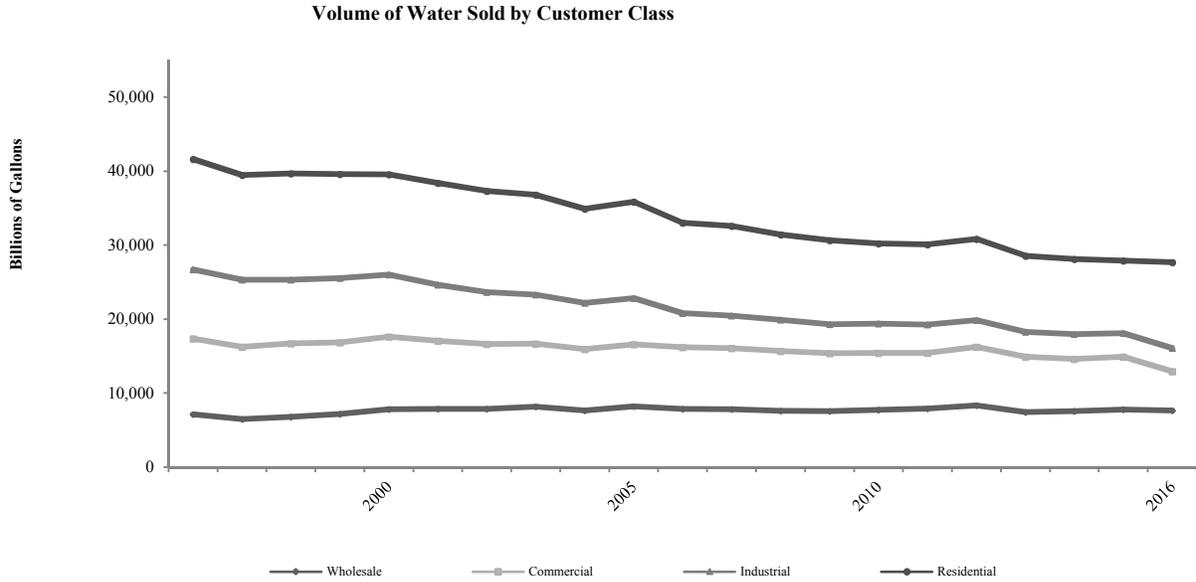
CITY OF MILWAUKEE – WATER WORKS

Management’s Discussion and Analysis

December 31, 2016 and 2015

(Unaudited)

Table A-5



Subsequent Events

The leadership of the Milwaukee Water Works changed in February 2017. Jennifer Gonda is the new Water Works Superintendent replacing Carrie Lewis who had been superintendent since 1997.

Contacting Water Works Financial Management

This financial report is designed to provide a general overview of the Water Works’ finances to its customers, creditors, and anyone who has an interest in the Water Works’ operations. If you have questions about this report or need additional information, contact the Water Works’ Superintendent, Jennifer Gonda or Water Financial Manager, Menbere W. Medhin, 841 N. Broadway, Room 409, Milwaukee, Wisconsin 53202.

CITY OF MILWAUKEE – WATER WORKS

Statements of Net Position
December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Assets:		
Current assets:		
Cash and cash equivalents	\$ 17,026,424	15,423,716
Restricted cash and cash equivalents	1,229,225	1,173,915
Accounts receivable, net	17,472,668	16,703,938
Unbilled accounts receivable	14,335,000	13,928,000
Due from other funds	1,387,460	3,891,795
Inventory of materials and supplies	3,223,998	3,132,586
Prepaid items	2,189,826	838,353
Other assets	107,359	22,303
Total current assets	<u>56,971,960</u>	<u>55,114,606</u>
Noncurrent assets:		
Water plant in service, net	413,835,442	412,444,363
Construction work in process	37,506,698	25,993,329
Other property, net	3,373,131	3,530,378
Total noncurrent assets	<u>454,715,271</u>	<u>441,968,070</u>
Total assets	<u>511,687,231</u>	<u>497,082,676</u>
Deferred outflow of resources		
Pension deferred outflows	<u>8,445,000</u>	<u>3,750,095</u>
Total deferred outflow of resources	<u>8,445,000</u>	<u>3,750,095</u>
Liabilities:		
Current liabilities:		
Accounts payable	9,157,407	9,545,806
Interest payable	152,840	135,070
Accrued wages	884,883	675,946
Compensated absences	1,154,450	1,189,006
Due to other funds	2,838,991	22,773,812
Long-term debt due within one year	3,061,457	13,493,986
Total current liabilities	<u>17,250,028</u>	<u>47,813,626</u>
Noncurrent liabilities:		
General obligation bonds payable	27,860,905	8,351,457
Revenue bonds payable	23,280,929	14,462,113
Pension obligation	7,652,000	2,147,000
Net other postemployment benefits obligation	6,901,902	6,068,775
Total noncurrent liabilities	<u>65,695,736</u>	<u>31,029,345</u>
Total liabilities	<u>82,945,764</u>	<u>78,842,971</u>
Deferred inflow of resources		
Pension deferred inflows	<u>557,000</u>	<u>10,000</u>
Total deferred inflow of resources	<u>557,000</u>	<u>10,000</u>
Net position:		
Net investment in capital assets	400,511,980	405,660,514
Restricted for debt service	1,229,225	1,173,915
Unrestricted	34,888,262	15,145,371
Total net position	<u>\$ 436,629,467</u>	<u>421,979,800</u>

See accompanying notes to basic financial statements.

CITY OF MILWAUKEE – WATER WORKS
Statements of Revenues, Expenses, and Changes in Fund Net Position
Years ended December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Operating revenues:		
Water sales	\$ 80,042,580	79,289,594
Fire protection service	8,938,360	8,723,475
Charges for shared services	5,991,652	5,797,797
Other	2,877,110	2,876,093
Total operating revenues	<u>97,849,702</u>	<u>96,686,959</u>
Operating expenses:		
Administrative and general	10,026,775	8,690,930
Billing and collection	3,028,822	2,998,506
Transmission and distribution	23,025,107	20,831,500
Water pumping	7,157,387	7,636,042
Water treatment	11,991,096	14,359,231
Depreciation	18,217,743	17,485,221
Total operating expenses	<u>73,446,930</u>	<u>72,001,430</u>
Operating income	<u>24,402,772</u>	<u>24,685,529</u>
Nonoperating revenues (expenses):		
Interest income	31,004	24,265
Interest expense	(173,225)	(709)
Miscellaneous	358,227	197,491
Total nonoperating revenues, net	<u>216,006</u>	<u>221,047</u>
Income before capital contributions and transfers	24,618,778	24,906,576
Capital contributions	2,798,060	1,276,094
Transfers out	<u>(12,767,171)</u>	<u>(12,880,259)</u>
Increase in net position	14,649,667	13,302,411
Net position – beginning of year	<u>421,979,800</u>	<u>408,677,389</u>
Net position – end of year	<u>\$ 436,629,467</u>	<u>421,979,800</u>

See accompanying notes to basic financial statements.

CITY OF MILWAUKEE – WATER WORKS
Statements of Cash Flows
Years ended December 31, 2016 and 2015

	2016	2015
Cash flows from operating activities:		
Receipts from customers and users	\$ 91,044,936	90,599,320
Receipts from interfund services provided	5,991,652	5,797,797
Payments to suppliers	(27,715,073)	(23,570,029)
Payments to employees	(22,506,191)	(21,733,594)
Payments to other funds	(22,352,761)	(16,331,032)
Net cash provided by operating activities	24,462,563	34,762,462
Cash flows from noncapital financing activities:		
Miscellaneous nonoperating revenue	358,227	197,491
Interfund transfers	(12,767,171)	(12,880,259)
Net cash used in noncapital financing activities	(12,408,944)	(12,682,768)
Cash flows from capital and related financing activities:		
Acquisition of property, plant, and equipment	(27,391,885)	(28,543,453)
Proceeds from bonds, notes, and revenue bonds	31,416,687	16,590,067
Retirement of bonds, notes, and revenue bonds	(13,493,987)	(3,845,595)
Interest paid	(957,420)	(923,292)
Net cash used in capital and related financing activities	(10,426,605)	(16,722,273)
Cash flows from investing activity:		
Interest income	31,004	24,265
Net cash provided by investing activity	31,004	24,265
Net increase in cash and cash equivalents	1,658,018	5,381,686
Cash and cash equivalents – beginning of year	16,597,631	11,215,945
Cash and cash equivalents – end of year	\$ 18,255,649	16,597,631
Cash and cash equivalents at year-end consist of:		
Unrestricted cash and cash equivalents	\$ 17,026,424	15,423,716
Restricted cash and cash equivalents	1,229,225	1,173,915
Total cash and cash equivalents	\$ 18,255,649	16,597,631

CITY OF MILWAUKEE – WATER WORKS
 Statements of Cash Flows
 Years ended December 31, 2016 and 2015

	2016	2015
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 24,402,772	24,685,529
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	18,217,743	17,485,221
Effect of changes in assets, deferred outflows of resources, liabilities, and deferred inflows of resources:		
Receivables	(1,175,731)	(626,936)
Due from/to other funds resulting from operations	(17,430,484)	(11,702,612)
Inventory of materials and supplies	(91,412)	(560,899)
Prepaid items	(1,351,472)	1,247,627
Other assets	(85,056)	(12,311)
Noncapital accounts payable	(388,400)	3,012,613
Accrued wages and compensated absences	174,381	42,033
Net pension obligations, deferred outflows and deferred inflows	1,357,095	182,905
Net other postemployment benefits obligation	833,127	1,009,292
Net cash provided by operating activities	\$ 24,462,563	34,762,462
Noncash activities:		
During the year, water mains and related property installed by others were deeded to the Water Works in the amount of	\$ 2,798,060	1,276,094
Book value of capital assets exchanged for a receivable	—	500,000

See accompanying notes to basic financial statements.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(1) Summary of Significant Accounting Policies

The City of Milwaukee – Water Works (Water Works) is an enterprise fund within the primary government of the City of Milwaukee (the City). The Water Works provides water to residents and commercial enterprises in the metropolitan Milwaukee area. The basic financial statements of the Water Works have been prepared in accordance with U.S. generally accepted accounting principles (GAAP), as prescribed by the Governmental Accounting Standards Board (GASB) modified for certain requirements of the Public Service Commission of Wisconsin (PSC). The PSC regulates rates charged to customers and other practices of the Water Works. To facilitate the understanding of data included in the basic financial statements, summarized below are the significant accounting policies:

(a) Reporting Entity

As defined by U.S. GAAP, the financial reporting entity consists of a primary government as well as its component units, which are legally separate organizations for which the elected officials of the primary government are financially accountable. Financial accountability is defined as:

- (1) Appointment of a voting majority of the component unit's board and either:
 - (a) the ability to impose will by the primary government; or
 - (b) the possibility that the component unit will provide a financial benefit to or impose a financial burden on the primary government; or
- (2) Fiscal dependency on the primary government.

Based on the application of these criteria, the Water Works has no component units and is not a component unit of any other entity. However, because the Water Works is not legally separate from the City, it is included in the basic financial statements of the City as an enterprise fund.

(b) Basis of Accounting

The accompanying basic financial statements were prepared on the accrual basis of accounting. Revenues from operations, investments, and other sources are recognized in the accounting period in which they are earned. Revenues for water sales are recognized when water services are rendered. Unbilled water services are accrued as receivables and revenue at year-end. Expenses (including depreciation and amortization) of providing services to the public are recognized in the period they are incurred.

Nonexchange transactions, in which the Water Works receives value without directly giving equal value in return, include contributions and grants. On an accrual basis, revenue from contributions and grants is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements and expenditure requirements. Timing requirements specify the year when the resources are required to be used or the fiscal year when use is first permitted. Expenditure requirements specify the year in which the resources are provided to the Water Works on a reimbursement basis.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(c) Cash Equivalents

Cash equivalents represent all highly liquid investments purchased with original maturities of three months or less, are stated at cost or amortized cost, which approximates fair value, and are invested with the City Treasurer. The City Treasurer manages a cash and investment pool to maximize return on funds while providing liquidity to meet day-to-day obligations. The Water Works' equity in the City's investment pool is considered to be a cash equivalent, since the Water Works can deposit or effectively withdraw cash at any time without prior notice or penalty.

(d) Accounts Receivable

Accounts receivable is composed of charges to customers for water services and receivables for sundry bill charges that cannot be attached to the property. The accounts receivable balance is stated net of allowance for doubtful accounts of \$665,248 and \$710,284 as of December 31, 2016 and 2015, respectively. The accounts receivable year-end balance includes actual unpaid charges. The unbilled accounts receivable balance consists of an estimate of the 2016 receivables that will be billed in the first quarter of 2017.

(e) Inventory of Materials and Supplies

Inventories of materials and supplies are stated at lower of moving average cost or market, based upon perpetual record-keeping systems and periodic cycle counts of quantities on hand.

(f) Investments

The City Treasurer is responsible for managing all of the Water Works' investments pursuant to the City's investment policy and Wisconsin Statutes. Wisconsin Statutes permit the City to invest funds not immediately needed in any of the following:

- Time deposits maturing within three years in any credit union, bank, savings bank, trust company, or savings and loan association which are authorized to transact business in the State of Wisconsin.
- Bonds or securities issued or guaranteed by the Federal government.
- Bonds or securities of any county, city, drainage district, technical college district, village, town or school district of the State of Wisconsin, as well as bonds issued by a local exposition district, a local professional baseball park district, or the University of Wisconsin Hospitals and Clinics Authority.
- Local Government Investment Pool – Investment Fund of the State of Wisconsin.
- Repurchase agreements with public depositories, if the agreement is secured by federal bonds or securities.
- Any security which matures or which may be tendered for purchase at the option of the holder within not more than seven years of the date on which it is acquired, if that security has a rating which is the highest or second highest rating category assigned by Standard & Poor's Corporation, Moody's Investors Service, Inc. or other similar nationally recognized rating

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

agency or if that security is senior to, or on a parity with, a security of the same issuer which has such a rating.

- Securities of open-end management investment companies or investment trusts (mutual funds) if the portfolio is limited to (a) bonds and securities issued by the federal government or a commission, board or other instrumentality of the federal government, (b) bonds that are guaranteed as to principal and interest by the federal government or a commission, board or other instrumentality of the federal government, and (c) repurchase agreements that are fully collateralized by these bonds or securities.

Investments, except the Local Government Investment Pool, are reported at fair value based on quoted market prices. The Local Government Investment Pool is an external investment pool administered by the State of Wisconsin. The value of the Water Works’ investment in the fund is the same as the value of the pooled shares. Although not subject to direct regulatory oversight, the fund is administered in accordance with the provisions of Section 25.50 of the Wisconsin Statutes.

(g) Capital Assets

Capital assets are defined by the Water Works as assets with an initial, individual cost of more than \$2,000 and an estimated useful life in excess of a year. Capital assets are capitalized at cost when purchased or constructed. Donated capital assets are recorded at their estimated fair value at the date of donation. Intangible assets not specifically excluded by its scope provisions will be classified as capital assets. Costs of depreciable property retired are removed from utility plant accounts and are charged to accumulated depreciation. Maintenance and repair costs are charged to operations as incurred and renewals and improvements are added to the asset accounts. Interest incurred during the construction phase is reflected in the capitalized value of the capital assets constructed, net of interest earned on the invested debt proceeds over the same period. \$775,000 and \$875,000 of interest was capitalized in 2016 or 2015, respectively. Depreciation is provided over the estimated useful lives using the straight-line method. The estimated useful lives are as follows:

Building and improvements	31 – 59 years
Transmission and distribution systems	45 – 77 years
Machinery and equipment	4 – 30 years

(h) Bond Premiums, Issuance Costs, and Deferred Amounts on Refunding

Bond premiums and deferred amounts on refunding are deferred and amortized over the life of the bonds using the effective-interest method. Bonds payable are reported net of the applicable bond premium and deferred amounts on refunding. Bond issuance costs are reported as expenses in the year incurred.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(i) Net Position

Equity is displayed in three components as follows:

Net Investment in Capital Assets – This consists of capital assets, net of accumulated depreciation, less the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

Restricted – This consists of amounts that are legally restricted by outside parties or by law through constitutional provisions or enabling legislation. When both restricted and unrestricted resources are available for use, it is the Water Works' policy to use restricted resources first, and then unrestricted resources when they are needed. The Water Works has restricted net position of \$1,229,225 and \$1,173,915 at December 31, 2016 and 2015, respectively. The restriction of net position is related to the debt service reserve requirements of the revenue bonds.

Unrestricted – This consists of net position that do not meet the definition of “restricted” or “investment in capital assets.”

(j) Vacation Benefits

Vacation benefits are recorded as expenses over the periods the benefits accrue to the employees.

(k) Sick Leave

The liability for sick leave has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included. Upon retirement, employees receive a portion of their unused sick leave, in accordance with the Code of Ordinances. Upon retirement, employees are generally entitled to payment of accumulated sick leave up to a maximum of 30 days. At December 31, 2016 and 2015, accumulated sick leave earned but not taken was approximately \$3,875,076 and \$3,885,236 respectively. Accumulated sick leave is determined on the basis of current salary rate. The Water Works has an estimated the portion of sick leave to be paid out upon retirement to be \$883,735 as of December 31, 2016. This liability has been included as part of the total liability carried on the City of Milwaukee's financial statements.

(l) Classification of Revenues and Expenses

The Water Works classifies its revenues and expenses as either operating or nonoperating.

Operating revenue includes activities that have the characteristics of exchange transactions including sales of water supplied to city, suburban, and commercial users. Nonoperating revenue includes activities that have the characteristics of nonexchange transactions, such as contributions and most Federal, State, and local grants and contracts.

Operating expenses include the costs of operating the water utility, administrative expenses, and depreciation on capital assets. All expenses not meeting this definition, including interest expense, are reported as nonoperating expenses.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(m) Taxes

Payments in lieu of property taxes are recognized as a transfer in the year billed by the City.

(n) Estimates

The preparation of basic financial statements, in conformity with U.S. generally accepted accounting principles, requires management to make estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the basic financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from this estimate.

(o) Pension

For purposes of measuring the net pension liability (asset), deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Employee Retirement System (ERS) and additions to/deductions from ERS' fiduciary net position have been determined on the same basis as they are reported by ERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

(p) New Accounting Pronouncements Implemented

In February 2015, the GASB issued Statement No. 72, *Fair value measurement and application*. This Statement addresses accounting and financial reporting issues related to fair value measurements. The definition of *fair value* is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. The City implemented this Statement beginning with the year ending December 31, 2016.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(2) Deposits and Investments

As of December 31, 2016 and 2015, the Water Works’ deposits and investments were as follows:

	<u>2016</u>	<u>2015</u>
Local Government Investment Pool	\$ 3,493,751	9,459,290
Deposits and cash on hand	<u>14,761,898</u>	<u>7,138,341</u>
Total	<u>\$ 18,255,649</u>	<u>16,597,631</u>

(a) Custodial Credit Risk – Deposits

Custodial credit risk for deposits is the risk that in the event of a financial institution failure, the Water Works’ deposits may not be returned. Per Common Council, the City Treasurer shall require collateralization of certificates of time deposit (including interest checking) at financial institutions when the total amount of such certificates of deposit with any institution exceeds the combined insured limit of \$650,000. As of December 31, 2016 and 2015, the Water Works’ deposits were not subject to custodial credit risk as they were either insured or collateralized by securities held in the pledging bank’s trust department in the City’s name.

(b) Interest Rate Risk

Interest rate risk is the risk that the fair value of the Water Works’ investments will decrease as a result of an increase in interest rates. The City’s investment policy does not explicitly limit investment maturities. However, the City manages its exposure to interest risk based on the anticipated cash flow needs of the City. The maturities for the Water Works’ deposits and investments are less than one year and are invested by the City Treasurer.

(c) Credit Risk

Credit risk is the risk that the City will not recover its investments due to the ability of the counterparty to fulfill its obligations. Wisconsin Statutes expressly limit the City to invest in certain allowable investments. The City’s investment policy generally does not further limit its investment choices. The Water Works’ investment in the Wisconsin Local Government Investment Pool is not rated by a nationally recognized rating agency.

(d) Fair Value

The Water Works uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures.

The Water Works follows an accounting standard that defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the quality of inputs used to measure fair value, and requires expanded disclosures about fair value measurements. In accordance with this standard, the Water Works has categorized its investments, based on the priority of the inputs in the valuation technique, into a three-level fair value hierarchy. The fair value hierarchy gives the highest

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

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 to measure the financial instruments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument.

Financial assets and liabilities recorded on the statement of net position are categorized based on the inputs to the valuation techniques as follows:

Level 1 – Financial assets and liabilities are valued using inputs that are unadjusted quoted prices in active markets accessible at the measurement date of identical financial assets and liabilities.

Level 2 – Financial assets and liabilities are valued based on quoted prices for similar assets, or inputs that are observable, either directly or indirectly for substantially the full term through corroboration with observable market data.

Level 3 – Financial assets and liabilities are valued using pricing inputs which are unobservable for the asset, inputs that reflect the reporting entity's own assumptions about the assumptions market participants and would use in pricing the asset.

The Water Works had no assets or liabilities that were subject to recurring fair value measurement.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(3) Capital Assets

Capital asset activity for the year ended December 31, 2016 was as follows:

	Balance December 31, 2015	Additions	Reduction	Transfers	Balance December 31, 2016
Capital assets not being depreciated:					
Land and land improvements	\$ 1,397,298			18,100	1,415,398
Nonutility property, land	654,868			(279,327)	375,541
Construction in progress	<u>25,993,329</u>	<u>31,301,061</u>	<u>(19,787,692)</u>		<u>37,506,698</u>
Total capital assets not being depreciated	<u>28,045,495</u>	<u>31,301,061</u>	<u>(19,787,692)</u>	<u>(261,227)</u>	<u>39,297,637</u>
Capital assets being depreciated					
Buildings	28,514,399	484,646	(6,279)		28,992,766
Transmission and distribution system	375,130,721	7,008,955	(458,475)		381,681,201
Machinery and equipment	251,944,886	12,294,091	(4,634,007)		259,604,970
Nonutility property	<u>3,654,126</u>	<u>2,266</u>	<u>—</u>	<u>261,227</u>	<u>3,917,619</u>
Total capital assets being depreciated	<u>659,244,132</u>	<u>19,789,958</u>	<u>(5,098,761)</u>	<u>261,227</u>	<u>674,196,556</u>
Less accumulated depreciation:					
Buildings	18,136,192	913,214	(6,279)		19,043,127
Transmission and distribution system	104,585,659	5,062,000	(457,799)		109,189,860
Machinery and equipment	121,821,090	12,101,116	(4,249,815)	(46,485)	129,625,906
Nonutility property	<u>778,616</u>	<u>141,413</u>			<u>920,029</u>
Total accumulated depreciation	\$ <u>245,321,557</u>	<u>18,217,743</u>	<u>(4,713,893)</u>	<u>(46,485)</u>	<u>258,778,922</u>
Total capital assets being depreciated, net	<u>413,922,575</u>	<u>1,572,215</u>	<u>(384,868)</u>	<u>307,712</u>	<u>415,417,634</u>
Total capital assets, net	\$ <u><u>441,968,070</u></u>	<u><u>32,873,276</u></u>	<u><u>(20,172,560)</u></u>	<u><u>46,485</u></u>	<u><u>454,715,271</u></u>

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

Capital asset activity for the year ended December 31, 2015 was as follows:

	Balance December 31, 2014	Additions	Reduction	Transfers	Balance December 31, 2015
Capital assets not being depreciated:					
Land and land improvements	\$ 1,410,560		(13,262)		1,397,298
Nonutility property, land	654,868				654,868
Construction in progress	<u>23,376,435</u>	<u>31,453,347</u>	<u>(28,836,453)</u>		<u>25,993,329</u>
Total capital assets not being depreciated	<u>25,441,863</u>	<u>31,453,347</u>	<u>(28,849,715)</u>	—	<u>28,045,495</u>
Capital assets being depreciated					
Buildings	29,055,664	1,463,469	(2,004,734)		28,514,399
Transmission and distribution system	369,921,899	5,488,816	(279,994)		375,130,721
Machinery and equipment	236,061,456	21,884,168	(6,000,738)		251,944,886
Nonutility property	<u>3,654,126</u>	—	—		<u>3,654,126</u>
Total capital assets being depreciated	<u>638,693,145</u>	<u>28,836,453</u>	<u>(8,285,466)</u>	—	<u>659,244,132</u>
Less accumulated depreciation:					
Buildings	18,668,237	911,637	(1,443,682)		18,136,192
Transmission and distribution system	99,879,165	4,993,622	(287,128)		104,585,659
Machinery and equipment	116,189,392	11,579,962	(5,948,264)		121,821,090
Nonutility property	<u>639,470</u>	<u>139,146</u>			<u>778,616</u>
Total accumulated depreciation	\$ <u>235,376,264</u>	<u>17,624,367</u>	<u>(7,679,074)</u>	—	<u>245,321,557</u>
Total capital assets being depreciated, net	<u>403,316,881</u>	<u>11,212,086</u>	<u>(606,392)</u>	—	<u>413,922,575</u>
Total capital assets, net	\$ <u><u>428,758,744</u></u>	<u><u>42,665,433</u></u>	<u><u>(29,456,107)</u></u>	—	<u><u>441,968,070</u></u>

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(4) Long-Term Obligations

(a) Changes in Long-Term Obligations

Changes in long-term obligations for the year ended December 31, 2016 were as follows:

	Balance December 31, 2015	Additions	Deletions	Balance December 31, 2016	Due within one year
General obligation bonds	\$ 10,158,460		(1,816,828)	8,341,632	856,010
Revolving Note	—	20,000,000		20,000,000	
Extendable municipal commercial paper	10,000,000	—	(10,000,000)	—	—
Unamortized premiums	—	392,424	(17,141)	375,283	—
Deferred amount on refundings	9,825	—	(9,825)	—	—
Revenue bonds	16,139,271	11,024,263	(1,677,159)	25,486,376	2,205,447
Other postemployment benefits	6,068,775	833,127	—	6,901,902	—
Total	\$ <u>42,376,331</u>	<u>32,249,814</u>	<u>(13,520,953)</u>	<u>61,105,193</u>	<u>3,061,457</u>

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

Changes in long-term obligations for the year ended December 31, 2015 were as follows:

	Balance December 31, 2014	Additions	Deletions	Balance December 31, 2015	Due within one year
General obligation bonds	\$ 12,669,849		(2,511,389)	10,158,460	1,816,828
Extendable municipal commercial paper	—	10,000,000	—	10,000,000	10,000,000
Unamortized premiums Deferred amount on refundings	38,854		(29,029)	9,825	
Revenue bonds	10,883,411	6,590,067	(1,334,206)	16,139,271	1,677,158
Other postemployment benefits	5,059,483	1,009,292	—	6,068,775	—
Total	\$ 28,651,597	17,599,359	(3,874,624)	42,376,331	13,493,986

(b) General Obligation Bonds

The City issues general obligation bonds to provide funds for the acquisition and construction of the water plant and related equipment (water system). General obligation bonds are secured by the full faith and unlimited taxing power of the City. The bonds for the Water Works will be retired by revenues from water services or, if the revenues are not sufficient, by future tax levies. The original amount of general obligation bonds issued in years prior to 2016 was \$43,604,015.

(c) Extendable Municipal Commercial Paper

During 2016, the City retired \$10,000,000 of extendable municipal commercial paper for the Water Works which was issued in 2015 and used to finance capital improvements of the water system.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

General obligation bonds outstanding at December 31, 2016 and 2015 were as follows:

Series	Maturity	Interest rates	Original	Principal	
				Balance at December 31 2016	2015
Refunding E	2016 to 2019	4.50% to 5.00%	\$ 3,125,658	66,632	125,459
Refunding C, D, F, G, J, & K	2016 to 2016	5.00% to 5.25%	17,953,357	—	923,001
2009 N1	2016 to 2019	3.00% to 5.00%	150,000	45,000	60,000
2009 B2	2020 to 2024	4.00% to 5.00%	75,000	75,000	75,000
2010-N1	2016 to 2020	2.50% to 5.00%	450,000	180,000	225,000
2010-B5	2021 to 2025	1.50% to 5.00%	225,000	225,000	225,000
2011-N3	2016 to 2021	4.00% to 5.00%	7,750,000	3,875,000	4,650,000
2011-B4	2021 to 2026	4.00% to 5.00%	3,875,000	3,875,000	3,875,000
2015-C6	2016	0.18%	10,000,000	—	10,000,000
2016-N9	2017	0.7375%	20,000,000	20,000,000	—
Total			\$ 63,604,015	28,341,632	20,158,460

(d) General Obligation Revolving Note

In November 2016, The City drew \$20,000,000 for Milwaukee Water Works use on a revolving note, Series 2016 N9, to pay for water system improvements. The interest rate is at a fluctuating rate per annum equal to the Index Rate. The note is automatically extended for a period of 18 months beyond its maturity date of December 1, 2017.

(e) Revenue Bonds

In December 1998, Water Works issued a revenue bond, in the amount of \$19,358,172, to the State of Wisconsin Safe Drinking Water Loan Program. This bond supports loans to the Water Works for water quality capital projects, or reimbursement for capital expenditures related to water quality, up to the face value of the bond. The revenue bond borrowing authority was closed in 2004, and the final loan amount was \$17,559,378. Loan covenants provide for the monthly escrow of revenues to repay the debt plus interest. Regardless of loan proceeds disbursement, the final maturity of the revenue bonds is May 1, 2018.

In December 2013, Water Works issued a revenue bond, in the amount of \$7,823,139, to the State of Wisconsin Safe Drinking Water Loan Program. This bond supports loans to the Water Works for specific Water Works capital projects, or reimbursement for capital expenditures related to those Water Works specific capital projects, up to the face value of the bond. The revenue bond borrowing authority was closed in 2015, and the final loan amount was \$6,221,748. Loan covenants provide for the monthly escrow of revenues to repay the debt plus interest. Regardless of loan proceeds disbursement, the final maturity of the revenue bonds is May 1, 2033.

In October 2014, Water Works issued a revenue bond, in the amount of \$8,548,447, to the State of Wisconsin Safe Drinking Water Loan Program. This bond supports loans to the Water Works for specific Water Works capital projects, or reimbursement for capital expenditures related to those Water Works specific capital projects, up to the face value of the bond. Loan covenants provide for the

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

monthly escrow of revenues to repay the debt plus interest. Regardless of loan proceeds disbursement, the final maturity of the revenue bonds is May 1, 2034.

In December 2016, Water Works issued water system revenue bonds, Series 2016 W10, in the amount of \$10,000,000. These bonds are for the purpose of financing the costs of improvements to the City’s Water Works System. The final maturity of the revenue bonds is December 1, 2036.

Revenue bonds outstanding at December 31, 2016 and 2015 were as follows:

Series	Maturity	Interest rates	Original	Principal	
				Balance at December 31	
				2016	2015
SDW Bond 4851-02	2016 to 2018	2.64%	\$ 17,559,378	2,283,493	3,381,380
SDW Bond 4851-08	2016 to 2033	1.93	6,221,748	5,466,000	5,735,650
SDW Bond 4851-23	2016 to 2034	1.93	8,046,504	7,736,883	7,022,241
Series 2016 W10	2017 to 2036	4.00	10,000,000	10,000,000	—
Total			\$ 41,827,630	25,486,376	16,139,271

(f) Debt Service Requirements

The maturities of the outstanding principal and related interest requirements as of December 31, 2016 are as follows:

Year:	General obligation bonds		Revenue bonds	
	Principal	Interest	Principal	Interest
2017	\$ 856,010	542,807	2,205,447	672,132
2018	857,211	500,126	2,242,489	623,928
2019	20,858,411	383,560	1,103,398	574,136
2020	835,000	267,475	1,121,168	544,680
2021	835,000	225,725	1,139,184	520,351
2022 – 2026	4,100,000	505,675	5,985,106	2,119,807
2027 – 2031	—	—	6,570,217	1,241,925
2032 – 2036	—	—	5,119,367	353,404
Total	\$ 28,341,632	2,425,368	25,486,376	6,650,363

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Notes to Basic Financial Statements

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(5) Revenue Bond Debt Covenants

	<u>Gross revenues</u>	<u>Debt coverage expenses</u>	<u>Net revenue available for debt service</u>	<u>Debt service requirements</u>			<u>Coverage</u>
				<u>Principal</u>	<u>Interest</u>	<u>Total</u>	
Fiscal year:							
2015	96,711,224	67,213,563	29,497,661	1,677,159	314,790	1,991,949	14.81
2016	97,880,706	67,996,358	29,884,348	2,205,447	672,132	2,877,579	10.39

Gross revenues are defined as total revenues plus interest income. Debt coverage expenses are defined as total operating expenses, including payment in lieu of taxes (PILOT), minus depreciation.

The revenue bonds debt service coverage ratio requirement is the greater of 1.1 or the highest debt service coverage ratio with respect to any other debt obligations payable from the revenues of the water system.

At December 31, 2016 and 2015, there were no other debt obligations payable from the revenues of the water system.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

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(6) Retirement Plan and Other Postemployment Benefits

(a) Pension Benefits

Plan Description - The following brief description of the more common provisions of the Employees' Retirement System of the City of Milwaukee (the Retirement System or ERS) is provided for financial statement purposes only. The provisions described reflect changes to the Retirement System enacted in 2000 as part of what is known as the Global Pension Settlement (GPS). GPS increased benefits to all members who consented to the settlement in exchange for allowing the City to make certain changes in plan administration, including allowing the use of Retirement System assets to pay for all costs to administer the Retirement System.

The Water Works makes contributions to the Employees' Retirement System of the City of Milwaukee (the Retirement System), a cost-sharing multiple-employer defined benefit pension plan, on behalf of all eligible City employees. The Retirement System provides retirement, disability, and death benefits to plan members and beneficiaries. The City Charter assigns the authority to establish and amend benefit provisions. The System issues a publicly available financial report that includes financial statements and required supplementary information for the System. That report may be obtained by writing to the Employees' Retirement System of the City of Milwaukee, 789 North Water Street, Suite 300, Milwaukee, WI 53202.

Funding Policy – Plan members are required to contribute, or have contributed on their behalf, a percentage of their annual earnable compensation equal to 5.5%, 7.0%, 7.0%, and 7.0% for general City employees, police officers, firefighters, and elected officials, respectively. New hires who are not sworn police/fire must pay 1.6% of pensionable earnings for eight years to fund the cost of benefit escalators due to the Global Pension Settlement. The Water Works is required to contribute the actuarially determined amount. The City of Milwaukee Charter assigns the authority to establish and amend contribution requirements.

Long-term Expected Rate of Return on Plan Assets –The long-term expected rate of return on the pension plan investments was determined based on the results of an experience review performed by Buck Consultants. The results of the experience review were presented to the Board by Buck Consultants at the Board's December, 2012 Meeting and adopted at the same meeting. The rate of return assumption was based on the Retirement System's target asset allocation. In the experience review, Buck Consultants developed best estimate ranges of expected future real rates of return (net of inflation) for the portfolio, based on the expected returns of each major asset class and their weights in the portfolio. Buck used an econometric model that forecasts a variety of economic environments and then calculates asset class returns based on functional relationships between the economic variables and the asset classes. Expected investment expenses were subtracted and expected inflation was added to arrive at the long term expected nominal return. A value for the expected long term expected return was selected for the portfolio such that there was a better than 50% likelihood of the emerging returns exceeding the expected return.

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December 31, 2016 and 2015

Best estimates of arithmetic real rates of return (net of inflation) for each major asset class included in the Retirement System’s target asset allocation as of December 31, 2015, are listed in the table below:

<u>Asset Class</u>	<u>Policy</u>	<u>Actual</u>	<u>Long-term Expected Rate of Return</u>
Domestic Equity	25.00%	28.70%	9.22%
International Equity	20.00%	21.40%	7.14%
Global Equity	10.00%	7.03%	8.00%
Fixed Income	24.00%	24.14%	1.41%
Cash	1.00%	0.84%	0.87%
Real Estate	7.00%	8.38%	6.91%
Real Assets	3.00%	0.00%	5.45%
Private Equity	5.00%	3.84%	12.40%
Absolute Return	5.00%	5.67%	4.68%
	<u>100.0%</u>	<u>100.0%</u>	

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Rate of Return – For the year ended December 31, 2015, the annual money-weighted rate of return, net of investment expense is shown below. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested.

Annual money-weighted rate of return,	<u>2015</u>
Net of investment expense	0.63%

Actuarial Assumptions – The last actuarial valuation was performed as of January 1, 2015, and the amounts were used to roll-forward the total pension liability to the plan’s year-end December 31, 2015, and was determined using the following actuarial assumptions, applied to all prior periods included in the measurement:

Valuation Date	January 1, 2015
Actuarial Cost Method:	Entry Age Normal - Level Percentage of Pay
Amortization Method	For pension expense; the difference between expected and actual liability experience and changes of assumptions are amortized over the average of the expected remaining service lives of all members. The differences between projected and actual earnings are amortized over a closed period of five years.
Asset Valuation Method:	Market Value
Actuarial Assumptions:	
Investment Rate of Return:	8.25% for calendar years through 2017, and 8.50% beginning with calendar year 2018.
Projected Salary Increases	General City (including Water Works) 3.0% - 7.5%
Inflation Assumption:	3.00%
Cost of Living Adjustments:	Vary by Employee Group as explained in summary of plan provisions.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

Sensitivity of the net pension liability (asset) to changes in the discount rate – The following presents the Water Works’ net pension liability (asset) calculated using the discount rate of 8.50%, as well as what the Water Works’ net pension liability (asset) would be if it were calculated using a discount rate that is 1-percentage-point lower (7.50%) or 1-percentage-point higher (9.50%) than the current rate as of December 31, 2016:

	1% Decrease to Discount Rate (7.50%)	Current Discount Rate (8.50%)	1% Increase to Discount Rate (9.50%)
Water Works' net pension liability (asset)	\$ 17,986,128	\$ 7,652,000	\$ (1,061,389)

The following presents the Water Works’ net pension liability (asset) calculated using the discount rate of 8.49%, as well as what the Water Works’ net pension liability (asset) would be if it were calculated using a discount rate that is 1-percentage-point lower (7.49%) or 1-percentage-point higher (9.49%) than the current rate as of December 31, 2015:

	1% Decrease to Discount Rate (7.49%)	Current Discount Rate (8.49%)	1% Increase to Discount Rate (9.49%)
Water Works' net pension liability (asset)	\$ 12,787,000	\$ 2,147,000	\$ (6,816,000)

Schedule of Employer Allocations – The Employer Allocation Percentage is based on the employers required contribution compared to the required contribution for all employers. The Employer Allocation Percentage is rounded to seven decimal places.

Schedule of Pension Amounts – The employer’s proportionate share of the Collective Net Pension Liability, Deferred Outflows of Resources, Deferred Inflows of Resources, and Total Employer Pension Expense (Income) is based on the Employer Allocation Percentage.

The Collective Deferred Inflows and Outflows of Resources due to liabilities are amortized over the Average Expected Service Lives of all Employees of 4.20 years. The Collective Deferred Inflows and Outflows of Resources due to the net difference between projected and actual earnings on pension plan investments are amortized over 5 years.

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Notes to Basic Financial Statements

December 31, 2016 and 2015

The Water Works portion of the Collective Deferred Inflows and Outflows of Resources to be recognized in the Future Pension Expense for the year ended December 31, 2016 are as follows:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>	<u>Net Outflows of Resources</u>
Differences between expected and actual experience	\$ 90,000	\$ (416,000)	\$ (326,000)
Changes in assumptions	—	(141,000)	(141,000)
Contributions made subsequent to measurement date	1,314,000	—	1,314,000
Net differences between projected and actual earnings on pension plan investments	<u>7,041,000</u>	<u>—</u>	<u>7,041,000</u>
 Total	 <u>\$ 8,445,000</u>	 <u>\$ (557,000)</u>	 <u>\$ 7,888,000</u>

The Water Works portion of the Collective Deferred Inflows and Outflows of Resources to be recognized in the Future Pension Expense for the year ended December 31, 2015 are as follows:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>	<u>Net Outflows of Resources</u>
Differences between expected and actual experience	\$ —	\$ (10,000)	\$ (10,000)
Changes in assumptions	—	—	—
Contributions made subsequent to measurement date	1,333,095	—	1,333,095
Net differences between projected and actual earnings on pension plan investments	<u>2,417,000</u>	<u>—</u>	<u>2,417,000</u>
 Total	 <u>\$ 3,750,095</u>	 <u>\$ (10,000)</u>	 <u>\$ 3,740,095</u>

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

\$1,314,000 reported as deferred outflows resulting from the ERS employer’s contributions made subsequent to the measurement date and will be recognized as a reduction of the net pension liability in the subsequent year. Other Deferred Outflows and Inflows of Resources to be recognized in the Future Pension Expense are as follows:

<u>Year Ended December 31:</u>	<u>Net Deferred Outflows of Resources</u>
2017	\$ 1,761,200
2018	1,761,200
2019	1,761,200
2020	1,180,200
2021	<u>110,200</u>
Total	<u>\$ 6,574,000</u>

The Water Works portion of the Collective Pension Expense and proportional share is determined as follows, for the year ended December 31:

	<u>2016</u>	<u>2015</u>
Service Cost	\$ 1,283,000	\$ 1,319,000
Interest cost on total pension liability	7,621,000	7,756,000
Projected earnings on plan investments	(7,258,000)	(7,544,000)
Contributions - Member	(902,000)	(826,000)
Administrative Expense	176,000	205,000
Plan Changes	-	-
Changes in assumptions	(23,000)	-
Differences between expected and actual liability experience	(130,000)	-
Difference between projected and actual earnings	1,324,000	604,000
Deferred Outflows	581,000	
Change in proportional share	<u>(21,000)</u>	<u>2,000</u>
Total Pension Expense	<u>\$ 2,652,000</u>	<u>\$ 1,516,000</u>

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(b) Other Postemployment Benefits

The City provides other postemployment benefits (OPEB) to its retirees for health and life insurance.

Plan Description – The City provides a single-employer defined benefit healthcare plan and life insurance administered by both the City and Milwaukee’s Employee Retirement System (MERS). The City provides medical insurance benefits for substantially all retirees in accordance with terms set forth in labor contracts or by Common Council resolution. Retirees are eligible to enroll in any of the group plans offered by the City. Aside from the basic plan, this includes a Health Maintenance Organization (HMO) plan currently offered to active employees. The City provides full health insurance coverage to general City employees who retire at age 55, but less than age 65, with 30 years of creditable service or age 60, but less than age 65, with 15 years of creditable service until the age of 65. Management employees retiring beginning in 2004 at age 55, but less than 65, pay a portion of health insurance the same as active management employees. In accordance with a “percentage formula” as provided in labor agreements, the City provides between 65% and 100% of the cost of the basic plan coverage for firefighters and police officers who retire with 25 years of creditable service and having attained at least the age of 52 but less than 60. Upon reaching the age of 60 but prior to the age of 65, the City provides full health insurance coverage for firefighters and police officers with single enrollment status. The City contribution for firefighters and police officers between the ages of 60 and 65 with family enrollment status is the greatest of 100% of the cost of single enrollment in the basic plan or an amount determined using the “percentage formula.” The “percentage formula” used to determine the City contribution in the labor agreements is based on the amount of unused sick leave at retirement.

After attaining the age of 65 and having completed a minimum of 15 years of creditable service, all retirees are eligible to enroll in a “subsidized plan” for medical insurance. Under this plan, the City contributes 25% of the base rate toward retirees enrolled in the basic plan, while the retiree pays 75% of the base rate and 100% of the major medical rate. For those retirees enrolled in an HMO, the City contributes a 25% subsidy of the applicable HMO premium.

In addition to medical insurance, the City allows its employees to continue life insurance coverage under the Group Life Insurance Plan offered to active employees in accordance with Section 350-25 of the Code of Ordinances. The base amount of coverage for general City employees is equal to the employee’s annual basic salary to the next higher thousand dollars. The base amount of coverage for firefighters and police officers is equal to one and one-half the employee’s annual basic salary to the next higher thousand dollars.

General City employees retiring at age 55 or older with 20 years of service or at age 60 regardless of years of service and covered under the group life insurance plan at retirement are eligible to continue coverage at the level on the date prior to their date of retirement. Firefighters and police officers retiring at age 52 or older with 20 years of service or at age 57 regardless of years of service and covered under the group life insurance plan at retirement are eligible to continue coverage up to their base amount of coverage on the date prior to their date of retirement. Prior to age 65, all retirees are required to pay the full premium rates as established by the insurance carrier, less an adjustment for estimated dividends. The rates established are group rates applied consistently to all employees, without regard to age or health. Upon reaching the age of 65, those retirees still part of the group life plan have their

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

coverage reduced in accordance with the reduction schedule in effect on their last day physically at work, with the City assuming all future premiums.

Funding Policy – The contribution of plan members and the Water Works is established and may be amended by the City. The required contribution for medical and life insurance for retirees is based on pay-as-you-go financing. Medical benefits provided through the basic healthcare plan are self-insured. For 2016, the Water Works paid approximately \$1,440,232 and \$24,000, respectively, toward medical and life insurance for retirees. For 2015, the Water Works paid approximately \$1,075,997 and \$24,000, respectively, toward medical and life insurance for retirees.

Annual OPEB Cost and Net OPEB Obligation – The Water Works’ annual OPEB cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years.

The following table shows the components of the Water Works’ annual OPEB cost for the year, the amount actually contributed to the plan (pay-as-you-go basis), and the changes in the Water Works’ net OPEB obligation for the years ended December 31, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Annual required contribution (ARC)	\$ 2,272,370	2,089,725
Interest on net OPEB obligation	266,908	209,026
Adjustment to ARC	<u>(241,918)</u>	<u>(189,462)</u>
Annual OPEB cost	2,297,359	2,109,289
Contributions made	<u>1,464,232</u>	<u>1,099,997</u>
Increase in net OPEB obligation	(833,127)	(1,009,292)
Net OPEB obligation at beginning of year	<u>(6,068,775)</u>	<u>(5,059,483)</u>
Net OPEB obligation at end of year	<u>\$ (6,901,902)</u>	<u>(6,068,775)</u>

The Water Works annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2016, 2015 and 2014 were as follows:

	<u>Employer contribution</u>			<u>Net OPEB obligation</u>
	<u>Annual OPEB cost</u>	<u>Percentage contributed</u>		
Year ended December 31:				
2016	\$ 2,297,359	63.7%	\$	6,901,902
2015	2,109,289	52.2		6,068,775
2014	1,983,096	79.8		5,059,483

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

Funded Status and Funding Progress – As of January 1, 2015, the most recent actuarial valuation date, the actuarial accrued liability for benefits related to all City employees was \$975,695,600 and the actuarial value of assets was zero, resulting in an unfunded actuarial accrued liability (UAAL) of \$975,695,600. Of this amount, it was estimated that 8.5% is attributable to Water Works. The covered payroll (annual payroll of all active City employees covered by the plan) was \$416,803,039 and the ratio of the UAAL to the covered payroll was 234.0%. The covered payroll for Water Works employees was \$15,857,186.

Actuarial valuations of an ongoing plan involve estimates of value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend amounts determined regarding the funded status of the plan, and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations, and new estimates are made about the future.

Actuarial Methods and Assumptions – The retiree healthcare valuation was based on the projected unit credit (PUC) cost method. The PUC method produces an explicit normal cost and actuarial accrued liability. The normal cost and actuarial accrued liability are directly proportional to the employee's service. That is, the normal cost equals the present value of future benefits divided by projected service at retirement, and the actuarial accrued liability equals the present value of benefits multiplied by the ratio of service at valuation date to projected service at retirement. Depending on the demographic characteristics of the current group and new entrants in the future, this method could produce stable annual costs, in the aggregate, when expressed as a percentage of pay.

The OPEB valuation uses a discount rate assumption of 4.5% based on the City's projected short-term investment rate of return. The healthcare cost trends rate is 8.0% initially, and reduced by decrements to the ultimate rate of 4.5% after 10 years. The actuarial assumption for wage inflation is 3.0%. The amortization of the unfunded actuarial accrued liability is based on a level percentage of pay over a 30-year open amortization period.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(7) Related-Party Transactions

A summary of significant revenue and expense transactions between the City and Water Works for 2016 and 2015 is shown below:

	<u>2016</u>	<u>2015</u>
Revenues (receipts from the City) – water consumption	\$ 565,328	571,158
Transfer from Parking Fund - Lincoln Yards Installment	27,229	27,229
Transfer from General Fund - Kinnickinnic Shop Installment	462,500	37,500
Total Revenues	<u>1,055,057</u>	<u>635,887</u>
Expenses (payments to the City):		
Payment in lieu of taxes and other transfers	\$ 12,767,171	12,880,259
Employee fringe benefits	7,178,751	7,075,924
Administrative services	869,004	926,730
Electrical equipment maintenance	602,154	701,092
Motor vehicle usage and maintenance	879,630	1,013,602
Street repairs	3,550,323	4,311,392
All other services	5,966,278	6,203,492
Total payments to the City	<u>\$ 31,813,311</u>	<u>33,112,491</u>

The Water Works also acts as a billing and collection agent for sewer and other municipal charges and is reimbursed for costs incurred in providing such billing services.

The City purchases the delinquent water and sewer accounts receivables of the Water Works at the unpaid amounts. Any subsequent uncollectible accounts are absorbed by the City.

The Water Works has an annual maximum contingent liability of \$200,000 for general liability claims. Claims in excess of this amount, if any, are the liability of the City.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(8) Regulatory Agency

PSC reporting requirements and the timing of the reports give rise to differences between revenues and expenses that are included in the PSC reports and these basic financial statements. The major categories of these differences are as follows: (1) the PSC recognizes the amortization of Contributions in Aid of Construction (CIAC) deferred credits over a 20-year period, (2) the PSC has elected to retain reporting pension related expense under the funding method, rather than the actuarial method required by GASB standards, and (3) some expenses are recognized in different years due to the timing of the PSC report and this report.

The effect of such differences on net income is as follows for the years ended December 31, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
	(In thousands)	(In thousands)
Increase in net assets as shown in accompanying financial statements	\$ 14,650	13,302
Amortization of deferred credits resulting from Contributions in Aid of Construction (CIAC) reclassification	811	811
Donated Property	—	121
OPEB, Adjust PSC Estimate to Actual Amount	—	609
Pension, difference between GASB and PSC reporting	19	183
Misc. debits to revenue	<u>31</u>	<u>—</u>
Net income as shown on PSC reports	<u>\$ 15,511</u>	<u>15,026</u>

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(9) Commitments and Contingencies

The Water Works is generally committed under the terms of various contracts for construction of improvements and additions to the Water Works' system. Contract terms provide for partial payments as construction progresses with specified retention to assure full contract compliance. Open commitments on such contracts as of December 31, 2016 totaled \$5,705,502.

The Water Works is exposed to various risks of loss related to torts, theft of, damage to, and destruction of assets; errors and omissions; injuries to employee or natural disaster. These risks are monitored and evaluated by the City of Milwaukee for all aspect of the City's operations, including the Water Works. With certain exceptions, it is not the policy of the City to purchase commercial insurance for the risks of losses to which it is exposed. Instead, the City believes it is more economical to manage its risks internally and set aside funds as needed for reasonably estimated current claim settlements and unfavorable judgements through annual appropriations and supplemental appropriations. The liabilities are recorded in the City's government-wide financial statements and are not separately determinable for the Water Works.

CITY OF MILWAUKEE – WATER WORKS

Notes to Basic Financial Statements

December 31, 2016 and 2015

(10) Transfers and Interfund Balances

At December 31, 2016 and 2015, the Water Works has recorded a due from other funds of \$1,387,460 and \$3,891,795, respectively, which represents the amount owed to the Water Works as a result of regular advance and reimbursement activities. At December 31, 2016 and 2015, the Water Works has recorded a due to the City (General and Sewer Funds) of \$2,838,991 and \$22,773,812 respectively, for sewer maintenance and other municipal fees collected by the Water Works.

The Water Works transfers funds to the City (general fund) for PILOT. In 2016 and 2015, the PILOT transfers to the City were \$12,767,171 and \$12,880,259, respectively.

CITY OF MILWAUKEE – WATER WORKS

Required Supplementary Information

December 31, 2016 and 2015

Schedule of Water Works Proportionate Share of the Net Pension Liability (Asset)
City of Milwaukee Employee Retirement System
Last 10 Measurement Periods*

	Year Ended December 31,	
	2015	2014
Water Works' proportion of the net pension liability (asset)	1.8194712%	1.8920740%
Water Works' proportionate share of the net pension liability (asset)	\$ 7,652,000	\$ 2,147,000
Water Works' covered - employee payroll	\$ 9,748,763	\$ 10,027,000
Plan fiduciary net position as a percentage of the total pension liability (asset)	92.41%	97.76%

Schedule of City of Milwaukee – Water Works Contributions
City of Milwaukee Employee Retirement System
Last 10 Fiscal Years*

	2016	2015
Contractually required contributions	\$ 1,314,000	\$ 1,464,233
Contributions in relation to the contractually required contributions	\$ (1,314,000)	\$ (1,464,233)
Contribution deficiency (excess)	\$ —	\$ —
Water Works' covered - employee payroll	\$ 10,126,658	\$ 9,748,763
Contributions as a percentage of covered - employee payroll	12.98%	15.02%

*Additional years' information will be displayed as it becomes available

Notes to the Required Supplementary Information
For the year ended December 31, 2016

Changes of benefit terms. There were no changes of benefit terms for any participating employer in ERS.

Changes of assumptions. There were no changes in the assumptions.