



REPORT OF INDEPENDENT AUDITORS AND FINANCIAL
STATEMENTS WITH REQUIRED SUPPLEMENTARY
INFORMATION AND OTHER INFORMATION

**SEATTLE PUBLIC UTILITIES –
DRAINAGE AND WASTEWATER FUND
(AN ENTERPRISE FUND OF THE CITY OF SEATTLE)**

December 31, 2019 and 2018

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Report of Independent Auditors

To the Director of Seattle Public Utilities
Drainage and Wastewater Fund
Seattle, Washington

Report on the Financial Statements

We have audited the accompanying financial statements of Seattle Public Utilities – Drainage and Wastewater Fund (the Fund), which comprise the statements of net position as of December 31, 2019 and 2018, and the related statements of revenues, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management’s Responsibility for the Financial Statements

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

Auditor’s Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity’s preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of Seattle Public Utilities – Drainage and Wastewater Fund as of December 31, 2019 and 2018, and the changes in net position and cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis, schedule of Seattle Public Utilities' proportionate share of the net pension liability, schedule of Seattle Public Utilities' contributions, and schedule of Seattle Public Utilities' proportionate share of the OPEB liability and related ratios, as listed in the table of contents, be presented to supplement the financial statements. This 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 financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the basic financial statements as a whole. The other information is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 30, 2020, on our consideration of the Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Fund's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Fund's internal control over financial reporting and compliance.

MossAdams LLP

Seattle, Washington
April 30, 2020

Seattle Public Utilities – Drainage and Wastewater Fund (An Enterprise Fund of the City of Seattle) Management’s Discussion and Analysis

As management of Seattle Public Utilities (SPU), a department of the City of Seattle (the City), we offer readers of SPU’s financial statements this narrative overview and analysis of the financial activities of the Drainage and Wastewater Fund (the Fund) for the fiscal years ended December 31, 2019 and 2018. The revenues, expenses, assets, deferred outflows of resources, and liabilities of the City of Seattle’s drainage and wastewater system are recorded in the Fund, the functions of which are primarily supported by user fees and charges to customers. The financial situation of other aspects of Seattle City government, including other utility services and general government operations, are reported elsewhere.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Fund’s financial statements. The financial statements include Management’s Discussion and Analysis and basic financial statements with accompanying notes.

Basic financial statements – The basic financial statements of the Fund report information similar to the presentation used by private sector companies. These statements offer short-term and long-term financial information about its activities. The basic financial statements begin on page 12 of this report and are comprised of three components: (1) statements of net position, (2) statements of revenues, expenses, and changes in net position, and (3) statements of cash flows.

The statements of net position present information, as of December 31, 2019 and 2018, on all of the Fund’s assets, deferred outflows of resources, liabilities, and deferred inflows of resources. The difference between assets combined with deferred outflows of resources and liabilities combined with deferred inflows of resources is reported as net position. They also provide information about the nature and amounts of investments in resources (assets and deferred outflows of resources), obligations to the Fund’s creditors (liabilities and deferred inflows of resources), and provide the basis for assessing the liquidity and financial flexibility of the Fund.

The statements of revenues, expenses, and changes in net position present changes in the Fund’s net position for the years ended December 31, 2019 and 2018. All changes in net position are reported when the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. These statements reflect the results of the Fund’s operations for the years identified to provide information about the Fund’s credit worthiness and its ability to successfully recover all its costs through service fees and other charges.

The statements of cash flows are required to provide information about the Fund’s cash receipts and cash payments during the years ended December 31, 2019 and 2018. To provide answers to questions about sources, uses, and impacts to cash, these statements report cash receipts, cash payments, and net changes in cash resulting from operations, investing and financing activities for the reporting period.

Notes to the financial statements – The notes are an integral part of the financial statements. They provide additional disclosures that are essential to a full understanding of the data provided in the financial statements, such as for certain estimates and financing details. The notes to the financial statements begin on page 17 of this report.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Management’s Discussion and Analysis**

Financial Analysis

Increases or decreases in net position may serve over time as a useful indicator of whether the Fund’s financial position is improving or deteriorating. At December 31, 2019 and 2018, the Fund’s assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources, resulting in a net position of \$451.8 million and \$379.1 million, respectively. In 2019, the Fund’s overall net position increased \$72.7 million (19.2%) as compared to an increase in net position of \$16.1 million (4.5%) in 2018. The following summary statements of net position present the assets and deferred outflows of resources of the Fund and show the mix of liabilities, deferred inflows of resources and net position used to acquire these assets and deferred outflows of resources:

Statements of Net Position

| | 2019 | 2018 | 2017 |
|--|-------------------------|-------------------------|-------------------------|
| ASSETS | | | |
| Current assets | \$ 292,633,791 | \$ 250,237,660 | \$ 211,045,692 |
| Capital assets, net | 1,222,123,319 | 1,160,660,014 | 1,109,390,842 |
| Other | 146,614,940 | 211,526,782 | 274,180,787 |
| Total assets | 1,661,372,050 | 1,622,424,456 | 1,594,617,321 |
| DEFERRED OUTFLOWS OF RESOURCES | 28,726,503 | 7,649,631 | 20,286,585 |
| Total assets and deferred outflows of resources | <u>\$ 1,690,098,553</u> | <u>\$ 1,630,074,087</u> | <u>\$ 1,614,903,906</u> |
| LIABILITIES | | | |
| Current liabilities | \$ 78,747,523 | \$ 91,108,610 | \$ 85,892,630 |
| Revenue bonds | 823,179,448 | 854,017,579 | 883,716,806 |
| Other | 327,655,004 | 296,186,563 | 275,166,238 |
| Total liabilities | 1,229,581,975 | 1,241,312,752 | 1,244,775,674 |
| DEFERRED INFLOWS OF RESOURCES | 8,677,263 | 9,628,120 | 7,164,363 |
| NET POSITION | | | |
| Net investment in capital assets | 448,542,091 | 392,376,343 | 379,865,089 |
| Restricted | 22,384,553 | 49,971,545 | 47,240,194 |
| Unrestricted | <u>(19,087,329)</u> | <u>(63,214,673)</u> | <u>(64,141,414)</u> |
| Total net position | 451,839,315 | 379,133,215 | 362,963,869 |
| Total liabilities, deferred inflows of resources, and net position | <u>\$ 1,690,098,553</u> | <u>\$ 1,630,074,087</u> | <u>\$ 1,614,903,906</u> |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Management’s Discussion and Analysis**

Financial Analysis (continued)

2019 Compared to 2018

Assets – Current assets increased \$42.4 million (16.9%) over the prior year primarily due to \$46.0 million increase in operating cash and equity in pooled investments, \$3.3 million in accounts receivable, net of allowance for doubtful accounts, \$3.7 million in unbilled revenues, and \$0.3 million in materials and supplies inventory. These increases are offset by decreases of \$10.1 million in amounts due from other funds, and \$0.9 million in amounts due from other governments.

Other assets decreased by \$64.9 million (-30.7%) from 2018. This is mostly attributable to \$64.0 million reduction in restricted cash and equity in pooled investments used to fund capital projects, and \$0.9 million reduction in other charges.

Deferred outflows of resources – Deferred outflows of resources increased by \$21.1 million (275.5%) from 2018. This increase is attributed to a \$21.4 million increase in pension contributions and changes in assumptions related to pension and other post-employment benefits, and offset by a \$0.4 million decrease in unamortized loss on refunded debt.

Liabilities – Current liabilities decreased by \$12.4 million (-13.6%) from 2018. This is mostly attributable to \$19.1 million reduction in due to other funds because of settlements made during the year. This decrease was offset by an increase of \$1.2 million in accounts payable; and \$4.6 million in salaries, benefits and payroll taxes payable.

Other liabilities increased by \$31.5 million (10.6%) from 2018. This is mostly attributable to \$6.8 million increase in environmental liabilities because of changes in estimates, \$24.9 million in net pension liability (Note 9) because of contributions and changes in assumptions, and \$1.5 million increase in other noncurrent liabilities. The increase was offset by \$2.4 million reduction in loan debt.

Deferred inflows of resources – Deferred inflow of resources decreased by \$1.0 million (-9.9%) from 2018. This decrease is due to assumptions related to pension accounting and difference between expected and actual expense in other post-employment benefits(OPEB).

Net position – The largest portion of the Fund’s net position (\$448.5 million or 99.3%) reflects the Fund’s investment in capital assets such as land, buildings, and equipment, less accumulated depreciation and any related outstanding debt used to acquire those assets. The Fund uses these assets to provide services to customers; consequently, these assets are not available for future spending. Although the Fund’s investment in its capital assets is reported net of related debt, the resources needed to repay the debt are provided by fees paid by customers for services provided by these assets. In 2019, net investment in capital assets increased \$56.2 million from 2018 due to an increase in capital assets placed in service, net of depreciation offset by the related debt.

Seattle Public Utilities – Drainage and Wastewater Fund (An Enterprise Fund of the City of Seattle) Management’s Discussion and Analysis

Financial Analysis (continued)

The Fund’s restricted net position (\$22.4 million or 5.0%) represent resources that are subject to restrictions on how they may be used. This portion of net position decreased by \$27.6 million from 2018.

The remaining portion of the Fund’s net position (a negative \$19.1 million or -4.2%) represents resources that are unrestricted. The unrestricted portion of net position increased by \$44.1 million from the prior year.

2018 Compared to 2017

Assets – Current assets increased \$39.2 million (18.6%) over the prior year primarily due to increases of \$20.1 million of operating cash and equity in pooled investments, \$14.6 million in amounts due from other funds, \$1.1 million in accounts receivable, net of allowance for doubtful accounts, \$2.0 million in amounts due from other governments and \$1.3 million in unbilled revenues.

Other assets decreased \$62.7 million (-22.9%) from 2017. This is mostly attributable to decreases of \$62.1 million in restricted cash and equity in pooled investments used to fund capital projects, \$0.3 million in regulatory assets, and \$0.3 million in other charges.

Deferred outflows of resources – Deferred outflows of resources decreased by \$12.6 million (-62.3%) from 2017. This decrease is attributed to a \$12.2 million reduction in pension contributions and changes in assumptions related to pension and other post-employment benefits, and by a \$0.4 million decrease in unamortized loss on refunded debt.

Liabilities – Current liabilities increased \$5.2 million (6.1%) from 2017. This is attributable to increases of \$7.6 million in due to other funds including an increase of \$3.6 million due to Seattle Department of Transportation, and an increase of \$1.2 million due to the City’s Construction and Inspections department; and an increase of \$4.9 million in accounts payable. These increases were mostly offset by decreases of \$4.6 million in due to other governments, and \$1.6 million in claims payable.

Other liabilities increased \$21.0 million (7.6%). This is mostly attributable to an increase of \$35.3 million to environmental liabilities due to changes in estimates. This increase was offset by decreases of \$14.8 million to net pension liability (Note 9) due to contributions and changes in assumptions.

Deferred inflows of resources – Deferred inflow of resources increased by \$2.5 million (34.4%) from 2017. This increase is due to a change in the proportionate share of employer pension contributions and changes in other post-employment benefits.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Management’s Discussion and Analysis**

Financial Analysis (continued)

Net position – The largest portion of the Fund’s net position (\$392.4 million or 103.5%) reflects the Fund’s investment in capital assets such as land, buildings, and equipment, less accumulated depreciation and any related outstanding debt used to acquire those assets. The Fund uses these assets to provide services to customers; consequently, these assets are not available for future spending. Although the Fund’s investment in its capital assets is reported net of related debt, the resources needed to repay the debt are provided by fees paid by customers for services provided by these assets. In 2018, net investment in capital assets increased \$12.5 million from 2017 due to a decrease in capital assets placed in service, net of depreciation offset by the related debt.

The Fund’s restricted net position (\$50.0 million or 13.2%) represent resources that are subject to restrictions on how they may be used. This portion of net position increased \$2.7 million from 2017.

The remaining portion of the Fund’s net position (a negative \$63.2 million or -16.7%) represents resources that are unrestricted. The unrestricted portion of net position increased \$0.9 million from the prior year.

The following summary statements of revenues, expenses, and changes in net position present the annual surplus of revenues over expenses (the change in net position):

Summary Statements of Revenues, Expenses, and Changes in Net Position

| | <u>2019</u> | <u>2018</u> | <u>2017</u> |
|-------------------------------------|----------------------|----------------------|----------------------|
| Operating revenues | \$ 454,381,865 | \$ 419,875,848 | \$ 400,284,279 |
| Operating expenses | <u>(370,768,095)</u> | <u>(355,581,801)</u> | <u>(344,645,809)</u> |
| Net operating income | 83,613,770 | 64,294,047 | 55,638,470 |
| Non-operating revenues and expenses | (2,005,208) | (7,425,190) | (15,298,003) |
| Environmental remediation | <u>(8,902,462)</u> | <u>(40,699,511)</u> | <u>(9,618,873)</u> |
| Change in net position | <u>\$ 72,706,100</u> | <u>\$ 16,169,346</u> | <u>\$ 30,721,594</u> |

2019 Compared to 2018

Current year operating revenues increased \$34.5 million (8.2%) from 2018. This is due to an average rate of increase of 7.4% for wastewater and 8.0% for drainage, resulting in additional revenues of \$25.7 million and \$9.5 million, respectively. Other operating revenues decreased by \$0.8 million.

Seattle Public Utilities – Drainage and Wastewater Fund (An Enterprise Fund of the City of Seattle) Management’s Discussion and Analysis

Financial Analysis (continued)

Operating expenses increased by \$15.2 million (4.3%) from 2018. The increases can largely be attributed to \$6.6 million increase in salaries, wages and personnel benefits and \$7.2 million increase in intergovernmental payments consisting of \$4.1 million for city and state taxes and \$3.1 million for wastewater treatment. Additional increases consisted of \$1.2 million for supplies and \$1.2 million for services. These increases were offset by a decrease in other operating expenses by \$1.0 million.

Nonoperating revenues (expenses) decreased by \$5.4 million (-73%) as compared to 2018. This decrease in net expenses is due to a \$6.0 million increase in investment income and \$2.8 million reduction in interest expense. The decrease in net expenses is offset by \$3.3 million decrease in contributions and grants.

The Fund had an environmental remediation expense of \$8.9 million for 2019 as compared to \$40.7 million in 2018 (Note 10). This significant reduction resulted from a one-time adjustment in 2018 to record additional estimated costs for remediation management and construction.

2018 Compared to 2017

Current year operating revenues increased \$19.6 million (4.9%) from 2017. This is due to average rate increases of 3.9% for wastewater and 10.7% for drainage, resulting in additional revenues of \$5.8 million and \$14.2 million, respectively. Other operating revenues decreased by \$0.3 million.

Operating expenses increased \$10.9 million (3.2%) from 2017. The largest operating expense increase was related to city and state business occupation tax of \$7.4 million as a result of the overall increase in taxable revenues. Depreciation and other amortization also increased \$5.1 million as a result of an increase in depreciable assets. These increases were offset by a decrease in salaries, wages and personnel benefits of \$2.8 million.

Nonoperating revenues (expenses) decreased by \$7.9 million (-51.5%) as compared to 2017. This decrease in net expenses is due to a \$5.5 million increase in contributions and grants, a \$3.9 million increase in investment income. These increases in revenue were offset by an increase in interest expense of \$1.4 million.

The Fund had an environmental remediation expense of \$40.7 million for 2018 as compared to \$9.6 million in 2017 (Note 10). This increase was due to additional estimated costs for remediation management and construction.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Management’s Discussion and Analysis**

Capital Assets

The following table summarizes capital assets, net of accumulated depreciation, by major asset category:

Summary of Capital Assets, Net of Accumulated Depreciation

| | 2019 | 2018 | 2017 |
|---|-------------------------|-------------------------|-------------------------|
| Land and land rights | \$ 40,330,875 | \$ 40,330,857 | \$ 23,690,882 |
| Buildings | 14,294,425 | 14,979,994 | 14,284,548 |
| Infrastructure | 893,366,112 | 881,069,327 | 858,754,751 |
| Machinery and equipment | 65,786,979 | 61,973,886 | 67,328,022 |
| Computer systems | 22,083,185 | 25,114,329 | 20,699,197 |
| Construction in progress | 184,069,459 | 135,164,900 | 122,606,722 |
| Artwork | 2,192,284 | 2,026,721 | 2,026,721 |
| Capital assets, net of accumulated depreciation | <u>\$ 1,222,123,319</u> | <u>\$ 1,160,660,014</u> | <u>\$ 1,109,390,843</u> |

Additional information about the Fund’s capital assets can be found in Note 3 of this report.

2019 Compared to 2018

The Fund’s investment in capital assets, net of accumulated depreciation, for the year ended December 31, 2019, was \$1.2 billion. This represented an increase of approximately \$61.5 million (5.3%) compared to 2018. Highlights of the Fund’s major capital assets placed in service during 2019 included the following:

- \$7.8 million for pipe rehabilitation and improvements
- \$6.6 million for sewer pipe lining projects
- \$6.2 million for emergency force main replacement
- \$5.8 million for pump station ventilation upgrades
- \$2.1 million for pump stations improvement
- \$15.5 million for various other small construction projects

Highlights of the Fund’s major construction projects in progress at the end of 2019 include the following:

- \$98.6 million for construction of a combined sewer overflow storage facility for the Ballard, Fremont, and Wallingford combined sewer overflow basins (Ship Canal Water Quality Project)
- \$14.0 million for sewer and storm water system improvements
- \$10.5 million to build a pump station facility near 7th Street and Riverside in South Park
- \$8.0 million for pipe improvements in the Alaska Way Viaduct Battery Street Tunnel project
- \$6.5 million for improvements to Taylor Creek downstream from Rainier Ave South
- \$4.3 million for the Alaskan Way Viaduct and Waterfront combined sewer overflow control
- \$4.1 million for pump station retrofit in the Magnolia area
- \$4.0 million for construction project artwork
- \$3.5 million for raingardens, cisterns and other national drainage improvements
- \$3.5 million for infrastructure improvements in South Park

Seattle Public Utilities – Drainage and Wastewater Fund (An Enterprise Fund of the City of Seattle) Management’s Discussion and Analysis

Capital Assets (continued)

- \$3.2 million for culvert replacement at Puget Way SW
- \$2.9 million for the South Park Stormwater Treatment Facility
- \$2.7 million for construction of combined sewer overflow storage facilities in Henderson North
- \$2.5 million for roadside bioretention for Longfellow Creek
- \$2.3 million for repairing 20 deficient sewer pipes
- \$2.3 million for combined sewer overflow retrofit in the Mountlake area

2018 Compared to 2017

The Fund’s investment in capital assets, net of accumulated depreciation, for the year ended December 31, 2018, was \$1.2 billion. This represented an increase of approximately \$51.3 million (4.6%) compared to 2017. Highlights of the Fund’s major capital assets placed in service during 2018 included the following:

- \$23.1 million for pipe rehabilitation and improvements
- \$12.0 million for land at the south operations facility
- \$6.2 million for the Fund’s share of a new Citywide financial system
- \$4.7 million for land purchased for the Ship Canal Water Quality project
- \$3.7 million for heavy equipment purchases

Highlights of the Fund’s major construction projects in progress at the end of 2018 include the following:

- \$70.7 million for construction of a combined sewer overflow storage facility for the Ballard, Fremont, and Wallingford combined sewer overflow basins (Ship Canal Water Quality Project)
- \$10.8 million for sewer and storm water system improvements
- \$8.6 million to build a pump station facility near 7th Street and Riverside in South Park
- \$7.3 million for pipe improvements in the Alaska Way Viaduct Battery Street Tunnel project
- \$5.2 million for improvements to Taylor Creek downstream from Rainier Ave South
- \$3.8 million for future art installations for construction projects
- \$3.2 million for raingardens, cisterns and other national drainage improvements
- \$3.1 million for the Alaskan Way Viaduct and Waterfront combined sewer overflow control
- \$2.8 million for sewer pipe lining projects
- \$2.5 million for the South Park Stormwater Treatment Facility
- \$2.5 million for construction of combined sewer overflow storage facilities in Henderson North
- \$2.3 million for ventilation upgrades at 50 pump stations
- \$2.1 million for pump station retrofit in the Magnolia area

Seattle Public Utilities – Drainage and Wastewater Fund (An Enterprise Fund of the City of Seattle) Management’s Discussion and Analysis

Debt Administration

The Fund’s debt primarily consists of bonded debt and loans. Bonded debt is secured solely by drainage and wastewater revenues and provides financing for capital improvements. Loans issued by various Washington State Agencies for certain capital improvements are unsecured. The Fund’s credit ratings on its bonds were Aa1 and AA+ by Moody’s Investors Service Inc. and Standard & Poor’s Rating Services, respectively. Additional details about the Fund’s revenue bonds and loans are in Notes 4 and 11 of this report.

2019 Compared to 2018

At the end of 2019, the Fund had \$769.6 million in bonded debt, as compared to \$796.0 million in 2018, all of which was secured solely by drainage and wastewater system revenues. This decrease of \$26.4 million is attributed to payment of debt principal.

At the end of 2019, the Fund had an outstanding loan balance of \$45.0 million compared to \$47.4 million in 2018. This decrease is due to \$2.7 million payment of debt principal offset by a \$0.4 million drawdown from a new loan with the Washington State Department of Ecology.

2018 Compared to 2017

At the end of 2018, the Fund had \$796.0 million in bonded debt, as compared to \$821.3 million in 2017, all of which was secured solely by drainage and wastewater system revenues. This decrease of \$25.2 million is attributed the payment of debt principal.

At the end of 2018, the Fund had an outstanding loan balance of \$47.4 million compared to \$46.1 million in 2017. This increase is mostly due to a \$3.8 million loan drawdown from the Department of Ecology for the Henderson combined sewer overflow project and a decrease of \$3.1 million due to payments of loan principal.

Requests for Information

The Fund’s financial statements are designed to provide a general overview of the Fund’s finances, as well as to demonstrate the Fund’s accountability to its customers, investors, creditors, and other interested parties. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Seattle Public Utilities, Finance and Administration Branch, Accounting Division, PO Box 34018, Seattle, Washington 98124-4018, telephone: (206) 684-3000.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Statements of Net Position**

| | December 31, | |
|---|-------------------------|-------------------------|
| | 2019 | 2018 |
| ASSETS | | |
| CURRENT ASSETS | | |
| Operating cash and equity in pooled investments | \$ 230,631,233 | \$ 184,599,555 |
| Receivables | | |
| Accounts, net of allowance | 24,374,625 | 21,117,951 |
| Interest and dividends | 300,369 | 305,648 |
| Unbilled revenues | 26,412,619 | 22,714,980 |
| Due from other funds | 5,228,230 | 15,306,291 |
| Due from other governments | 3,819,492 | 4,672,172 |
| Materials and supplies inventory | 1,832,708 | 1,486,548 |
| Prepayments and other current assets | 34,515 | 34,515 |
| | <u>292,633,791</u> | <u>250,237,660</u> |
| NONCURRENT ASSETS | | |
| Restricted cash and equity in pooled investments | 88,092,415 | 152,136,162 |
| Prepayments long-term | 518,531 | 553,046 |
| Environmental costs and recoveries | 2,635,475 | 2,029,086 |
| External infrastructure costs | 17,863,808 | 18,156,657 |
| Regulatory assets - bond issue costs | 5,119,856 | 5,374,853 |
| Other charges | 32,384,855 | 33,276,978 |
| Capital assets | | |
| Land and land rights | 40,330,875 | 40,330,857 |
| Plant in service, excluding land | 1,404,055,071 | 1,370,836,335 |
| Less accumulated depreciation | (408,524,370) | (387,698,799) |
| Construction in progress | 184,069,459 | 135,164,900 |
| Other property, net | 2,192,284 | 2,026,721 |
| | <u>1,368,738,259</u> | <u>1,372,186,796</u> |
| | <u>1,661,372,050</u> | <u>1,622,424,456</u> |
| DEFERRED OUTFLOWS OF RESOURCES | | |
| Unamortized loss on refunded debt | 5,962,106 | 6,329,428 |
| Pension and OPEB contributions and changes in assumptions | 22,764,397 | 1,320,203 |
| | <u>28,726,503</u> | <u>7,649,631</u> |
| | <u>\$ 1,690,098,553</u> | <u>\$ 1,630,074,087</u> |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Statements of Net Position**

| | December 31, | |
|---|-------------------------|-------------------------|
| | 2019 | 2018 |
| LIABILITIES | | |
| CURRENT LIABILITIES | | |
| Accounts payable | \$ 11,075,543 | \$ 9,863,973 |
| Salaries, benefits, and payroll taxes payable | 7,577,491 | 3,006,856 |
| Compensated absences payable | 246,294 | 217,456 |
| Due to other funds | 10,632 | 19,157,303 |
| Due to other governments | 13,829,482 | 13,353,353 |
| Interest payable | 10,995,428 | 11,404,628 |
| Taxes payable | 433,100 | 437,616 |
| Revenue bonds due within one year | 27,575,000 | 26,425,000 |
| Claims payable | 1,630,749 | 1,507,535 |
| Environmental liabilities | 1,730,070 | 2,281,722 |
| Loans payable, due within one year | 2,792,896 | 2,744,897 |
| Other | 850,838 | 708,271 |
| | <u>78,747,523</u> | <u>91,108,610</u> |
| Total current liabilities | | |
| NONCURRENT LIABILITIES | | |
| Compensated absences payable | 4,679,584 | 4,131,656 |
| Claims payable | 5,549,328 | 5,457,201 |
| Environmental liabilities | 179,154,291 | 172,340,070 |
| Loans | 42,222,552 | 44,634,227 |
| Unfunded other post employment benefits | 2,968,115 | 2,956,196 |
| Net pension liability | 91,293,054 | 66,368,647 |
| Other noncurrent liabilities | 1,788,080 | 298,566 |
| Revenue bonds | 769,605,000 | 796,030,000 |
| Less bonds due within one year | (27,575,000) | (26,425,000) |
| Bond discount and premium, net | 81,149,448 | 84,412,579 |
| | <u>1,150,834,452</u> | <u>1,150,204,142</u> |
| Total noncurrent liabilities | | |
| Total liabilities | <u>1,229,581,975</u> | <u>1,241,312,752</u> |
| DEFERRED INFLOWS OF RESOURCES | | |
| Deferred inflows - pension and OPEB | 8,677,263 | 9,628,120 |
| | <u>8,677,263</u> | <u>9,628,120</u> |
| NET POSITION | | |
| Net investment in capital assets | 448,542,091 | 392,376,343 |
| Restricted for | | |
| External infrastructure costs | 6,807,082 | 6,878,380 |
| Other charges | 14,291,333 | 43,093,165 |
| Retainage | 1,286,138 | - |
| Unrestricted | (19,087,329) | (63,214,673) |
| | <u>451,839,315</u> | <u>379,133,215</u> |
| Total net position | | |
| Total liabilities, deferred inflows of resources, and net position | <u>\$ 1,690,098,553</u> | <u>\$ 1,630,074,087</u> |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Statements of Revenues, Expenses, and Changes in Net Position**

| | Years Ended December 31, | |
|---|--------------------------|----------------|
| | 2019 | 2018 |
| OPERATING REVENUES | | |
| Charges for services and other revenues | \$ 454,381,865 | \$ 419,875,848 |
| OPERATING EXPENSES | | |
| Salaries, wages, and personnel benefits | 55,874,922 | 49,258,786 |
| Supplies | 3,229,100 | 2,076,567 |
| Services | 43,255,596 | 42,047,566 |
| Intergovernmental payments | 226,517,154 | 219,283,988 |
| Depreciation and amortization | 38,134,482 | 38,161,539 |
| Other operating expenses | 3,756,841 | 4,753,355 |
| Total operating expenses | 370,768,095 | 355,581,801 |
| OPERATING INCOME | 83,613,770 | 64,294,047 |
| NONOPERATING REVENUES (EXPENSES) | | |
| Investment income | 14,954,743 | 8,959,368 |
| Interest expense | (25,294,016) | (28,094,422) |
| Contributions and grants | 6,382,015 | 9,673,436 |
| Other, net | 1,952,050 | 2,036,428 |
| Total nonoperating expenses | (2,005,208) | (7,425,190) |
| INCOME BEFORE SPECIAL ITEMS | 81,608,562 | 56,868,857 |
| ENVIRONMENTAL REMEDIATION | (8,902,462) | (40,699,511) |
| CHANGE IN NET POSITION | 72,706,100 | 16,169,346 |
| NET POSITION | | |
| Beginning of year | 379,133,215 | 362,963,869 |
| End of year | \$ 451,839,315 | \$ 379,133,215 |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Statements of Cash Flows**

| | Years Ended December 31, | |
|---|--------------------------|-----------------------|
| | 2019 | 2018 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Cash received from customers | \$ 461,717,020 | \$ 394,452,739 |
| Cash paid to suppliers | (234,066,948) | (207,654,312) |
| Cash paid to employees | (50,010,015) | (43,183,339) |
| Cash paid for taxes | (59,091,556) | (54,721,815) |
| | 118,548,501 | 88,893,273 |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES | | |
| Noncapital grants received | 2,397,668 | 7,116,639 |
| Payments for environmental liabilities | (3,324,535) | (4,612,577) |
| | (926,867) | 2,504,062 |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | |
| Principal payments on long-term debt | (27,958,299) | (24,275,556) |
| Capital expenditures and other charges paid | (90,312,606) | (82,773,263) |
| Interest paid on long-term debt | (36,693,933) | (38,139,667) |
| Build America Bonds federal interest subsidy | 1,686,168 | 1,712,960 |
| Capital fees and grants received | 3,984,348 | 2,556,797 |
| Proceeds from sale of capital assets | 386,764 | 338,082 |
| | (148,907,558) | (140,580,647) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Gain on investments | 13,273,855 | 7,235,860 |
| | 13,273,855 | 7,235,860 |
| NET CHANGE IN CASH AND EQUITY IN POOLED INVESTMENTS | (18,012,069) | (41,947,452) |
| CASH AND EQUITY IN POOLED INVESTMENTS | | |
| Beginning of year | 336,735,717 | 378,683,169 |
| End of year | \$ 318,723,648 | \$ 336,735,717 |
| CASH AT THE END OF THE YEAR CONSISTS OF | | |
| Operating cash and equity in pooled investments | \$ 230,631,233 | \$ 184,599,555 |
| Noncurrent restricted cash and equity in pooled investments | 88,092,415 | 152,136,162 |
| | \$ 318,723,648 | \$ 336,735,717 |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Statements of Cash Flows (continued)**

| | Years Ended December 31, | |
|--|------------------------------|-----------------------------|
| | 2019 | 2018 |
| RECONCILIATION OF NET OPERATING INCOME TO NET CASH FROM OPERATING ACTIVITIES | | |
| Operating income | <u>\$ 83,613,770</u> | <u>\$ 64,294,047</u> |
| Adjustments to reconcile net operating income to net cash from operating activities | | |
| Adjustment for net pension liability | 1,948,677 | (5,889,804) |
| Depreciation and amortization | 38,134,482 | 38,161,538 |
| Other receipts and payments | 1,643,538 | 1,447,893 |
| Changes in operating assets and liabilities | | |
| Accounts receivable | (830,192) | (1,069,006) |
| Unbilled revenues | (3,697,640) | (1,299,228) |
| Due from other funds | 10,025,579 | (14,596,803) |
| Due from other governments | (1,521,321) | (1,984,539) |
| Materials and supplies inventory | (346,159) | (103,778) |
| Other assets | 34,515 | 13,516,958 |
| Accounts payable | 1,211,571 | 4,943,995 |
| Salaries, benefits, and payroll taxes payable | 4,570,635 | (1,060,639) |
| Compensated absences payable | 576,766 | (595,351) |
| Due to other funds | (19,146,672) | 7,617,529 |
| Due to other governments | 476,129 | (4,593,736) |
| Claims payable | 215,341 | (435,246) |
| Taxes payable | (4,517) | 198,879 |
| Other liabilities | <u>1,643,999</u> | <u>(9,659,436)</u> |
| Total adjustments | <u>34,934,731</u> | <u>24,599,226</u> |
| Net cash from operating activities | <u><u>\$ 118,548,501</u></u> | <u><u>\$ 88,893,273</u></u> |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 1 – Operations and Summary of Significant Accounting Policies

Operations – The City of Seattle, Seattle Public Utilities – Drainage and Wastewater Fund (the Fund) is a public utility enterprise fund of the City of Seattle (the City). The Fund was established to account for the drainage and wastewater activities of Seattle Public Utilities (SPU). Drainage activities include regulating storm water runoff, alleviating flooding, mitigating water pollution caused by runoff, and responding to federal storm water regulations, in addition to managing drainage utility assets. Wastewater activities consist of managing the City’s sewer system, including the operation of sewer utility facilities and pumping stations necessary to collect the sewage of the City and discharge it into the King County Department of Natural Resources Wastewater Treatment System for treatment and disposal.

On January 1, 1997, the City created SPU, which brought together under one administrative umbrella the water, solid waste, and drainage and wastewater functions of the City. The Fund (as well as SPU’s other funds) remains separate for accounting purposes.

SPU receives certain services from other departments and agencies of the City, including information technology and others that are normally considered to be general and administrative. The Fund is charged a share of these costs and during 2019 and 2018, paid \$23,487,277 and \$22,752,480, respectively, to the City for its share of these services. Additionally, the Fund pays a business and occupation utility tax to the City’s General Fund. The Fund paid \$53,151,086 and \$49,694,689 for these taxes in 2019 and 2018, respectively.

The utility billing function is co-managed by SPU and Seattle City Light (SCL). SPU provides customer service through the call center and walk-in center. SCL operates and manages the billing system. SPU and SCL bill and reimburse each other for these services. SPU reimburses Seattle IT for the information technologies services mentioned above. Within SPU, the costs and reimbursements were shared among its three utility funds (Water, Drainage and Wastewater, and Solid Waste). The Fund received reimbursements related to the call center and walk-in center of \$2,256,796 and \$2,335,964 in 2019 and 2018, respectively. The Fund paid \$8,390 and \$28,264 for the utility billing services in 2019 and 2018, respectively.

Wastewater disposal and drainage services provided to other City departments and agencies are billed at rates prescribed by City ordinances. The Fund collected \$3,198,764 in 2019 and \$3,226,365 in 2018 from the City for wastewater services provided. The Fund also collected \$10,072,336 in 2019 and \$9,353,846 in 2018 from the City for drainage services.

The Fund is subject to regulation by the City and the State of Washington. Service rates are authorized by ordinances passed by the City Council. Financial reporting is reviewed by the Washington State Auditor’s Office and conforms to accounting principles generally accepted in the United States of America as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

Seattle Public Utilities – Drainage and Wastewater Fund (An Enterprise Fund of the City of Seattle) Notes to Financial Statements

Note 1 – Operations and Summary of Significant Accounting Policies (continued)

Basis of accounting – The Fund is accounted for on a flow of economic resources measurement focus. Its financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as applied to governmental units using the accrual basis of accounting. With the flow of economic resources measurement focus, all assets, deferred outflows of resources, liabilities, and deferred inflows of resources associated with the Fund’s operations are included on the statements of net position. The operating statements present increases (revenues) and decreases (expenses) in total net position.

Cash and equity in pooled investments – Cash resources of the Fund are combined with cash resources of the City in a pooled investment portfolio that is managed by the City’s Finance and Administration Services Department. The City’s investment portfolio consists of fixed income securities authorized by the Revised Code of Washington and other applicable law. The pool operates like a demand deposit account in that all City departments may deposit cash at any time and withdraw cash out of the pool without prior notice or penalty. Interest earned on the pooled investments is prorated to individual funds at the end of each month on the basis of their average daily cash balances during the month when interest was earned. Cash and equity in pooled investments are reported at fair market value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, and GASB Statement No. 72, *Fair Value Measurement and Application*. The Fund’s share of the pool is included in the accompanying Statement of Net Position under the caption “cash and equity in pooled investments.” Accordingly, the Statements of Cash Flows reconcile to cash and equity in pooled investments. The restricted cash and equity in pooled investments are comprised of unexpended bond proceeds, bond reserve funds and vendor’s escrow deposits.

Receivables and unbilled revenues – Customer accounts receivable consist of amounts owed by private individuals and organizations for goods delivered or services rendered in the regular course of business operations. Receivables are shown net of allowances for doubtful accounts. The Fund also accrues an estimated amount for services that have been provided but not billed.

Due from/to other funds and governments – Activity between other funds and governments that is outstanding at the end of the year, not related to the provision of utility services, is reported as due from or due to other funds and governments.

Allowance for doubtful accounts – A reserve has been established for uncollectible accounts receivable based on actual historical write-off trends and knowledge of specific circumstances that indicate collection of an account may be unlikely. As of December 31, 2019 and 2018, the Fund’s allowance for doubtful accounts was \$712,715 and \$645,798, respectively.

Materials and supplies inventory – The Fund values its inventory based on a moving average method. The most recent total cost of an inventory item is divided by the total units of the item that remain in inventory to determine the moving average cost of the item. The moving average cost is then applied to all the units of the inventory item.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 1 – Operations and Summary of Significant Accounting Policies (continued)

Environmental costs and recoveries – The Fund is involved in several remediation efforts around the City (Note 10). When estimated remediation costs are approved to be recovered through rates, the costs, net of recoveries, associated with these efforts are deferred when accrued as a regulatory asset and are amortized over the rate recovery period. Certain environmental remediation costs that are infrequent in occurrence are treated as a special item in the Statements of Revenues, Expenses, and Changes in Net Position.

External infrastructure costs – The Fund has contributed \$21,963,686 to a joint project with King County to expand one of their transmission lines to help alleviate sewer overflows in the area. These costs represent the portion of the project that did not result in a capital asset for the Fund. The project was completed in 2005. The Fund has deferred these costs and began amortizing them in 2006 over a 75-year period.

Regulatory assets – bond issue costs – GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, allows for certain costs to be capitalized as a regulatory asset instead of charged to expense. A regulatory asset is recorded when it is probable that future revenue in an amount at least equal to the capitalized costs will be recovered through customer rates over some future period. The Fund uses regulatory accounting for debt issuance costs because these costs are included in the rate structure and, as such, will continue to be amortized over the life of the associated bond issues. GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, would have required these costs to be expensed in the period incurred if the Fund had not utilized regulatory accounting for these costs.

Other charges – Other charges primarily represent costs related to the Long Term Control Plan which direct the Fund's construction and monitoring of several Combined Sewer Overflow projects. The Fund amortizes these charges over a 5 to 30-year period.

Capital assets – Capital assets are stated at cost or, if contributed, at fair value at the date of contribution. Costs include direct material, labor, and indirect costs such as engineering, supervision, payroll taxes, pension benefits, and interest relating to the financing of projects under construction. The cost of current repairs and maintenance is charged to expense, while the cost of additions and improvements is capitalized. SPU's policy is to generally capitalize assets with a cost of \$5,000 or more. The Fund received donated assets, such as sewer and drainage pipes, from developers and other government agencies. These donated assets are recorded under capital contributions and grants in the statements of revenues, expenses, and changes in net position.

Construction in progress – Capitalizable costs incurred on projects which are not in use or ready for use are held in construction in progress. When the asset is ready for use, related costs are transferred to capital assets. Upon determining that a project will be abandoned, the related costs are charged to expense.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 1 – Operations and Summary of Significant Accounting Policies (continued)

Other property – Other property is stated at cost, or if contributed, the fair value at the date of contribution. Other property includes artwork and property held for future use. The artwork is acquired through the City’s “One Percent for Art” program, which supports the City ordinance established to direct the inclusion of works of art in public spaces within the City.

Depreciation – Capital assets in service are depreciated on the straight-line method over estimated useful lives as follows:

| | |
|--|----------------|
| Buildings and fixtures | 10 to 50 years |
| Laterals, mains, and outfalls | 75 years |
| Detention structures | 75 years |
| Pumping stations, equipment, and overflow structures | 10 to 50 years |
| Machinery and equipment | 3 to 20 years |
| Computer systems | 3 to 11 years |

In 2018, SPU’s depreciation policy was changed when the City implemented a new financial system. For most assets, depreciation begins in the month the asset is placed in service.

Deferred outflows/inflows of resources – In addition to assets, the Statement of Net Position, when applicable, will report a separate section for deferred outflows of resources. It represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense) until then. The Fund has deferred loss on refunding debt which qualifies for reporting in this category. A deferred loss on refunding debt results from the difference in the carrying value of refunded debt and its reacquisition price. This amount is deferred and amortized over the shorter of the life of the refunded or refunding debt. The Fund has also recorded deferred outflows of resources for certain pension activities including, the difference between projected and actual experience, the difference between projected and actual earnings on investments, and contributions made subsequent to the measurement date (Note 9).

In addition to liabilities, the statement of net position, when applicable, will report a separate section for deferred inflows of resources. It represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until then. The Fund has also recorded deferred inflows of resources for the difference between projected and actual experience and changes in proportion and differences between employer contributions and proportionate share of contributions.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 1 – Operations and Summary of Significant Accounting Policies (continued)

Environmental liabilities – The Fund has accrued a liability for pollution remediation activities in accordance with GASB Statement No. 49 (GASB 49), *Accounting and Financial Reporting for Pollution Remediation Obligations*. GASB 49 outlines five specific obligating events that give rise to estimating expected pollution remediation outlays. These outlays may be accrued as a liability and expensed, or if appropriate, capitalized. The Fund will accrue a liability if any of the following obligating events occurs:

- The Fund is compelled to take pollution remediation action because of an imminent endangerment.
- The Fund violates a pollution prevention-related permit or license.
- The Fund is named, or evidence indicates it will be named, by a regulator as a potentially responsible party (PRP) for remediation.
- The Fund is named, or evidence indicates that it will be named, in a lawsuit to compel participation in pollution remediation.
- The Fund commences or legally obligates itself to commence pollution remediation.

Most pollution remediation outlays do not qualify for capitalization and the Fund does not anticipate significant capitalized costs in the future. See Note 10 for site descriptions.

Pensions – For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Seattle City Employees' Retirement System (SCERS) are reported on the same basis as reported by SCERS. For this purpose, benefit payments are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Postemployment Benefits Other Than Pensions (OPEB) – For purposes of measuring the net OPEB liability, deferred outflows of resources and deferred inflows of resources related to OPEB, and OPEB expense, information about the benefit have been determined on the same basis as they are reported by the City. For this purpose, benefit payments are recognized when due and payable in accordance with the benefit terms.

Compensated absences – Employees earn vacation based upon their date of hire and years of service, and may accumulate earned vacation up to a maximum of 480 hours. Unused vacation at retirement or normal termination is considered vested and payable to the employee. Earned but unused vacation is accrued as a liability of the Fund. Employees also earn up to 12 days of sick leave per year and may accumulate sick leave balances without limit.

Employees who submit the required documentation when represented by the Coalition of City Unions are paid 35% of the value of unused sick leave upon retirement as part of the Health Reimbursement Arrangement – Voluntary Employees' Beneficiary Association (HRA-VEBA) program. If the employee fails to submit the required documentation by their last working day of employment, their sick leave balance is forfeited.

Seattle Public Utilities – Drainage and Wastewater Fund (An Enterprise Fund of the City of Seattle) Notes to Financial Statements

Note 1 – Operations and Summary of Significant Accounting Policies (continued)

Retiring employees who are not eligible to participate in the HRA-VEBA program may elect to receive 25% of the value of unused sick leave upon retirement or defer receipt of 35% of the value of their sick leave balance to the City's 457 Plan and Trust, subject to the year-to-date or life-to-date limitations on deferrals and contributions. If the 35% value of the sick leave balance exceeds the maximum amount deferred to the City's 457 Plan and Trust, the employee shall receive a taxable cash payment equal to the amount by which the 25% value of the sick leave balance exceeds the 35% that was allowed to be deferred. The Fund records a liability for estimated sick leave payments.

Operating revenues – Wastewater service revenues are recorded through cycle billings rendered to customers monthly or bimonthly. The Fund accrues and records unbilled wastewater service revenues in the financial statements for services provided from the date of the last billing to year end.

Drainage service charges are billed to the City's drainage residential and nonresidential customers twice a year through the service of King County's property tax billing system. These charges fund operations and maintenance of, and improvements to, the City's system of storm and drainage facilities.

Other operating revenues include revenues generated from wastewater and sewer permits, and engineering services provided to other City funds.

Operating expenses – The Fund's operating expenses include the cost of sales and services, administrative expenses, depreciation on capital assets and amortization of deferred assets.

Taxes – The Fund is charged a public utility tax by the City at a rate of 12.0% for wastewater revenues and 11.5% for drainage revenues, net of certain credits. In addition, the Fund paid a 3.85% public utility tax to the State on a certain portion of revenues identified as sewer collection revenues. The Fund also paid business and occupation tax to the State on certain drainage and other non-utility revenues at the rate of 1.5%.

Nonoperating revenues and expenses – This includes the non-operating revenues and expenses that arise from transactions not related directly to the major income-earning operations of the Fund and are of a recurring nature. Major items are investment and interest income, interest expense, and capital assets.

Net position – The Statement of Net Position reports all financial and capital resources. Assets and deferred outflows of resources minus liabilities and deferred inflows of resources is net position. There are three components of net position: net investment in capital assets, restricted, and unrestricted.

Net investment in capital assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Net position is restricted when constraints placed on net position use are either: (1) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments, or (2) imposed by law through constitutional provisions or enabling legislation. The Fund's restricted net position as of December 31, 2019 and 2018, are related to external infrastructure costs, certain other charges and retainage. Unrestricted net position is the portion that is not "net investment in capital assets" or "restricted."

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 1 – Operations and Summary of Significant Accounting Policies (continued)

Arbitrage rebate requirement – The Fund is subject to the Internal Revenue Code (IRC), Section 148(f), related to its tax-exempt revenue bonds. The IRC requires that earnings on gross proceeds of any revenue bonds that are in excess of the amount prescribed be surrendered to the Internal Revenue Service. As such, the Fund would record such a rebate as a liability. The Fund had no liability for arbitrage as of December 31, 2019 and 2018.

Accounting standard changes – GASB has issued Statement No. 87, *Standards of Accounting and Financial Reporting for Leases*. The new GASB Lease Rules were issued in June 2017 and will be effective for reporting periods beginning after December 15, 2019. Under this rule, leases are all assumed to be capital financings of the underlying asset with only a narrow range of short-term equipment and motor vehicle leases treated as an ‘operating lease. GASB now assumes that all leases are ‘capital leases’ except for the specific exceptions noted. The Fund is evaluating the impact of this standard on the financial statements.

GASB has also issued Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*. This Statement establishes accounting requirements for interest cost incurred before the end of a construction period. Such interest cost includes all interest that previously was accounted for in accordance with the requirements of paragraphs 5–22 of Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which are superseded by this Statement. This Statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. As a cost of a capital asset reported in a business-type activity or enterprise fund. The Statement was issued in June 2018 to be implemented effective for reporting periods beginning after December 15, 2019. The Fund plans to invoke regulatory accounting under GASB 62 and will continue to capitalize interest as an expense to projects.

Use of estimates – The preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements. Estimates and assumptions are used to record unbilled revenues, allowance for doubtful accounts, fair market value of cash and equity in pooled investments, accrued sick leave, capitalized interest, depreciation, environmental liabilities, risk liabilities, pension liability, and other contingencies. Changes in these estimates and assumptions may have a material impact on the financial statements.

Significant risks and uncertainty – The Fund is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include, but are not limited to, weather and natural disaster-related disruptions, collective bargaining labor disputes, Environmental Protection Agency regulations, and federal government regulations or orders concerning the operation, maintenance, and licensing of facilities

Reclassifications – Certain reclassifications have been made to the prior year financial statement and footnote presentation to correspond to the current year presentation. These reclassifications had no effect on the operating results of the Fund.

Seattle Public Utilities – Drainage and Wastewater Fund (An Enterprise Fund of the City of Seattle) Notes to Financial Statements

Note 2 – Cash and Equity in Pooled Investments

Per Seattle Municipal Code, SMC 5.06.010 Investment Authority, the City's Director of Finance and Administrative Services (FAS) is authorized to invest all moneys in the City Treasury. Cash resources of the Department are combined with cash resources of the City to form a pool of cash that is managed by the City's Department of Finance and Administrative Services (FAS). Under the City's investment policy, all temporary cash surpluses in the pool are invested. The Fund's share of the pool is included on the balance sheets as Cash and Equity in Pooled Investments or as restricted assets. The pool operates like a demand deposit account in that all departments, including the Department, may deposit cash at any time and can also withdraw cash, out of the pool, up to the amount of the Department's fund balance, without prior notice or penalty. Accordingly, the statements of cash flows reconcile to cash and equity in pooled investments. The City considers investments in financial instruments having a maturity of 90 days or less as a cash equivalent.

Custodial credit risk – deposits – Custodial credit risk of deposits is the risk that in the event of bank failure for one of the City's depository institutions, the City's deposits or related collateral securities may not be returned in a timely manner.

As of December 31, 2019, and 2018, the City did not have custodial credit risk. The City's deposits are covered by insurance provided by the Federal Deposit Insurance Corporation (FDIC) and the National Credit Union Association (NCUA) as well as protection provided by the Washington State Public Deposit Protection Commission (PDPC) as established in RCW 39.58. The PDPC makes and enforces regulations and administers a program to ensure public funds deposited in banks and thrifts are protected if a financial institution becomes insolvent. The PDPC approves which banks, credit unions, and thrifts can hold state and local government deposits and monitors collateral pledged to secure uninsured public deposits. This secures public treasurers' deposits when they exceed the amount insured by the FDIC or NCUA by requiring banks, credit unions, and thrifts to pledge securities as collateral.

As of December 31, 2019, and 2018, the City held sufficient cash in its vault for operations. Additional small amounts of cash were held in departmental revolving fund accounts with the City's various custodial banks, all of which fell within the NCUA/FDIC's \$250,000 standard maximum deposit insurance amount. Any of the City's cash not held in its vault, or a local depository, was held in the City's operating fund (investment pool), and at the close of every business day, any cash remaining in the operating fund is swept into an overnight repurchase agreement that matures the next day.

Custodial Credit Risk – investments – Custodial credit risk for investments is the risk that, in the event of failure of the counterparty, the City will not have access to, or be able to recover, its investments or collateral securities that are in the possession of an outside party. The City mitigates custodial credit risk for its investments by having its investment securities held by the City's contractual custodial agent. The City maintains a custody relationship with Wells Fargo under the State of Washington's statewide custody provider program arranged by the State Treasurer's Office. The City mitigates counterparty risk by settling trades through its custodian on a delivery-versus-payment method.

By investment policy, the City maintains a list of approved securities dealers for transacting business. The City also conducts its own due diligence as to the financial wherewithal of its counterparties.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 2 – Cash and Equity in Pooled Investments (continued)

Credit risk – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Some of the City’s pooled investments have credit risk from holdings in commercial paper, corporate notes, and taxable municipal bonds. The City may not hold more than 50% of the Pool’s total assets in these credit sensitive sectors.

State statute defines the investments in commercial paper and corporate notes as a “credit portfolio”. The credit portfolio may not exceed 25 percent of the Pool’s market value. Credit investments must be diversified by sector and industry. No single issuer shall exceed 3 percent of the Pool’s market value. Commercial Paper investments may not have maturities exceeding 270 days and must hold the highest short-term credit rating by all the major credit rating agencies that rate the issuer at the time of purchase.

Corporate notes must mature within 5.5 years from the time of purchase and must be rated at least weak single-A or better by all the major rating agencies that rate the note at the time of purchase. No single issuer rated AA or better may exceed 3 percent of the Pool’s market value. No single issuer rated in the single-A category may exceed 2 percent of the Pool’s market value.

Municipal bonds must have a credit rating of weak single-A or better by all the major rating agencies that rate the issuer at the time of purchase. No single issuer may exceed 5 percent of the Pool’s market value.

Interest rate risk – Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. To mitigate interest rate risk, the City intentionally immunizes its known and expected cash flow needs. To best accomplish meeting its investment objectives, the City has divided the Pool into two separate portfolios: Operating and Strategic.

The Operating Portfolio is invested to meet reasonably expected liquidity needs over a period of twelve to eighteen months. This portfolio has low duration and high liquidity. Consistent with this profile, and for the purpose of comparing earnings yield, its benchmark is the net earnings rate of the State of Washington’s Local Government Investment Pool (LGIP).

The Strategic Portfolio consists of cash that is in excess of known and expected liquidity needs. Accordingly, this portfolio is invested in debt securities with longer maturities than the Operating Portfolio, which over a market cycle, is expected to provide a higher return and greater investment income. Consistent with this profile, and for the purpose of comparing duration, yield and total return, the benchmark for the Strategic portfolio is the Barclays U.S. Government 1-7 year index. The duration of the Strategic Portfolio is targeted between 75% and 125% of the benchmark.

To further mitigate interest rate risk a minimum of 60% of the Operating Portfolio and 30% of the Strategic Portfolio must be invested in asset types with high liquidity, specifically U.S. Government obligations, U.S. Government Agency obligations, LGIP, Demand Accounts, Repo, Sweep, and Commercial Paper.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 2 – Cash and Equity in Pooled Investments (continued)

Investments – The Department’s cash resources may be invested by FAS separate from the cash and investments pool. Investments are managed in accordance with the City’s Statement of Investment Policy, with limits and restrictions applied at the City-wide level rather than to specific investments of the Department. As of December 31, 2019, and 2018, the Department did not have any dedicated investments. The City’s Statement of Investment Policy was modified on January 1, 2018, with an effective date of March 8, 2018. There have been no subsequent changes to the policy. Eligible investments are those securities and deposits authorized by statute (chapters 35.39, 39.58, 39.59, 39.60, and 43.250 RCW; RCW 43.84.080, 43.180.190).

The City of Seattle has three objectives in managing its investments that define its risk profile and guide implementation of its investment strategy. In order of importance they are Safety of Principal, Maintenance of Liquidity, and Return on Investment.

The City follows a set of Standards of Care when it comes to its investments that include the following:

- **Social Policies:** A City social policy shall take precedence over furthering the City’s financial objectives when expressly authorized by City Council resolution, except where otherwise provided by law or trust principles.
- **Prudence:** The standard of prudence to be used by investment personnel shall be the “Prudent Investor Rule” and will be applied in the context of managing an overall portfolio.
- **Ethics and Conflict of Interest:** Investment officers shall comply with the City’s Ethics Code (SMC 4.16.080) and annually submit a Financial Interest Statement to the City’s Ethics & Elections Commission that identifies any potential financial interest that could be related to the performance of the City’s investment portfolio.

Delegation of authority – The Director of Finance and Administrative Services has delegated management responsibility for the City’s investment program to the Director of Finance who has designated day to day management responsibility to investment officers under the supervision of the City’s Treasury Services Director. No persons may engage in an investment transaction except as provided under the terms of the City Statement of Investment Policy and the procedures established therein.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 2 – Cash and Equity in Pooled Investments (continued)

As of December 31, 2019 and 2018, the City's pooled investments were categorized within the fair value hierarchy as follows:

| Investments | Fair Value as of December 31, 2019 | Fair Value Measurements Using | | | Weighted Average Maturity (Days) |
|---|---|-------------------------------|-------------------------|-------------------|---|
| | | Level 1 Inputs | Level 2 Inputs | Level 3 Inputs | |
| U.S. Government Agency Securities | \$ 693,744,193 | \$ 693,744,193 | \$ - | \$ - | 1,246 |
| U.S. Treasury and U.S. Government- Backed Securities | 583,535,317 | 583,535,317 | - | - | 902 |
| Municipal Bonds | 354,007,423 | - | 354,007,423 | - | 2,184 |
| Commercial Paper | 84,916,181 | - | 84,916,181 | - | 22 |
| U.S. Government Agency Mortgage- Backed Securities | 290,939,453 | - | 290,939,453 | - | 1,821 |
| Repurchase Agreements | 118,189,506 | 118,189,506 | - | - | 2 |
| Local Government Investment Pool | 509,563,594 | - | 509,563,594 | - | 2 |
| Corporate Bonds | 50,188,027 | 50,188,027 | - | - | 570 |
| International Bank for Reconstruction & Deve | 44,743,700 | 44,743,700 | - | - | 1,714 |
| | <u>\$ 2,729,827,393</u> | <u>\$ 1,490,400,743</u> | <u>\$ 1,239,426,651</u> | <u>\$ -</u> | |

Weighted Average Maturity of the City's Pooled Investments 1,026

| Investments | Fair Value as of December 31, 2018 | Fair Value Measurements Using | | | Weighted Average Maturity (Days) |
|---|---|-------------------------------|-----------------------|-------------------|---|
| | | Level 1 Inputs | Level 2 Inputs | Level 3 Inputs | |
| U.S. Government Agency Securities | \$ 986,081,743 | \$ 986,081,743 | \$ - | \$ - | 1,052 |
| U.S. Treasury and U.S. Government- Backed Securities | 449,668,993 | 449,668,993 | - | - | 840 |
| Municipal Bonds | 361,335,017 | - | 361,335,017 | - | 1,954 |
| Commercial Paper | 114,534,384 | - | 114,534,384 | - | 14 |
| U.S. Government Agency Mortgage- Backed Securities | 295,828,238 | - | 295,828,238 | - | 432 |
| Repurchase Agreements | 109,436,707 | 109,436,707 | - | - | 1 |
| Local Government Investment Pool | 143,657,503 | - | 143,657,503 | - | 1 |
| Bank Note | 8,098,219 | 8,098,219 | - | - | 22 |
| | <u>\$ 2,468,640,804</u> | <u>\$ 1,553,285,662</u> | <u>\$ 915,355,142</u> | <u>\$ -</u> | |

Weighted Average Maturity of the City's Pooled Investments 912

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 2 – Cash and Equity in Pooled Investments (continued)

The Fund's share of the City pool was as follows as of December 31:

| | <u>2019</u> | <u>2018</u> |
|---|---------------------------|---------------------------|
| Operating cash and equity in pooled investments | \$ 230,631,233 | \$ 184,599,555 |
| Restricted cash and equity in pooled investments | <u>88,092,415</u> | <u>152,136,162</u> |
| Total | <u>\$ 318,723,648</u> | <u>\$ 336,735,717</u> |
| Balance as a percentage of City pool cash and investments | 11.7% | 13.6% |

Concentration of credit risk – Concentration Risk is the risk of loss attributed to the magnitude of investments in a single issuer. The City manages concentration risk by limiting its investments in any one issuer in accordance with the City's investment policy and state statutes. The policy limits vary for each investment category. State statute and the City's Statement of Investment Policy do not stipulate concentration limits for holdings of U.S. Government or U.S. Government Agency Obligations. However, as noted under credit risk, the City's Statement of Investment Policy outlines maximum percentage allocations for municipal securities, commercial paper as well as bank notes and corporate notes. The City's investments in which five percent or more is invested in any single issuer, as of December 31 are as follows:

| <u>Issuer</u> | <u>2019</u> | | <u>2018</u> | |
|--|-------------------|---|-------------------|---|
| | <u>Fair Value</u> | <u>Percent of Total Investments</u> | <u>Fair Value</u> | <u>Percent of Total Investments</u> |
| United States Government | \$ 583,535,317 | 21% | \$ 449,668,993 | 18% |
| Local Government Investment Pool | 509,563,594 | 19% | 143,657,503 | 6% |
| Federal Home Loan Mortgage Corp | 293,802,918 | 11% | 144,168,950 | 6% |
| Federal National Mortgage Association | 283,978,980 | 10% | 324,783,135 | 13% |
| Federal Home Loan Bank | 244,714,007 | 9% | 328,232,508 | 13% |
| Federal Farm Credit Bank | 162,187,740 | 6% | 328,716,755 | 13% |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 3 – Capital Assets

Capital asset activity consisted of the following for the year ended December 31, 2019:

| | Beginning Balance | Additions and Transfers In | Retirements and Transfers Out | Ending Balance |
|---|-------------------------|----------------------------------|-------------------------------------|-------------------------|
| Buildings | \$ 24,656,787 | \$ 312,244 | \$ - | \$ 24,969,031 |
| Structures | 1,167,784,504 | 32,597,517 | (452,580) | 1,199,929,441 |
| Machinery and equipment | 105,465,391 | 11,497,317 | (2,397,901) | 114,564,808 |
| Computer systems | 72,929,653 | 849,796 | (9,187,658) | 64,591,791 |
| Total capital assets, excluding land | 1,370,836,335 | 45,256,874 | (12,038,139) | 1,404,055,071 |
| Less accumulated depreciation | (387,698,799) | (32,825,355) | 11,999,783 | (408,524,370) |
| | 983,137,536 | 12,431,519 | (38,356) | 995,530,701 |
| Construction in progress | 135,164,900 | 105,534,157 | (56,629,598) | 184,069,459 |
| Land and land rights | 40,330,857 | 18 | - | 40,330,875 |
| Artwork | 2,026,721 | 165,563 | - | 2,192,284 |
| Capital assets, net | <u>\$ 1,160,660,014</u> | <u>\$ 118,131,257</u> | <u>\$ (56,667,954)</u> | <u>\$ 1,222,123,319</u> |

Capital asset activity consisted of the following for the year ended December 31, 2018:

| | Beginning Balance | Additions and Transfers In | Retirements and Transfers Out | Ending Balance |
|---|-------------------------|----------------------------------|-------------------------------------|-------------------------|
| Buildings | \$ 23,057,745 | \$ 1,599,042 | \$ - | \$ 24,656,787 |
| Structures | 1,126,435,916 | 41,929,081 | (580,493) | 1,167,784,504 |
| Machinery and equipment | 106,199,839 | 6,033,948 | (6,768,396) | 105,465,391 |
| Computer systems | 63,878,430 | 9,516,935 | (465,712) | 72,929,653 |
| Total capital assets, excluding land | 1,319,571,930 | 59,079,006 | (7,814,601) | 1,370,836,335 |
| Less accumulated depreciation | (358,505,412) | (32,917,427) | 3,724,040 | (387,698,799) |
| | 961,066,518 | 26,161,579 | (4,090,561) | 983,137,536 |
| Construction in progress | 122,606,721 | 94,366,786 | (81,808,607) | 135,164,900 |
| Land and land rights | 23,690,882 | 16,639,975 | - | 40,330,857 |
| Artwork | 2,026,721 | - | - | 2,026,721 |
| Capital assets, net | <u>\$ 1,109,390,842</u> | <u>\$ 137,168,340</u> | <u>\$ (85,899,168)</u> | <u>\$ 1,160,660,014</u> |

During 2019 and 2018, the Fund capitalized interest costs relating to construction of \$8,100,208 and \$6,392,939, respectively.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 4 – Revenue Bonds

The Fund issues bonds to provide financing for capital improvements. Payment of debt service on the bonds is derived solely from the revenues generated by the Fund. The Fund has \$30,872,471 in a debt service reserve fund and has obtained reserve insurance policies to meet the remainder of its reserve requirements. The total bonds outstanding as of December 31, 2019 and 2018, were \$769,605,000 and \$796,030,000, respectively. Revenue bonds outstanding as of December 31, 2019 and 2018, consisted of the following Municipal Drainage and Wastewater bonds:

| Name of Issue | Issuance Date | Maturity Years | Interest Rates | Original Issue Amount | Bonds Outstanding | |
|------------------------------|---------------|----------------|----------------|-----------------------|-----------------------|-----------------------|
| | | | | | 2019 | 2018 |
| 2009A parity bonds | 12/17/09 | 2017-2039 | 4.2-5.5% | \$ 102,535,000 | \$ 93,210,000 | \$ 96,405,000 |
| 2009B parity refunding bonds | 12/17/09 | 2010-2027 | 2.0-4.0% | 36,680,000 | 9,565,000 | 10,540,000 |
| 2012 parity refunding bonds | 6/27/12 | 2012-2042 | 2.0-5.0% | 222,090,000 | 171,790,000 | 179,815,000 |
| 2014 parity refunding bonds | 7/10/14 | 2015-2044 | 3.0-5.0% | 133,180,000 | 123,475,000 | 125,585,000 |
| 2016 parity refunding bonds | 6/22/16 | 2016-2046 | 4.0-5.0% | 160,910,000 | 153,755,000 | 157,480,000 |
| 2017 parity refunding bonds | 6/28/17 | 2018-2047 | 4.0-5.0% | 234,125,000 | 217,810,000 | 226,205,000 |
| | | | | <u>\$ 889,520,000</u> | <u>\$ 769,605,000</u> | <u>\$ 796,030,000</u> |

Minimum debt service requirements to maturity on revenue bonds are as follows:

| Years Ending December 31, | Principal | Interest | Total |
|---------------------------|-----------------------|-----------------------|-------------------------|
| 2020 | \$ 27,575,000 | \$ 34,273,978 | \$ 61,848,978 |
| 2021 | 27,300,000 | 32,996,413 | 60,296,413 |
| 2022 | 28,610,000 | 31,651,003 | 60,261,003 |
| 2023 | 28,640,000 | 30,228,553 | 58,868,553 |
| 2024 | 30,035,000 | 28,800,297 | 58,835,297 |
| 2025 - 2029 | 165,420,000 | 120,990,333 | 286,410,333 |
| 2030 - 2034 | 163,370,000 | 82,074,200 | 245,444,200 |
| 2035 - 2039 | 150,940,000 | 47,719,580 | 198,659,580 |
| 2040 - 2044 | 108,210,000 | 19,560,800 | 127,770,800 |
| 2045 - 2049 | 39,505,000 | 2,763,298 | 42,268,298 |
| | <u>\$ 769,605,000</u> | <u>\$ 431,058,455</u> | <u>\$ 1,200,663,455</u> |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 4 – Revenue Bonds (continued)

The following table shows the revenue bond activity during the year ended December 31, 2019:

| | Beginning Balance | Additions | Reductions | Ending Balance | Due Within One Year |
|-------------------------------|-----------------------|-------------|------------------------|-----------------------|------------------------|
| Bonds payable | | | | | |
| Revenue bonds | \$ 796,030,000 | \$ - | \$ (26,425,000) | \$ 769,605,000 | \$ 27,575,000 |
| Add (deduct) deferred amounts | | | | | |
| Issuance premiums | 84,887,787 | - | (3,286,891) | 81,600,896 | - |
| Issuance discounts | (475,209) | - | 23,760 | (451,449) | - |
| Total bonds payable | <u>\$ 880,442,578</u> | <u>\$ -</u> | <u>\$ (29,688,131)</u> | <u>\$ 850,754,447</u> | <u>\$ 27,575,000</u> |

The following table shows the revenue bond activity during the year ended December 31, 2018:

| | Beginning Balance | Additions | Reductions | Ending Balance | Due Within One Year |
|-------------------------------|-----------------------|-------------|------------------------|-----------------------|------------------------|
| Bonds payable | | | | | |
| Revenue bonds | \$ 821,255,000 | \$ - | \$ (25,225,000) | \$ 796,030,000 | \$ 26,425,000 |
| Add (deduct) deferred amounts | | | | | |
| Issuance premiums | 88,185,775 | - | (3,297,988) | 84,887,787 | - |
| Issuance discounts | (498,969) | - | 23,760 | (475,209) | - |
| Total bonds payable | <u>\$ 908,941,806</u> | <u>\$ -</u> | <u>\$ (28,499,228)</u> | <u>\$ 880,442,578</u> | <u>\$ 26,425,000</u> |

Defeasance of debt – The Fund defeases certain obligations by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. As a result, the old bonds are considered defeased, and the corresponding liabilities and trust account assets are not included in the statement of net position. No bonds were defeased in 2019.

In 2018, \$68,380,000 bonds were redeemed as shown below:

| Name of Issue | Amount Outstanding at December 31, 2017 | Additions | Redemptions | Amount Outstanding at December 31, 2018 |
|---------------|--|-------------|------------------------|--|
| 2008 Parity | <u>\$ 68,380,000</u> | <u>\$ -</u> | <u>\$ (68,380,000)</u> | <u>\$ -</u> |

Financial covenants – The revenue bonds contain certain financial covenants, the most significant of which requires the Fund to maintain net revenue available for debt service of at least equal to 125% of annual debt service. For 2019, net revenue available for debt service, as defined by the bond covenants, is 303% of annual debt service. Management believes the Fund was in compliance with all debt covenants as of December 31, 2019. For more information, see Other Information (page 50).

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 5 – Leases

The Fund has noncancelable operating lease commitments for real and personal property, with payments of \$131,332 and \$55,375 and in 2019 and 2018, respectively. The Fund has three leases. The two existing leases at 5821 First Avenue South and 2702 6th Avenue South expire on July 31, 2020. A new 10-year lease for the property at 4209 21st Avenue West has terms from October 1, 2019 to September 30, 2029. Rents are paid as they become due and payable. Minimum lease payments under the leases for the years ending December 31 are as follows:

| | | |
|-------------|----|-------------------------|
| 2020 | \$ | 321,416 |
| 2021 | | 310,360 |
| 2022 | | 318,119 |
| 2023 | | 325,878 |
| 2024 | | 333,637 |
| 2025 - 2029 | | <u>1,690,007</u> |
| | \$ | <u><u>3,299,417</u></u> |

Note 6 – Postemployment Benefit Plans

Deferred compensation – The City offers all of its employees a deferred compensation plan (the Plan) created in accordance with Internal Revenue Code (IRC) Section 457. The Plan permits employees to defer a portion of their salaries until future years. The deferred compensation is paid to employees upon termination, retirement, death, or unforeseen emergency.

The Plan is an eligible deferred compensation plan under Section 457 of the IRC of 1986, as amended, and a trust exempt from tax under IRC Sections 457(g) and 501(a). The Plan is operated for the exclusive benefit of participants and their beneficiaries. No part of the corpus or income of the Plan shall revert to the City or be used for, or diverted to, purposes other than the exclusive benefit of participants and their beneficiaries. The Plan is not reported in the financial statements of the City or the Fund.

It is the opinion of the City’s legal counsel that the City has no liability for investment losses under the Plan. Under the Plan, participants select investments from alternatives offered by the Plan Administrator, who is under contract with the City to manage the Plan. Investment selection by a participant may be changed from time to time. The City does not manage any of the investment selections. By making the selection, participants accept and assume all risks inherent in the Plan and its administration.

Other postemployment benefits

Plan description – Health care plans for active and retired employees are administered by the City of Seattle as single-employer defined benefit public employee health care plans.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 6 – Postemployment Benefit Plans (continued)

Employees retiring under the City may continue their health insurance coverage under the City's health insurance plans for active employees. When a retired participant dies, the spouse remains fully covered until age 65 and covered by the Medicare supplement plan thereafter. Employees that retire with disability retirement under the City may continue their health coverage through the City with same coverage provisions as other retirees. Eligible retirees self-pay 100 percent of the premium based on blended rates which were established by including the experience of retirees with the experience of active employees for underwriting purposes. The postemployment benefit provisions are established and may be amended by ordinance of the Seattle City Council and as provided in Seattle Municipal Code 4.50.020. The City provides an implicit subsidy of the post-retirement health insurance costs and funds the subsidy on a pay-as-you-go basis.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

Calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and plan members in the future. Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets. Based on the latest biennial actuarial valuation date the significant methods and assumptions are as follows:

Actuarial data and assumptions – the demographic assumptions of mortality, termination, retirement, and disability are set equal to the assumptions used for City pension actuarial valuations based on a Seattle City Employees' Retirement System Experience Report for the period 2014-2017.

| | |
|---------------------------------------|--|
| Valuation date | January 1, 2019 |
| Actuarial cost method | Entry age normal |
| Amortization method | Level dollar |
| Discount rate | 4.10% |
| Health care cost trend rates—medical: | 6.77% in 2019, decreasing to 6.55% in 2020, and decreasing by varying amounts until 2030 thereafter. |
| Health care cost trend rates—Rx: | 9.50% in 2019, decreasing to 9.00% in 2020, and decreasing by varying amounts until 2030 thereafter. |
| Participation | 25% of Active Employees who retire participate |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 6 – Postemployment Benefit Plans (continued)

Mortality

General Service (Actives)

Males: RP-2014 Employees Table for Males, adjusted by 60%.

Females: RP-2014 Employees Table for Females, adjusted by 95%

Rates are projected generationally using Scale MP-2014 ultimate rates

General Service (Retirees)

Males: RP-2014 Healthy Annuitant Males, adjusted by 95%

Females: RP-2014 Healthy Annuitant Females, adjusted by 95%

Rates are projected generationally using Scale MP-2014 ultimate rates

Marital status – 35% of members electing coverage: married or have a registered domestic partner. Male spouses two years older than their female spouses.

Health Care Claims Development – The sample per capita claim cost assumptions shown below by age, benefit, and plan represent the true underlying baseline experience estimated for the City of Seattle’s sponsored postretirement benefits and costs.

| Age | Aetna Preventive Plan | | | Aetna Traditional Plan | | |
|-----|-----------------------|----------|--------|------------------------|----------|--------|
| | Medical | Rx | Admin | Medical | Rx | Admin |
| 50 | \$ 9,368 | \$ 2,621 | \$ 465 | \$ 9,599 | \$ 2,731 | \$ 465 |
| 52 | 10,191 | 2,852 | 465 | 10,443 | 2,970 | 465 |
| 55 | 11,563 | 3,236 | 465 | 11,849 | 3,370 | 465 |
| 57 | 12,603 | 3,527 | 465 | 12,914 | 3,673 | 465 |
| 60 | 14,341 | 4,013 | 465 | 14,694 | 4,180 | 465 |
| 62 | 15,452 | 4,324 | 465 | 15,832 | 4,504 | 465 |

| Age | Group Health Deductible | | | Group Health Standard | | |
|-----|-------------------------|----------|--------|-----------------------|----------|--------|
| | Medical | Rx | Admin | Medical | Rx | Admin |
| 50 | \$ 4,534 | \$ 1,215 | \$ 734 | \$ 4,285 | \$ 1,097 | \$ 734 |
| 52 | 4,932 | 1,321 | 734 | 4,661 | 1,193 | 734 |
| 55 | 5,596 | 1,499 | 734 | 5,288 | 1,353 | 734 |
| 57 | 6,099 | 1,634 | 734 | 5,764 | 1,475 | 734 |
| 60 | 6,939 | 1,859 | 734 | 6,559 | 1,679 | 734 |
| 62 | 7,476 | 2,004 | 734 | 7,067 | 1,810 | 734 |

**Seattle Public Utilities –
Drainage and Wastewater Fund
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Notes to Financial Statements**

Note 6 – Postemployment Benefit Plans (continued)

The average medical/Rx per capita claims costs were developed from calendar year 2019 fully insured premium rates for Aetna plans or self-funded premium-equivalent rates for Group Health (acquired by Kaiser Permanente in 2017) plans. Premium or premium-equivalent rates were provided by the City of Seattle’s health pricing actuary. The average medical/Rx per capita claims costs were trended to the mid-point of the annual period following the valuation date. Average medical/ Rx per capita claims costs were then age-adjusted based on the demographics of the population, and the assumed health care aging factors shown in the morbidity factors table below.

For the Aetna plans only, the average medical/Rx per capita claims costs were blended with the 2017 medical/Rx per capital developed claims cost trended forward to the valuation date.

Morbidity factors – The claim costs for medical and prescription drugs were assumed to increase with age according to the table below.

| Age | Medical | Rx | Composite |
|-------|---------|------|-----------|
| 40–44 | 3.0% | 4.8% | 3.3% |
| 45–49 | 3.7% | 4.7% | 3.8% |
| 50–54 | 4.2% | 4.7% | 4.3% |
| 55–59 | 4.4% | 4.6% | 4.4% |
| 60–64 | 3.7% | 4.6% | 3.8% |
| 65–69 | 2.7% | 3.8% | 3.1% |
| 70–74 | 1.8% | 2.5% | 2.1% |
| 75–79 | 2.2% | 0.8% | 1.4% |
| 80–84 | 2.8% | 0.2% | 1.3% |
| 85–89 | 1.4% | 0.1% | 0.6% |
| 90+ | 0.0% | 0.0% | 0.0% |

Other considerations – Active employees with current spouse and/or dependent coverage elect same plan and coverage. After retirement, it is assumed that children will have aged off coverage and will have \$0 liability.

**Seattle Public Utilities –
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Note 6 – Postemployment Benefit Plans (continued)

OPEB liability – The Fund reported an OPEB liability of approximately \$3.0 million in 2019 and 2018. The Fund’s proportionate share of the OPEB liability was 4.87% and 4.84% for the years ended December 31, 2019 and December 31, 2018. Based on the actuarial valuation date of January 1, 2019, details regarding the Fund’s Total OPEB Liability, Plan Fiduciary Net Position, and Net OPEB Liability as of December 31, 2019, are shown below.

| <i>(\$ in thousands)</i> | <u>Total OPEB Liability</u> |
|--|--|
| Changes recognized for the fiscal year: | |
| Service cost | \$ 187.1 |
| Interest on the total OPEB liability | 106.9 |
| Differences between expected and actual experience | 0.0 |
| Changes of assumptions | (189.3) |
| Benefit payments | (113.6) |
| Contributions from the Employer | 0.0 |
| Other Changes | <u>20.8</u> |
| Net Changes | 11.9 |
| Balance recognized at 12/31/2018 | <u>2,956.2</u> |
| Balance recognized at 12/31/2019 | <u><u>\$ 2,968.1</u></u> |

The Fund recorded an expense for OPEB of \$227,322 in 2019 and \$263,806 in 2018. The Health Care Subfund of the General Fund is reported in The City of Seattle’s Comprehensive Annual Financial Report.

Discount rate and healthcare cost trend rates – The discount rate used to measure the total OPEB liability is 4.10 % for 2019 and 3.44% for 2018. The following tables present the sensitivity of net OPEB liability calculation to a 1% increase and a 1% decrease in the discount rate used to measure the total OPEB liability:

**Seattle Public Utilities –
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Notes to Financial Statements**

Note 6 – Postemployment Benefit Plans (continued)

| | Discount Rate Sensitivity <i>(in millions)</i> | OPEB Liability at December 31, 2019 |
|-------------------------------|---|---|
| Discount rate | | |
| 1% decrease – 3.10% | | \$ 3.2 |
| Current discount rate – 4.10% | | 3.0 |
| 1% increase – 5.10% | | 2.7 |

| | Discount Rate Sensitivity <i>(in millions)</i> | OPEB Liability at December 31, 2018 |
|-------------------------------|---|---|
| Discount rate | | |
| 1% decrease – 2.44% | | \$ 3.2 |
| Current discount rate – 3.44% | | 3.0 |
| 1% increase – 4.44% | | 2.7 |

The following table presents the sensitivity of net Health Plan OPEB liability calculation to a 1% increase and a 1% decrease in the healthcare cost trend rates used to measure the total Health Plan OPEB liability:

| | Healthcare Cost Trend Rate Sensitivity <i>(in millions)</i> | | OPEB Liability at December 31, | |
|---------------|--|--------|-----------------------------------|------|
| | 2019 | 2018 | 2019 | 2018 |
| Discount rate | | | | |
| 1% decrease | \$ 2.6 | \$ 2.6 | | |
| Trend rate | 3.0 | 3.0 | | |
| 1% increase | 3.4 | 3.4 | | |

**Seattle Public Utilities –
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Note 6 – Postemployment Benefit Plans (continued)

Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB – The following table presents information about the OPEB-related deferred outflows of resources and deferred inflows of resources for the Fund at December 31, 2019.

| <i>(in thousands)</i> | <u>Deferred Outflows</u> | <u>Deferred Inflows</u> |
|---|------------------------------|-----------------------------|
| Difference between actual and expected experience | \$ 512.5 | \$ - |
| Assumption changes | - | 1,009.0 |
| Contributions made in 2019 after measurement date | <u>121.0</u> | <u>N/A</u> |
| Total | <u>\$ 633.5</u> | <u>\$ 1,009.0</u> |

The Fund's contributions made in 2019 in the amount of \$120,986 are reported as deferred outflows of resources and will be recognized as a reduction of the net OPEB liability in the year ended December 31, 2019. These contributions will be recognized in the future as shown in the following table. Note that additional future deferred outflows and inflows of resources may impact these amounts.

| <i>Year Ending December 31, (in thousands)</i> | <u>Amortization</u> |
|--|---------------------|
| 2020 | \$ (66.7) |
| 2021 | (66.7) |
| 2022 | (66.7) |
| 2023 | (66.7) |
| 2024 | (66.7) |
| Thereafter | <u>(163.3)</u> |
| Total | <u>\$ (496.8)</u> |

The Health Care Subfund of the General Fund is reported in the City's Comprehensive Annual Financial Report which can be obtained by writing the Department of Finance, City of Seattle, PO Box 94747, Seattle, WA 98124-4747 or www.seattle.gov/cafrs/.

Note 7 – Claims Payable

The City and the Fund are self-insured for certain losses arising from personal and property damage claims by third parties and for casualty losses to the Fund's property. Liabilities for identified claims and claims incurred, but not reported have been recorded by the Fund.

**Seattle Public Utilities –
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Note 7 – Claims Payable (continued)

For 2019 and 2018, liabilities for workers' compensation claims, as well as other claims, are discounted over a 15-year period at the City's rate of return on investments, 2.334% and 1.978%, respectively. Claims expected to be paid within one year are \$1,630,749 and \$1,507,535 as of December 31, 2019 and 2018, respectively. The schedules below present the changes in the liability for workers' compensation claims and other claims (risk financing liabilities) as of December 31:

| | 2019 | 2018 |
|--|--------------|--------------|
| Beginning liability, discounted | \$ 6,964,736 | \$ 7,399,982 |
| Payments | (544,550) | (993,756) |
| Incurred claims and change in estimate | 759,891 | 558,510 |
| | \$ 7,180,077 | \$ 6,964,736 |
| Ending liability, discounted | | |

The Fund is involved in litigation from time to time as a result of operations.

Note 8 – Compensated Absences

The Fund has recorded a liability for earned but unused compensatory and vacation leave, as well as estimated sick leave payments calculated based on the termination payment method. The schedules below show the compensated absences activity during the years ended December 31, 2019 and 2018:

| | 2019 | 2018 |
|---------------------|--------------|--------------|
| Beginning liability | \$ 4,349,112 | \$ 4,944,463 |
| Additions | 6,197,063 | 5,101,088 |
| Reductions | (5,620,297) | (5,696,439) |
| | \$ 4,925,878 | \$ 4,349,112 |
| Ending liability | | |

Note 9 – Pension Benefit Plan

Plan description – The Seattle City Employees' Retirement System (the System) is a cost-sharing multiple employer pension plan covering employees of the City of Seattle and is administered in accordance with Chapter 4.36 of the Seattle Municipal Code.

The System is governed by the Retirement System Board of Administration (the Board). The Board consists of seven members including the Chair of the Finance Committee of the Seattle City Council, the City of Seattle Finance Director, the City of Seattle Personnel Director, two active members and one retired member of the System who are elected by other System members, and one outside board member who is appointed by the other six board members. Elected and appointed board members serve for three-year terms.

**Seattle Public Utilities –
Drainage and Wastewater Fund
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Notes to Financial Statements**

Note 9 – Pension Benefit Plan (continued)

System benefits – The System provides retirement, death, and disability benefits. Retirement benefits vest after five years of credited service, while death and disability benefits vest after ten years of service. All permanent Fund employees are eligible to participate in the System. Members are eligible for retirement benefits after 30 years of service; at age 52 after 20 years of service; at age 57 after ten years of service; and at age 62 after five years of service.

Member and employer contributions – Employees are required to contribute 10.03% of their annual base salaries to the System. The employer’s contribution rate for the years ended December 31, 2019 and 2018, was 15.23% and 15.29%, respectively. Employer rates are established by the City Council on a biannual basis. The Fund’s contributions to the System for the years ended December 31, 2019 and 2018, were \$7,273,022 and \$7,205,678 respectively.

The System issues stand-alone financial statements, which may be obtained by writing to the Seattle City Employees’ Retirement System, 720 Third Avenue, Suite 900, Seattle, Washington, 98104, and telephone: (206) 386-1293, or www.seattle.gov/retirement/annual_report.htm.

Pension liabilities, pension expense, and deferred outflows of resources and deferred inflows of resources related to pensions – At December 31, 2019 and 2018, the Fund reported a liability of \$91,293,054 and \$66,368,647, respectively, its proportionate share of the Systems’ net pension liability. The net pension liability was measured as of December 31, 2018 and 2017, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of those dates. The Fund’s proportion of the net pension liability was based on a projection of the City’s long-term share of contributions to the pension plan relative to the projected contributions of all participating parties, actuarially determined. At December 31, 2019 and 2018, the Fund’s proportion was 6.26% and 6.33%, respectively.

For the years ended December 31, 2019 and 2018, the Fund recognized pension expense of approximately \$12,121,000 and \$8,761,000, respectively.

The Fund’s deferred outflows and inflows of resources are as follows at December 31, 2019:

| | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|-----------------------------------|----------------------------------|
| Differences between expected and actual experience | \$ 33,836 | \$ 2,011,932 |
| Change of assumptions | 5,142,579 | - |
| Net difference between projected and actual earnings | 10,012,412 | - |
| Contributions made subsequent to measurement date | 6,942,096 | - |
| Changes in proportion and differences between employer contributions and proportionate share of contributions | - | 5,656,030 |
| | <hr/> | <hr/> |
| Total | <u>\$ 22,130,923</u> | <u>\$ 7,667,962</u> |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 9 – Pension Benefit Plan (continued)

The Fund's deferred outflows and inflows of resources are as follows at December 31, 2018:

| | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|-----------------------------------|----------------------------------|
| Differences between expected and actual experience | \$ 57,092 | \$ 1,820,458 |
| Net difference between projected and actual earnings | (6,305,173) | - |
| Contributions made subsequent to measurement date | 6,874,752 | - |
| Changes in proportion and differences between employer contributions and proportionate share of contributions | - | 6,855,370 |
| | <u> </u> | <u> </u> |
| Total | <u>\$ 626,671</u> | <u>\$ 8,675,828</u> |

Other amounts currently reported as deferred outflows and inflows of resources will be recognized in pension expense as follows for years ending December 31:

| | |
|-------|-----------------------------|
| 2019 | \$ 1,739,764 |
| 2020 | (100,328) |
| 2021 | 948,988 |
| 2022 | 4,448,203 |
| 2023 | 484,238 |
| | <u> </u> |
| Total | <u>\$ 7,520,865</u> |

Actuarial assumptions – The total pension liability as of December 31, 2019, was determined using the following actuarial assumptions:

| | |
|----------------------------------|--|
| Valuation date | January 1, 2018 |
| Measurement date | December 31, 2018 |
| Actuarial cost method | Individual Entry Age Normal |
| Amortization method | Level Percent, Closed |
| Remaining amortization period | 30 years as of January 1, 2013 valuation |
| Asset valuation method | 5-Year Non-asymptotic |
| Inflation | 2.75% |
| Investment rate of return | 7.25% compounded annually, net of expenses |
| Discount rate | 7.25% |
| Projected general wage inflation | 3.5% |
| Postretirement benefit increases | 1.5% |
| Mortality | generational projection of improvement using MP-2014 Ultimate projection scale. See 2018 Investigation of Experience report for details. |

The actuarial assumptions that determined the total pension liability as of the measurement date were based on the results of an actuarial experience study for the period January 1, 2014, through December 31, 2017.

**Seattle Public Utilities –
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Notes to Financial Statements**

Note 9 – Pension Benefit Plan (continued)

The discount rate used to measure the pension liability is based on a projection of cash flows assuming that plan member contributions will be made at the current contribution rate and that participating employer contributions will be made at rates equal to the difference between actuarially determined contribution rates and the member rate. Based on those assumptions, the System’s fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods on projected benefit payment to determine total pension liability.

The long-term expected rate of return assumption was based on the System’s investments using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expect future real rates of return by the target asset allocation percentage and by adding expected inflation.

Best estimates of geometric real rates of return for each major asset class included in the System’s target asset allocation as of December 31, 2018, are summarized in the following table:

| <u>Asset Class</u> | <u>Long-Term Expected Real Rate of Return</u> |
|-----------------------------|---|
| Equity: Public | 5.43% |
| Equity: Private | 8.40% |
| Fixed Income: Broad | 1.62% |
| Fixed Income: Credit | 4.30% |
| Real Assets: Real Estate | 3.90% |
| Real Assets: Infrastructure | 4.25% |
| Diversifying Strategies | 4.01% |

Sensitivity analysis – The following presents the Fund’s proportionate share of the net pension liability calculated using the discounted rate of 7.25%, as well as what the employer’s proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.25%) or 1 percentage point higher (8.25%) than the current rate.

| <u>1% Decrease 6.25%</u> | <u>Current Discount Rate 7.25%</u> | <u>1% Increase 8.25%</u> |
|----------------------------------|--|----------------------------------|
| \$ 122,189,097 | \$ 91,293,054 | \$ 64,349,024 |

**Seattle Public Utilities –
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Notes to Financial Statements**

Note 10 – Environmental Liabilities

Following is a brief description of the significant sites that require environmental remediation:

Duwamish sites – The U.S. Environmental Protection Agency (EPA) has indicated that it will require the clean-up and remediation of certain Duwamish sites under its Superfund authority. In order to manage the liability, the City has worked with the EPA and other PRPs to complete a Remedial Investigation (RI) and Feasibility Study (FS). On November 2, 2012, the EPA and Ecology approved the Lower Duwamish Waterway Group’s FS. The EPA announced their proposed cleanup plan in February 2013 for public comment. The remaining scope of cleanup by potentially responsible parties (PRPs) has been decided by the EPA in the 2014 Record of Decision. The Fund recorded an estimate of its share of the estimated total cost. Remedial design work began in 2019.

Specific “early action sites” have been cleaned up separately under Administrative Orders on Consent (AOC). The Fund, together with other PRPs, has completed two early action sites identified during the RI under EPA issued AOC: Slip 4 and T-117.

East Waterway Site – In 2006 the EPA issued an AOC for a Supplemental RI and FS for the East Waterway, an operable unit of the Harbor Island Superfund Site. The Port of Seattle (the Port) alone signed the AOC. Both the City and King County signed a Memorandum of Agreement with the Port to participate as cost share partners in the RI/FS work required by the EPA. The RI is complete, and a draft final FS was submitted to EPA in early 2019. The FS identifies a range of alternatives for cleanup construction that range in cost from \$256 million to \$411 million. Once the FS is approved, EPA will then develop a Proposed Plan followed by a Record of Decision. The schedule for release of EPA’s Proposed Plan is 2020. The Record of Decision is expected in 2021. Remedial design activities would start in late 2021 at the earliest. The Fund recorded an estimate of its share of the estimated total cost.

Gas Works Park Sediment Site – In April 2002, the Department of Ecology (DOE) named the City and another party, Puget Sound Energy, as PRPs for contamination at the Gas Works Sediments Site in North Lake Union. The City and Puget Sound Energy signed an Agreed Order with the DOE in 2005 to initiate two RIs and FSs for the sediment site – one in the western portion of the site led by the City, and another in the eastern portion of the site led by Puget Sound Energy. Subsequently, in fall of 2012, the City and Puget Sound Energy entered into a Settlement, Release, and Cost Allocation Agreement that puts Puget Sound Energy in the lead for all additional cleanup work at the site; the east-west split is no longer in place. Based on the 2012 Agreement, the City pays for 20% of the Shared Costs incurred by Puget Sound Energy for the cleanup work. The RI and FS include an evaluation of the nature and extent of contamination on the site, an evaluation of multiple alternatives for remediating the sediments and a recommended preferred alternative. Puget Sound Energy collected additional environmental data in 2013 and the draft RI/FS was submitted to DOE in March 2016. A revised draft RI/FS is anticipated to be submitted to DOE in 2020 A Clean-up Action Plan, which is the States’ equivalent to a Record of Decision under the Model Toxics Control Act, is expected in 2021.

Seattle Public Utilities – Drainage and Wastewater Fund (An Enterprise Fund of the City of Seattle) Notes to Financial Statements

Note 10 – Environmental Liabilities (continued)

North Boeing Field/Georgetown Steam Plant – The City, King County, and Boeing have signed an Administrative Order with the DOE requiring them to investigate and possibly remove contamination in an area that encompasses North Boeing Field, the Georgetown Steam Plant, and the King County Airport.

7th Avenue South Pump Station – The City acquired land in the South Park area of Seattle to construct the 7th Ave South Pump Station. The land was determined to be contaminated subsequent to the purchase. The Fund has voluntarily agreed to clean up the contamination in order to continue with the planned construction of the pump station. The cleanup was completed in 2012; however, the Fund has ongoing monitoring activities it must perform.

Terminal 108 – EPA notified the City in 2019 that it is a Potentially Responsible Party for a site adjacent to the Lower Duwamish Waterway that is known as Terminal 108 or T108. The City's potential liability arises from a former sewage treatment plant that was located there. Other PRPs include the Port of Seattle, which is the current owner of the site, King County, the United States and several private entities. The PRPs are negotiating the terms of an agreed Administrative Order with EPA and a cost-sharing agreement among themselves. The Department's ultimate liability is indeterminate.

South Park Marina – The Washington Department of Ecology notified the City in 2016 that it is a Potentially Liable Party for contamination at the South Park Marina, which is adjacent to Terminal 117. The City Light Department is the lead department for the City at this site. The Potentially Liable Parties (PLPs), which are the City, the Port and South Park Marina (SPM), signed a final Agreed Order for a Remedial Investigation (RI) in April 2019. A Common Interest and Cost Sharing Agreement among the PLPs was signed in 2019 with an interim cost share of one-third each. In 2019, the City contracted with a consultant to complete the RI. The City's share is split between City Light (97.5%) and SPU (2.5%). The Department's ultimate liability is indeterminate.

The Fund has included in its estimated liability those portions of the environmental remediation work that are currently deemed to be reasonably estimable. Cost estimates were developed using the expected cash flow technique in accordance with GASB 49. For most of the sites, estimated outlays were based on current cost and no adjustments were made for discounting or inflation. The Duwamish site cost estimates were adjusted to remove discounting and to record the costs in 2018 dollars. Cost scenarios were developed for a given site based on data available at the time of estimation and will be adjusted for changes in circumstance. Scenarios consider the relevant potential requirements and are adjusted when benchmarks are met or when new information revises estimated outlays, such as changes in the remediation plan or operating conditions. Costs were calculated on a weighted average that was based on the probabilities of each scenario being selected and reflected cost-sharing agreements in effect. In addition, certain estimates were derived from independent engineers and consultants. The estimates were made with the latest information available; however, as new information becomes available, estimates may vary significantly due to price fluctuations, technological advances, or applicable laws.

The Fund is aggressively pursuing other third parties that may have contributed to the contamination of the sites noted. The Fund's estimate for not yet realized recoveries from other parties for their share of remediation work that offset the Fund's estimated environmental liability was \$2.6 million as of December 31, 2019, and \$2.0 million as of December 31, 2018.

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 10 – Environmental Liabilities (continued)

The following changes in the provision for environmental liabilities at December 31 are:

| | <u>2019</u> | <u>2018</u> |
|--|-----------------------|-----------------------|
| Beginning environmental liability, net of recovery | \$ 174,621,792 | \$ 138,806,475 |
| Payments or amortization | (3,246,282) | (4,863,030) |
| Incurred environmental liability | <u>9,508,851</u> | <u>40,678,347</u> |
| Ending environmental liability, net of recovery | <u>\$ 180,884,361</u> | <u>\$ 174,621,792</u> |

The following table represents the current and long term portions for the environmental liabilities:

| | <u>2019</u> | <u>2018</u> |
|-------------------------------------|-----------------------|-----------------------|
| Environmental liability, current | \$ 1,730,070 | \$ 2,281,722 |
| Environmental liability, noncurrent | <u>179,154,291</u> | <u>172,340,070</u> |
| Ending liability | <u>\$ 180,884,361</u> | <u>\$ 174,621,792</u> |

Note 11 – Loans

The Fund has various construction projects that are financed by low interest loans issued by the State of Washington. The loan agreements require that the Fund finance a portion of these projects from other sources. These loans have been used to enhance the drainage system.

In 2019, The Fund entered into a 20-year loan agreement with the Washington State Department of Ecology to borrow up to \$25.0 million to support the Ship Canal Water Quality Project for protecting Lake Washington Ship Canal from combined sewer overflow from Ballard, Fremont, Wallingford, and North Queen Anne. Amounts borrowed under this agreement accrue interest at the rate of 2.0% per annum and estimated initiation of operation date is December 31, 2020. As of December 31, 2019, the Fund had drawn \$381,221 on the loan.

**Seattle Public Utilities –
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Notes to Financial Statements**

Note 11 – Loans (continued)

Loans outstanding as of December 31, 2019 and 2018, are as follows:

| Description | Maturity Years | Interest Rate | Amount Borrowed | Loans Outstanding | |
|--|-------------------|------------------|----------------------|----------------------|----------------------|
| | | | | 2019 | 2018 |
| Midvale | 2013-2031 | 0.25% | \$ 4,000,000 | \$ 2,541,249 | \$ 2,753,019 |
| Thornton Creek Natural Drainage Systems | 2006-2024 | 0.50% | 3,700,000 | 979,412 | 1,175,294 |
| High Point Natural Drainage Systems | 2010-2029 | 1.50% | 2,679,413 | 1,392,866 | 1,528,274 |
| South Park Flood Control and Local Drainage Program | 2007-2025 | 0.50% | 3,400,000 | 1,182,737 | 1,379,860 |
| Ballard Green Streets ARRA Project | 2011-2020 | 2.90% | 603,209 | 71,233 | 140,432 |
| Thornton Creek Water Quality Project | 2011-2030 | 1.50% | 6,983,021 | 4,027,198 | 4,378,706 |
| Capital Hill Water Quality Project | 2014-2033 | 2.60% | 1,880,598 | 1,454,831 | 1,539,888 |
| Henderson CSO | 2018-2037 | 2.40% | 36,372,252 | 32,984,702 | 34,483,650 |
| Ship Canal Water Quality Project | 2021-2039 | 2.00% | 381,221 | 381,221 | - |
| | | | <u>\$ 59,999,714</u> | <u>\$ 45,015,448</u> | <u>\$ 47,379,124</u> |

Minimum debt service requirements to maturity on long term loans are as follows:

| Years Ending December 31, | Principal | Interest | Total |
|---------------------------|----------------------|---------------------|----------------------|
| 2020 | \$ 2,792,896 | \$ 922,293 | \$ 3,715,189 |
| 2021 | 3,149,901 | 883,765 | 4,033,666 |
| 2022 | 2,816,776 | 820,628 | 3,637,404 |
| 2023 | 2,865,973 | 768,936 | 3,634,909 |
| 2024 | 2,916,299 | 716,116 | 3,632,415 |
| 2025 - 2029 | 13,530,911 | 2,762,605 | 16,293,516 |
| 2030 - 2034 | 11,342,621 | 1,398,190 | 12,740,811 |
| 2035 - 2039 | 5,600,070 | 204,232 | 5,804,302 |
| | <u>\$ 45,015,448</u> | <u>\$ 8,476,765</u> | <u>\$ 53,492,213</u> |

The following table shows the loan activity during the years ended December 31:

| | 2019 | 2018 |
|------------------------------|----------------------|----------------------|
| Net loans, beginning of year | \$ 47,379,124 | \$ 46,099,148 |
| Loan proceeds | 381,221 | 4,403,125 |
| Principal payments | <u>(2,744,897)</u> | <u>(3,123,149)</u> |
| Net loans, end of year | <u>\$ 45,015,448</u> | <u>\$ 47,379,124</u> |
| Loans due within one year | <u>\$ 2,792,896</u> | <u>\$ 2,744,897</u> |
| Loans, noncurrent | <u>\$ 42,222,552</u> | <u>\$ 44,634,227</u> |

**Seattle Public Utilities –
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(An Enterprise Fund of the City of Seattle)
Notes to Financial Statements**

Note 12 – Wastewater Disposal Agreement

The Fund has a wastewater disposal agreement with the King County Department of Natural Resources Wastewater Treatment Division (the Division), which expires in 2036. The monthly wastewater disposal charge paid to the Division is based on the Division's budgeted cost for providing the service. The charges are determined by water consumption and the number of single-family residences as reported by SPU and other component agencies. Payments made by the Fund were \$165,796,390 and \$167,006,025 for fiscal years 2019 and 2018, respectively.

Note 13 – Subsequent Events

Debt agreement – On April 24, 2020, the Fund entered into a 34-year loan agreement with the Water Infrastructure Finance and Innovation Act (WIFIA) to borrow up to \$192.2 million to support the Ship Canal Water Quality Project to protect Lake Washington Ship Canal from combined sewer overflow from Ballard, Fremont, Wallingford and North Queen Anne. Amounts borrowed under this agreement will accrue interest at the rate of 1.01% per annum. The Fund plans to begin drawing on this loan in early 2022. The project's expected completion date is March 2025.

Coronavirus – In March 2020, the World Health Organization declared the novel coronavirus outbreak a global pandemic. In response, the Governor of the state of Washington issued a stay-at-home order, restricting travel and the closing of all non-essential businesses. The City and SPU have implemented measures to mitigate the impacts to its operations, its employees and its customers, including closing offices, requiring employees not required to be on site for essential services to work from home, and implementing social distancing measures for employees required to be onsite. This did not have an impact to the financial results and operations for 2019. SPU will continue to monitor the situation closely, but given the uncertainty surrounding the situation, the estimated impact to SPU's future operations and financial statements cannot be determined.

Required Supplementary Information

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Required Supplementary Information**

Schedule of Seattle Public Utilities' Proportionate Share of the Net Pension Liability

| | <u>2019</u> | <u>2018</u> | <u>2017</u> | <u>2016</u> | <u>2015</u> |
|--|----------------|----------------|----------------|----------------|----------------|
| Employer's proportion of the net pension liability | 14.55% | 14.73% | 15.13% | 16.37% | 16.96 |
| Employer's proportionate share of the net pension liability | \$ 221,049,893 | \$ 163,086,154 | \$ 197,454,529 | \$ 212,671,200 | \$ 187,919,945 |
| Employer's covered payroll | \$ 111,973,027 | \$ 107,715,383 | \$ 106,696,535 | \$ 105,031,141 | \$ 102,783,473 |
| Employer's proportionate share of the net pension liability as a percentage of its covered payroll | 197.41% | 151.40% | 185.06% | 202.48% | 182.83% |
| Plan fiduciary net position as a percentage of the total pension liability | 64.14% | 72.04% | 65.60% | 64.03% | 67.70% |

Schedule of Seattle Public Utilities' Contributions

| | <u>2019</u> | <u>2018</u> | <u>2017</u> | <u>2016</u> | <u>2015</u> |
|---|---------------------|---------------------|---------------------|---------------------|---------------------|
| Contractually required employer contribution | \$ 17,103,559 | \$ 16,466,270 | \$ 16,354,089 | \$ 16,487,154 | \$ 15,170,276 |
| Contributions in relation to the contractually required employer contribution | <u>(17,103,559)</u> | <u>(16,466,270)</u> | <u>(16,354,089)</u> | <u>(16,487,154)</u> | <u>(15,170,276)</u> |
| Employer contribution deficiency (excess) | <u>\$ -</u> |
| Employer's covered payroll | \$ 111,973,027 | \$ 107,715,383 | \$ 106,696,535 | \$ 105,031,141 | \$ 102,783,473 |
| Employer contributions as a percentile of covered payroll | 15.27% | 15.29% | 15.33% | 15.70% | 14.76% |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Required Supplementary Information**

Schedule of Seattle Public Utilities' Proportionate Share of the OPEB Liability and Related Ratios

| | <u>December 31, 2019</u> | <u>December 31, 2018</u> |
|--|--------------------------|--------------------------|
| Total OPEB Liability | | |
| Normal cost | \$ 3,842,152 | \$ 3,821,876 |
| Interest | 2,195,238 | 2,583,105 |
| Differences between expected and actual experience | - | 13,491,865 |
| Changes in assumptions | (3,886,702) | (22,126,128) |
| Benefit payment | (2,333,610) | (2,289,000) |
| Total OPEB liability – beginning of year | 61,129,833 | 65,648,115 |
| Total OPEB liability – end of year | <u>\$ 60,946,911</u> | <u>\$ 61,129,833</u> |
| Covered-employee payroll | \$ 1,015,097,334 | \$ 1,015,097,334 |
| Net OPEB liability as percentage of covered-employee payroll | 6.00% | 6.02% |

Other Information (Unaudited)

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Other Information (Unaudited)**

Drainage Wastewater Debt Service Coverage Calculation 2019

| | |
|--|-----------------------|
| Operating Revenues | |
| Wastewater | \$ 304,831,874 |
| Drainage | 143,323,151 |
| Other | 6,226,840 |
| Total Operating Revenue | <u>454,381,865</u> |
| Operating Expense | |
| Wastewater Treatment Contract | 166,786,279 |
| Other Operations and Maintenance | 106,760,294 |
| City Taxes | 53,151,086 |
| Other Taxes | 5,935,952 |
| Total Operating Expenses Before Debt Service | <u>332,633,611</u> |
| Net Operating Income | <u>121,748,254</u> |
| Adjustments | |
| Add: Claim Expense | 759,891 |
| Add: City Taxes | 53,151,086 |
| Add: Investment Interest | 7,573,751 |
| Less: DSRF Earnings | (761,062) |
| Add: BAB's Subsidy | 1,686,168 |
| Add (Less): Net Other Nonoperating Revenues/(Expenses) | 1,566,959 |
| Add: Proceeds from Sale of Assets | 6,973 |
| Total Adjustments | <u>63,983,766</u> |
| Net Revenue Available for Debt Service | <u>\$ 185,732,019</u> |
| Net Revenue Available for Debt Service (w/o City Taxes) | <u>\$ 132,580,933</u> |
| | |
| Annual Debt Service | \$ 62,005,553 |
| Less: DSRF Earnings | (761,062) |
| Adjusted Annual Debt Service | <u>\$ 61,244,491</u> |
| | |
| Coverage | 3.03 |
| Coverage without taxes | 2.16 |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Other Information (Unaudited)**

Statistics Required for Revenue Bond Continuing Disclosure

Wastewater System Operating Statistics

| | <u>2014</u> | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>2018</u> | <u>2019</u> |
|---|-------------|-------------|-------------|-------------|-------------|-------------|
| Population Served | 640,500 | 662,400 | 686,800 | 713,700 | 730,400 | 747,300 |
| Billed Wastewater Revenues (in thousands) | \$ 242,844 | \$ 257,092 | \$ 262,006 | \$ 272,085 | \$ 280,554 | \$ 303,935 |
| Billed Wastewater Volume (Thousand CCF) | | | | | | |
| Residential | 7,408 | 7,546 | 7,694 | 7,699 | 7,613 | 7,723 |
| Commercial | 13,243 | 13,872 | 14,127 | 13,584 | 13,504 | 13,554 |
| Total | 20,651 | 21,418 | 21,821 | 21,283 | 21,117 | 21,277 |
| Gallons Used Per Day Per Capita | 66.03 | 66.22 | 65.07 | 61.07 | 59.21 | 58.31 |

Drainage and Wastewater – 2019 Accounts and Billed Revenues

| | <u>Drainage</u> | <u>Wastewater</u> |
|--------------------------|-----------------------|-----------------------|
| Customer Accounts | | |
| Residential | 153,472 | 154,453 |
| Commercial | 65,563 | 19,337 |
| Total | <u>219,035</u> | <u>173,790</u> |
| | | |
| | <u>Drainage</u> | <u>Wastewater</u> |
| Billed Revenue | | |
| Residential | \$ 73,190,332 | \$ 107,492,858 |
| Commercial | 68,839,659 | 201,316,311 |
| Total | <u>\$ 142,029,990</u> | <u>\$ 308,809,168</u> |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Other Information (Unaudited)**

Major Wastewater Customers – 2019 Annual Billed Revenues and Percentage of Revenue

| <u>Name</u> | <u>Revenue</u> | <u>% of Total Revenue</u> |
|-----------------------------|-----------------|---------------------------|
| University of Washington | \$ 9,776,898.11 | 3.2% |
| Seattle Housing Authority | \$ 5,548,942.77 | 1.8% |
| City of Seattle | \$ 3,198,764.09 | 1.0% |
| King County | \$ 2,683,792.58 | 0.9% |
| Equity Residential | \$ 2,604,718.34 | 0.8% |
| Marriott International Inc. | \$ 2,469,180.62 | 0.8% |
| Port of Seattle | \$ 1,537,802.83 | 0.5% |
| Hyatt | \$ 1,472,489.60 | 0.5% |
| Darigold | \$ 1,470,158.17 | 0.5% |
| Bellwether Housing | \$ 1,233,737.33 | 0.4% |

Major Drainage Customers – 2019 Annual Billed Revenues and Percentage of Revenue

| <u>Name</u> | <u>Revenue</u> | <u>% of Total Revenue</u> |
|----------------------------|----------------|---------------------------|
| City of Seattle | \$ 10,072,336 | 7.1% |
| Seattle Public Schools | \$ 3,178,904 | 2.2% |
| King County | \$ 3,088,906 | 2.2% |
| University of Washington | \$ 2,536,311 | 1.8% |
| BNSF Railway | \$ 2,346,554 | 1.7% |
| US Federal Government | \$ 1,216,782 | 0.9% |
| Seattle Housing Authority | \$ 1,048,214 | 0.7% |
| Union Pacific Railroad | \$ 927,434 | 0.7% |
| Seattle Community Colleges | \$ 648,526 | 0.5% |
| Prologis Inc | \$ 627,494 | 0.4% |

**Seattle Public Utilities –
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)
Other Information (Unaudited)**

Wastewater Rates

Note: 1 CCF equals 748 gallons. Wastewater rate increased 7.6% and 4.1% in 2019 and 2018, respectively.

Drainage Rates

| Flat Rate per Parcel | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>2018</u> | <u>2019</u> | <u>2020</u> | <u>% Impervious Space</u> |
|-------------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-----------------------------------|
| Single Family Residential* | | | | | | | |
| 0-1,999 sq. ft. | | \$ 123.81 | \$ 140.46 | \$ 159.68 | \$ 169.81 | \$ 183.47 | |
| 2,000 - 2,999 sq. ft. | \$ 198.83 | \$ 206.93 | \$ 231.47 | \$ 259.68 | \$ 276.51 | \$ 298.75 | |
| 3,000 - 4,999 sq. ft. | \$ 258.06 | \$ 286.63 | \$ 319.05 | \$ 356.15 | \$ 383.43 | \$ 414.26 | |
| 5,000 - 6,999 sq. ft. | \$ 350.40 | \$ 390.03 | \$ 432.45 | \$ 480.86 | \$ 516.72 | \$ 558.27 | |
| 7,000 - 9,999 sq. ft. | \$ 443.55 | \$ 491.40 | \$ 543.98 | \$ 603.90 | \$ 652.61 | \$ 705.09 | |
| Rate per 1,000 sq. ft. | | | | | | | |
| Undeveloped | | | | | | | |
| Regular | \$ 28.25 | \$ 31.24 | \$ 34.76 | \$ 38.78 | \$ 42.62 | \$ 46.05 | 0 - 15% |
| Low Impact | \$ 16.54 | \$ 18.57 | \$ 20.67 | \$ 23.06 | \$ 25.36 | \$ 27.40 | |
| Light | | | | | | | |
| Regular | \$ 43.69 | \$ 48.52 | \$ 53.54 | \$ 59.24 | \$ 63.64 | \$ 68.75 | 16 - 35% |
| Low Impact | \$ 34.36 | \$ 38.31 | \$ 42.26 | \$ 46.74 | \$ 49.85 | \$ 53.85 | |
| Medium | | | | | | | |
| Regular | \$ 63.45 | \$ 70.67 | \$ 77.60 | \$ 85.45 | \$ 90.58 | \$ 97.86 | 36 - 65% |
| Low Impact | \$ 51.04 | \$ 57.21 | \$ 62.86 | \$ 69.28 | \$ 73.31 | \$ 79.21 | |
| High | | | | | | | |
| | \$ 85.12 | \$ 93.56 | \$ 102.48 | \$ 112.57 | \$ 119.86 | \$ 129.50 | 66 - 85% |
| Very High | | | | | | | |
| | \$ 100.69 | \$ 112.38 | \$ 122.94 | \$ 134.85 | \$ 143.10 | \$ 154.60 | 86 - 100% |

* SFR parcels more than 10,000 sq. ft. are billed under the commercial rate structure.



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