



Report of Independent Auditors and
Financial Statements with Required
Supplementary Information and
Other Information for

**Seattle Public Utilities -
Drainage and Wastewater Fund
(An Enterprise Fund of the City of Seattle)**

December 31, 2014 and 2013

MOSS-ADAMS_{LLP}

Certified Public Accountants | Business Consultants

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REPORT OF INDEPENDENT AUDITORS

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

Report on 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, 2014 and 2013, 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 an opinion 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. Those standards require that we plan and perform the audits 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 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 financial position of Seattle Public Utilities - Drainage and Wastewater Fund as of December 31, 2014 and 2013, and the results of its operations and its 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

The accompanying management discussion and analysis is not part of the financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. This information, although not a part of the 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 financial statements, and other knowledge we obtained during our audit of the 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 financial statements taken as a whole. The other information on pages 43-45 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion or provide any assurance on it.

Moss Adams LLP

Seattle, Washington

April 30, 2015, except as to Note 13, which is as of July 2, 2015

**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, 2014 and 2013. The revenues, expenses, assets, deferred outflows of resources, and liabilities of the City of Seattle’s drainage and wastewater system are recorded in the Drainage and Wastewater 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 14 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, 2014 and 2013, on all of the Fund’s assets, deferred outflows of resources, and liabilities. The difference between assets combined with deferred outflows of resources and liabilities 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 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, 2014 and 2013. 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, 2014 and 2013. 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.

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MANAGEMENT'S DISCUSSION AND ANALYSIS**

OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED)

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 19 of this report.

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, 2014 and 2013, the Fund's assets and deferred outflows of resources exceeded liabilities, resulting in a surplus of total assets of \$344.1 million and \$295.6 million, respectively. In 2014, the Fund's overall position improved, with an increase in net position of \$48.5 million (16.4%) as compared to an increase in net position of \$24.6 million (9.1%) in 2013. The following summary statements of net position present the assets of the Fund and show the mix of liabilities and net position used to acquire these assets:

STATEMENTS OF NET POSITION

	<u>2014</u>	<u>2013</u>	<u>2012</u>
ASSETS			
Current assets	\$ 142,586,093	\$ 118,469,314	\$ 100,945,852
Capital assets, net	843,837,995	765,496,217	699,131,240
Other	163,283,878	111,118,802	179,031,335
Total assets	<u>1,149,707,966</u>	<u>995,084,333</u>	<u>979,108,427</u>
DEFERRED OUTFLOWS OF RESOURCES	<u>6,478,895</u>	<u>6,054,354</u>	<u>6,428,342</u>
Total assets and deferred outflows of resources	<u>\$ 1,156,186,861</u>	<u>\$ 1,001,138,687</u>	<u>\$ 985,536,769</u>
LIABILITIES			
Current liabilities	\$ 67,827,554	\$ 63,638,332	\$ 59,447,182
Revenue bonds	646,693,450	547,321,148	564,542,092
Other	97,568,020	94,545,484	90,536,749
Total liabilities	<u>812,089,024</u>	<u>705,504,964</u>	<u>714,526,023</u>
NET POSITION			
Net investment in capital assets	301,792,748	271,755,951	242,182,374
Restricted	21,201,195	20,523,523	18,956,455
Unrestricted	21,103,894	3,354,249	9,871,917
Total net position	<u>344,097,837</u>	<u>295,633,723</u>	<u>271,010,746</u>
Total liabilities and net position	<u>\$ 1,156,186,861</u>	<u>\$ 1,001,138,687</u>	<u>\$ 985,536,769</u>

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
MANAGEMENT'S DISCUSSION AND ANALYSIS**

FINANCIAL ANALYSIS (CONTINUED)

2014 Compared to 2013

Assets - Current assets increased \$24.1 million (20.4%) over the prior year primarily due to increases totaling \$27.2 million in operating cash and equity in pooled investments, unbilled revenues, due from other governments and materials and supplies inventory. These increases were offset by a decrease of \$3.1 million in accounts receivable, net from the Combined Customer Service System.

Other assets increased \$52.2 million (46.9%) from 2013. This is mostly attributable to an increase in restricted cash and equity in pooled investments of \$51.6 million resulting from new debt issued in 2014 and spending on construction projects. Regulatory assets and other charges also increased \$1.9 million mainly due to capitalization of 2014 bond issue costs, Long Term Control Plan, and Rainwise program. The projects identified in the Long Term Control Plan will ultimately enhance the water quality of Ballard, North Union Bay, Interbay, Fremont/Wallingford, Duwamish, West Seattle, Montlake, Leschi, Union Bay, East Waterway, and Lake Union/Portage Bay. These increases were offset by a decrease of \$1.3 million in environmental costs and recoveries and external infrastructure costs.

Liabilities - Current liabilities increased \$4.2 million (6.6%) from 2013. This is mostly attributable to increases in due to other funds and revenue bonds due within one year, totaling \$6.0 million, offset by a decrease of \$1.8 million in accounts payable.

Other liabilities increased \$3.0 million (3.2%). This is due to increases totaling \$3.7 million in compensated absences payable, claims payable, environmental liabilities, vendor and other deposits payable, and unfunded other post employment benefits. These increases were offset by a decrease in loans of \$0.7 million.

Net Position - The largest portion of the Fund's net position (\$301.8 million or 87.7%) reflects the Fund's investment in capital assets such as land, buildings, and equipment, less 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 2014, net investment in capital assets increased \$30.0 million from 2013 due to an increase in capital assets placed in service, net of depreciation offset by the related debt.

The Fund's restricted net position (\$21.2 million or 6.2%) represent resources that are subject to restrictions on how they may be used. This portion of net position increased \$0.7 million from 2013. This change was primarily due to the increase in other charges.

**SEATTLE PUBLIC UTILITIES -
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MANAGEMENT'S DISCUSSION AND ANALYSIS**

FINANCIAL ANALYSIS (CONTINUED)

The remaining portion of the Fund's net position (\$21.1 million or 6.1%) represent resources that are unrestricted and may be used to meet the Fund's obligations to creditors. Unrestricted net position increased \$17.7 million from 2013 in part due to a lower percentage of capital projects funded with operating cash as compared to the prior year and increase in revenues.

2013 Compared to 2012

Assets - Current assets increased \$17.5 million (17.4%) over the prior year primarily due to increases totaling \$20.1 million in operating cash and equity in pooled investments, accounts receivable, net from the Combined Customer Service System, interest and dividends, unbilled revenues, due from other funds, and materials and supplies inventory. These increases were offset by a decrease of \$2.6 million in due from other governments.

Other assets decreased \$67.9 million (37.9%) from 2012. This is mostly attributable to a decrease in restricted cash and equity in pooled investments of \$52.6 million for use toward construction projects and reduction in environmental costs and recoveries of \$18.3 million due to expensing deferred costs related to cleanup of contamination along the Duwamish River. External infrastructure costs and regulatory assets also decreased by \$0.8 million due to amortization. Other charges increased \$3.8 million mainly due to the Long Term Control Plan and Meadowbrook pond sediments. The projects identified in the Long Term Control Plan will ultimately enhance the water quality of Ballard, North Union Bay, Interbay, Fremont/Wallingford, Duwamish, West Seattle, Montlake, Leschi, Union Bay, East Waterway, and Lake Union/Portage Bay.

Liabilities - Current liabilities increased \$4.2 million (7.1%) from 2012. This is mostly attributable to increases in accounts payable, due to other funds, due to other governments, revenue bonds due within one year, and credits and other.

Other liabilities increased \$4.0 million (4.4%). This is due to increases totaling \$5.4 million in environmental liabilities, loans, vendor and other deposits payable, and unfunded other post employment benefits. These increases were offset by a decrease in claims payable of \$1.4 million.

Net Position - The largest portion of the Fund's net position (\$271.8 million or 91.9%) reflects the Fund's investment in capital assets such as land, buildings, and equipment, less 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 2013, net investment in capital assets increased \$29.6 million from 2012 due to an increase in capital assets placed in service, net of depreciation offset by the related debt.

**SEATTLE PUBLIC UTILITIES -
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MANAGEMENT'S DISCUSSION AND ANALYSIS**

FINANCIAL ANALYSIS (CONTINUED)

The Fund's restricted net position (\$20.5 million or 6.9%) represent resources that are subject to restrictions on how they may be used. This portion of net position increased \$1.6 million from 2012. This change was primarily due to the increase in other charges.

The remaining portion of the Fund's net position (\$3.4 million or 1.1%) represent resources that are unrestricted and may be used to meet the Fund's obligations to creditors. Unrestricted net position decreased \$6.5 million from 2012 in part due to a higher percentage of capital projects funded with operating cash as compared to 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>2014</u>	<u>2013</u>	<u>2012</u>
Operating revenues	\$ 341,999,940	\$ 333,760,233	\$ 304,001,717
Operating expenses	<u>(284,220,570)</u>	<u>(275,112,916)</u>	<u>(258,684,757)</u>
Net operating income	57,779,370	58,647,317	45,316,960
Other income (expenses)	(15,118,084)	(16,401,438)	(15,751,552)
Fees, contributions, grants, special items and environmental remediation	<u>5,802,828</u>	<u>(17,622,902)</u>	<u>(28,813,646)</u>
Change in net position	<u>\$ 48,464,114</u>	<u>\$ 24,622,977</u>	<u>\$ 751,762</u>

2014 Compared to 2013

Current year operating revenues increased approximately \$8.2 million (2.5%) from 2013. This is primarily due to an \$8.7 million increase in drainage revenues resulting from an average increase in rates of 10.3%. Wastewater revenues, however, remained steady as the increase in wastewater rates mostly offset a decrease in wastewater volume. Other operating revenues decreased by \$0.5 million due to a decrease in engineering services.

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FINANCIAL ANALYSIS (CONTINUED)

Operating expenses increased \$9.1 million (3.3%) from 2013. Notable factors affecting this change include a decrease of \$2.2 million in allocated fringe and benefit costs offset by an increase of \$4.2 million in allocated general and administrative overhead costs. In addition, the cost of living adjustment caused labor costs to increase by \$2.5 million. City business and occupation taxes increased \$1.4 million as a result of overall increase in revenues. Wastewater treatment costs increased \$0.9 million due to an increase in King County's treatment rate by 5.6%. Depreciation and other amortization also increased \$0.9 million as a result of increase in depreciable assets. Additional increases to expenses include \$2.5 million in claims as actual payments incurred while risk financing liability remained steady, \$1.2 million in other operational expenses mainly impacted by an increase in drainage and wastewater conveyance expense, \$0.9 million in expensed projects primarily Thornton Confluence Improvement project, \$0.7 million in bad debt expense, \$0.4 million in compensated absences, and \$0.4 million for Consent Decree penalty. These expenses were offset by decrease in services for others of \$0.7 million.

Nonoperating revenues (expenses) decreased by \$1.3 million (7.8%) as compared to 2013. This is primarily due to an increase in investment and interest income, which is mostly due to the increase in the fair market value adjustment as value of the bond investments increase and investment of bond proceeds.

Capital contributions and grants increased \$4.2 million (64.2%) mainly due to increases of \$2.7 million in donated assets, \$1.1 million in capital grant revenue, and \$0.4 million in other contributions. The Fund had a decrease in environmental remediation expenses of \$19.2 million.

2013 Compared to 2012

Current year operating revenues increased approximately \$29.8 million (9.8%) from 2012. This is primarily due to a \$21.7 million increase in wastewater revenues resulting from an average increase in rates of 9.1%, offset by a decrease in consumption of 0.5%. Drainage revenues also increased \$8.8 million due to increase in rates while other operating revenues decreased by \$0.7 million due to decrease in engineering services.

Operating expenses increased \$16.4 million (6.4%) from 2012. This increase was mainly attributable to higher wastewater treatment cost of \$13.7 million due to an increase in King County's treatment rate by 10.2%. Another notable factor affecting the increase in operating expenses includes increases in city business and occupation and other taxes of \$3.6 million due to overall increase in revenues. Field operations increased \$7.6 million while utility systems management decreased \$6.8 million mainly due to the reorganization of work groups between the branches. Moreover, staff realignments from project delivery and customer services branches to the corporate asset management division in the general and administrative branch reduced costs by a net \$1.9 million.

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MANAGEMENT'S DISCUSSION AND ANALYSIS**

FINANCIAL ANALYSIS (CONTINUED)

Nonoperating revenues (expenses) increased by \$0.6 million as compared to 2012. Interest expense increased \$0.8 million, offset by \$1.6 million increase in premium amortization as a result of issuing a new 2012 bond. In addition, fair market value adjustment decreased by \$1.7 million as the value of bond investments decrease inversely while interest rates increase.

Capital contributions and grants decreased \$1.7 million mainly due to a decrease in grant billings of \$3.5 million as available grant funding diminished, offset by an increase of \$1.8 million in capital contributions. The Fund had a decrease in environmental remediation expenses of \$12.9 million.

CAPITAL ASSETS

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

SUMMARY OF CAPITAL ASSETS, NET OF ACCUMULATED DEPRECIATION

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Land and land rights	\$ 19,766,808	\$ 19,474,903	\$ 19,583,084
Buildings	6,979,156	7,181,503	7,436,540
Structures	122,355,093	117,454,430	117,155,245
Machinery and equipment	502,706,765	479,418,707	460,902,462
Computer systems	12,106,000	12,444,964	9,926,960
Construction in progress	178,365,927	128,551,817	83,224,105
Other property	<u>1,558,246</u>	<u>969,893</u>	<u>902,844</u>
Capital assets, net of accumulated depreciation	<u>\$ 843,837,995</u>	<u>\$ 765,496,217</u>	<u>\$ 699,131,240</u>

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

2014 Compared to 2013

The Fund's investment in capital assets, net of accumulated depreciation, for the year ended December 31, 2014 was \$843.8 million. This represented an increase of approximately \$78.3 million (10.2%) compared to 2013. Highlights of the Fund's major capital assets placed in service during 2014 included the following:

- \$8.3 million to replace sewer pipelines throughout several locations within the city.
- \$6.5 million to replace damaged culvert at 35th Avenue Northeast and restore floodplain area at the confluence of Thornton Creek.

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(An Enterprise Fund of the City of Seattle)
MANAGEMENT'S DISCUSSION AND ANALYSIS**

CAPITAL ASSETS (CONTINUED)

- \$3.6 million for construction of new pipeline in the 52nd Avenue South.
- \$2.9 million to relocate several hundred feet of the Thornton Creek and create a 1.5 acre vegetated Knickerbocker floodplain to increase storage capacity.
- \$2.7 million to divert a portion of the creek flow to create a natural creek mouth for Mapes Creek in Beer Sheva Park.
- \$2.5 million of drainage improvement at Portland Avenue South constructed in coordination with Duwamish Bike Trail project.
- \$2.2 million in emergency rehabilitation work on sewer mainlines.

Highlights of the Fund's major construction projects in progress at the end of 2014 include the following:

- \$58.0 million for construction of 2 million gallons of storage for the combined sewer system in the Windermere drainage basin.
- \$39.5 million for construction of two combined sewer overflow ("CSO") facilities in the South Genesee area.
- \$20.4 million for construction of combined sewer overflow storage facilities in Henderson North basins.
- \$5.7 million to construct new side sewers, collector sewers and connections as a result of Seawall Replacement project.
- \$5.3 million to build a pump station and a water quality facility near 7th and Riverside in South Park.
- \$4.6 million for improvements to the Delridge combined sewer overflow facilities.
- \$4.1 million to develop natural drainage system at Venema Creek.
- \$3.8 million to replace the customer service billing system.
- \$3.4 million for the bored tunnel portion of the Alaskan Way Viaduct and Seawall Replacement projects.
- \$2.7 million for construction of a CSO storage facility for the Ballard, Fremont, and Wallingford CSO Basins.
- \$2.4 million for implementation of the Ballard Natural Drainage System.

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CAPITAL ASSETS (CONTINUED)

2013 Compared to 2012

The Fund's investment in capital assets, net of accumulated depreciation, for the year ended December 31, 2013 was \$765.5 million. This represented an increase of approximately \$66.4 million (9.5%) compared to 2012. Highlights of the Fund's major capital assets placed in service during 2013 included the following:

- \$8.3 million for construction of stormwater detention pond to reduce flooding near North 107th Street and Midvale.
- \$6.9 million for construction of swales in the Cascade Neighborhood to improve runoff from Capitol Hill.
- \$5.6 million for the relocation and replacement of wastewater and drainage infrastructure as part of the SDOT Mercer East Transportation Improvements Project.
- \$5.0 million to replace sewer pipelines throughout several locations within the city.
- \$3.2 million to upgrade the Maximo system.
- \$1.6 million in emergency rehabilitation work on sewer mainlines.
- \$1.1 million for the completion of the Madison Valley stormwater flood control facilities.
- \$1.0 million for SCADA installations at various wastewater infrastructure monitoring sites.

Highlights of the Fund's major construction projects in progress at the end of 2013 include the following:

- \$45.3 million for construction of 2 million gallons of storage for the combined sewer system in the Windermere drainage basin.
- \$24.9 million for construction of two combined sewer overflow facilities in the South Genesee area.
- \$16.3 million for construction of combined sewer overflow storage facilities in Henderson North basins.
- \$4.3 million to build a pump station and a water quality facility near 7th and Riverside in South Park.
- \$3.7 million for improvements to the Delridge combined sewer overflow facilities.
- \$2.7 million to develop natural drainage system at Venema Creek.
- \$2.5 million for bored tunnel portion of the Alaskan Way Viaduct and Seawall Replacement projects.

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CAPITAL ASSETS (CONTINUED)

- \$2.0 million to replace damaged culvert at 35th Avenue Northeast and restore floodplain area at the confluence of Thornton Creek.
- \$1.9 million for major enhancements to the I-SCADA data management program and IMS web site portal application.
- \$1.6 million for construction of new pipeline in the 52nd Ave South.
- \$1.4 million for implementation of the Ballard Natural Drainage System.
- \$1.1 million to construct sewer and stormwater improvements in Broadview's 12th Ave NW basin.
- \$1.1 million to divert a portion of the creek flow to create a natural creek mouth of Mapes Creek in Beer Sheva Park.
- \$1.1 million to construct new side sewers, collector sewers and connections as a result of Seawall Replacement project.
- \$1.0 million to construct new stormwater drainage system in a small area of South Park.

DEBT ADMINISTRATION

The Fund's debt primarily consists of bonded debt and loans. Bonded debt is secured solely by drainage and wastewater system 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 AA+ by Standard and Poor's Rating Service and Aa1 by Moody's Investor Service.

2014 Compared to 2013

At the end of 2014, the Fund had \$618.9 million in bonded debt, as compared to \$525.3 million in 2013, all of which was secured solely by drainage and wastewater system revenues. The key factor in this increase of \$93.6 million was the issuance of \$133.2 million new debt, offset by refunding \$23.8 million of 2004 bonds, and partially refunding the 2006 bonds and payments of \$15.8 million of debt principal.

At the end of 2014, the Fund had an outstanding loan balance of \$17.8 million compared to \$18.4 million in 2013. During 2014, the Fund borrowed an additional \$0.5 million from the Washington State Department of Ecology for the Capitol Hill Water Quality project.

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MANAGEMENT'S DISCUSSION AND ANALYSIS**

DEBT ADMINISTRATION (CONTINUED)

2013 Compared to 2012

At the end of 2013, the Fund had \$525.3 million in bonded debt, as compared to \$540.5 million in 2012, all of which was secured solely by drainage and wastewater system revenues. There were no new bonds issued in 2013.

At the end of 2013, the Fund had an outstanding loan balance of \$18.4 million compared to \$17.7 million in 2012. During 2013, the Fund borrowed an additional \$0.4 million from the Washington State Department of Commerce for the Midvale project and \$1.3 million from the Washington State Department of Ecology for the Capitol Hill Water Quality project.

Additional information about the Fund's long-term debt can be found in Notes 4 and 10.

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, Finance 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,	
	2014	2013
ASSETS		
CURRENT ASSETS		
Operating cash and equity in pooled investments	\$ 101,300,976	\$ 74,502,511
Receivables		
Accounts, net of allowance	18,042,262	21,171,279
Interest and dividends	460,223	447,978
Unbilled revenues	18,272,010	18,043,479
Notes, and other contracts	76,378	49,042
Due from other funds	983,559	1,015,322
Due from other governments	2,373,576	2,266,634
Materials and supplies inventory	1,042,594	938,554
Prepayments and other current assets	34,515	34,515
Total current assets	<u>142,586,093</u>	<u>118,469,314</u>
NONCURRENT ASSETS		
Restricted cash and equity in pooled investments	99,431,825	47,873,429
Prepayments long-term	691,106	725,621
Notes and contracts receivable	1,159,089	1,210,467
Environmental costs and recoveries	3,969,706	4,849,507
External infrastructure costs	19,328,054	19,616,799
Regulatory assets - bond issue costs	4,236,099	3,542,883
Other charges	34,467,999	33,300,096
Capital assets		
Land and land rights	19,766,808	19,474,903
Plant in service, excluding land	941,062,422	902,671,203
Less accumulated depreciation	(296,915,408)	(286,171,599)
Construction in progress	178,365,927	128,551,817
Other property, net	1,558,246	969,893
Total noncurrent assets	<u>1,007,121,873</u>	<u>876,615,019</u>
Total assets	1,149,707,966	995,084,333
DEFERRED OUTFLOWS OF RESOURCES		
Unamortized loss on refunded debt	6,478,895	6,054,354
Total assets and deferred outflows of resources	<u>\$ 1,156,186,861</u>	<u>\$ 1,001,138,687</u>

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
STATEMENTS OF NET POSITION (CONTINUED)**

	December 31,	
	2014	2013
LIABILITIES		
CURRENT LIABILITIES		
Accounts payable	\$ 10,178,298	\$ 11,944,809
Salaries, benefits, and payroll taxes payable	2,417,105	2,187,966
Compensated absences payable	446,114	397,926
Due to other funds	9,220,920	5,536,439
Due to other governments	11,588,823	11,624,345
Interest payable	7,226,127	6,934,251
Taxes payable	298,726	334,038
Revenue bonds due within one year	18,215,000	15,825,000
Claims payable	1,928,051	1,922,207
Environmental liabilities	1,637,670	1,805,212
Loans payable, due within one year	1,201,646	1,116,399
Other	3,469,074	4,009,740
Total current liabilities	<u>67,827,554</u>	<u>63,638,332</u>
NONCURRENT LIABILITIES		
Compensated absences payable	4,625,243	4,125,640
Claims payable	6,752,164	6,502,498
Environmental liabilities	66,042,731	63,655,889
Loans	16,565,787	17,242,849
Vendor and other deposits payable	1,017,751	536,488
Unfunded other post employment benefits	2,505,202	2,378,401
Other noncurrent liabilities	59,142	103,719
Revenue bonds	618,895,000	525,280,000
Less bonds due within one year	(18,215,000)	(15,825,000)
Bond discount and premium, net	46,013,450	37,866,148
Total noncurrent liabilities	<u>744,261,470</u>	<u>641,866,632</u>
Total liabilities	<u>812,089,024</u>	<u>705,504,964</u>
NET POSITION		
Net investment in capital assets	301,792,748	271,755,951
Restricted for		
External infrastructure costs	7,061,221	7,130,843
Other charges	14,139,974	13,392,680
Unrestricted	21,103,894	3,354,249
Total net position	<u>344,097,837</u>	<u>295,633,723</u>
Total liabilities and net position	<u>\$ 1,156,186,861</u>	<u>\$ 1,001,138,687</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,	
	2014	2013
OPERATING REVENUES		
Charges for services and other revenues	\$ 341,999,940	\$ 333,760,233
OPERATING EXPENSES		
Planning and development	1,786,810	2,334,654
Utility systems management	11,373,723	10,545,768
Field operations	26,430,927	27,176,807
Project delivery	8,099,883	10,020,333
Customer services	4,402,663	4,108,949
Wastewater treatment	140,307,103	139,433,612
General and administrative	25,034,314	17,046,124
City business and occupation taxes	40,265,835	38,852,253
Other taxes	4,329,268	4,339,943
Depreciation and other amortization	22,190,044	21,254,473
Total operating expenses	<u>284,220,570</u>	<u>275,112,916</u>
OPERATING INCOME	<u>57,779,370</u>	<u>58,647,317</u>
NONOPERATING REVENUES (EXPENSES)		
Investment and interest income	4,008,812	2,009,540
Interest expense	(20,616,518)	(21,361,044)
Amortization of bonds premiums and discounts, net	1,542,213	1,395,944
Amortization of refunding loss	(383,813)	(373,988)
Loss on sale of capital assets	(817,345)	(167,451)
Contributions and grants	978,178	1,974,585
Other, net	170,389	120,976
Total nonoperating revenues (expenses)	<u>(15,118,084)</u>	<u>(16,401,438)</u>
INCOME BEFORE CAPITAL CONTRIBUTIONS AND GRANTS, AND SPECIAL ITEMS	42,661,286	42,245,879
CAPITAL CONTRIBUTIONS AND GRANTS	10,751,537	6,546,159
ENVIRONMENTAL REMEDIATION	<u>(4,948,709)</u>	<u>(24,169,061)</u>
CHANGE IN NET POSITION	48,464,114	24,622,977
NET POSITION		
Beginning of year	<u>295,633,723</u>	<u>271,010,746</u>
End of year	<u>\$ 344,097,837</u>	<u>\$ 295,633,723</u>

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
STATEMENTS OF CASH FLOWS**

	Years Ended December 31,	
	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from customers	\$ 346,022,044	\$ 329,789,633
Cash paid to suppliers	(155,800,652)	(156,949,272)
Cash paid to employees	(57,034,170)	(50,923,303)
Cash paid for taxes	(44,634,545)	(42,716,088)
Net cash provided by operating activities	<u>88,552,677</u>	<u>79,200,970</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Noncapital grants received	1,028,715	1,946,381
Payments for environmental liabilities	(1,849,607)	(1,903,351)
Net cash provided by (used in) noncapital financing activities	<u>(820,892)</u>	<u>43,030</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from sale of bonds and other long-term debt	144,425,158	1,739,977
Principal payments on long-term debt and refunding	(42,524,376)	(16,309,601)
Capital expenditures and other charges paid	(89,352,766)	(83,635,360)
Interest paid on long-term debt	(27,163,850)	(26,021,620)
Build America Bonds federal interest subsidy	1,734,794	1,817,762
Capital fees and grants received	1,887,187	4,381,277
Debt issuance costs	(865,214)	-
Proceeds from sale of capital assets	222,371	643,776
Net cash used in capital and related financing activities	<u>(11,636,696)</u>	<u>(117,383,789)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
(Loss) gain on investments	2,261,772	(134,591)
NET INCREASE (DECREASE) IN CASH AND EQUITY IN POOLED INVESTMENTS		
	78,356,861	(38,274,380)
CASH AND EQUITY IN POOLED INVESTMENTS		
Beginning of year	<u>122,375,940</u>	<u>160,650,320</u>
End of year	<u>\$ 200,732,801</u>	<u>\$ 122,375,940</u>
CASH AT THE END OF THE YEAR CONSISTS OF		
Operating cash and equity in pooled investments	\$ 101,300,976	\$ 74,502,511
Noncurrent restricted cash and equity in pooled investments	<u>99,431,825</u>	<u>47,873,429</u>
Total cash at the end of the year	<u>\$ 200,732,801</u>	<u>\$ 122,375,940</u>

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
STATEMENTS OF CASH FLOWS (CONTINUED)**

	Years Ended December 31,	
	2014	2013
RECONCILIATION OF NET OPERATING INCOME TO NET CASH FROM OPERATING ACTIVITIES		
Operating income	\$ 57,779,370	\$ 58,647,317
Adjustments to reconcile net operating income to net cash from operating activities		
Depreciation and amortization	22,190,044	21,254,473
Other receipts and payments	1,384,355	1,268,530
Changes in operating assets and liabilities		
Accounts receivable	3,129,017	(3,736,641)
Unbilled revenues	(228,531)	(1,315,004)
Due from other funds	31,763	(334,947)
Due from other governments	268,250	1,079,987
Materials and supplies inventory	(104,040)	(110,580)
Other assets	24,042	91,807
Accounts payable	(1,766,511)	819,919
Salaries, benefits, and payroll taxes payable	229,139	484,941
Compensated absences payable	547,791	123,478
Due to other funds	3,684,481	678,277
Due to other governments	(35,523)	1,181,046
Claims payable	255,510	(1,897,343)
Taxes payable	(35,312)	45,107
Other liabilities	1,198,832	920,603
Total adjustments	<u>30,773,307</u>	<u>20,553,653</u>
Net cash from operating activities	<u>\$ 88,552,677</u>	<u>\$ 79,200,970</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 some that are normally considered to be general and administrative. The Fund is charged a share of these costs and additionally pays a business and occupation tax to the City's General Fund. During 2014 and 2013, the Fund paid \$10,428,019 and \$10,325,448, respectively, to the City for its share of general and administrative services. Additionally, the Fund paid \$40,265,835 and \$38,852,253 to the City for business and occupation utility taxes in 2014 and 2013, respectively.

Wastewater disposal and drainage services provided to other City departments and agencies are billed at rates prescribed by City ordinances. The Fund collected \$3,153,242 in 2014 and \$2,062,980 in 2013 from the City for wastewater services provided. The Fund also collected \$5,662,105 in 2014 and \$5,150,236 in 2013 from the City for drainage services.

The utility billing function is co-managed by both 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, Combined Customer Services System ("CCSS"). SPU and SCL bills and reimburses each other for these services. 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 \$1,742,130 and \$1,604,865 in 2014 and 2013, respectively. The Fund paid \$158,550 and \$220,537 for CCSS services in 2014 and 2013, respectively, which does not include reimbursements to SCL for the Fund's share of capital costs to upgrade the CCSS system.

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, and liabilities 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 to form a pool of cash that is managed by the City's Finance and Administration Services Department. Under the City's investment policy, the Finance and Administration Services Department invests all temporary cash surpluses either directly or through a "sweep account." 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. The Fund's share of the pool is included in the accompanying Statements of Net Position under the caption "cash and equity in pooled investments." The pool operates like a demand deposit account in that all City departments may deposit cash at any time and can also withdraw cash out of the pool without prior notice or penalty. Accordingly, the Statements of Cash Flows reconcile to cash and equity in pooled investments. Cash and equity in pooled investments are reported at fair value. The restricted cash and equity in pooled investments are comprised of unexpended bond proceeds, a portion of which is scheduled to be spent in 2014, 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, 2014 and 2013, the Fund's allowance for doubtful accounts was \$393,166 and \$315,093, 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 (see Note 9). 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 include costs related to leasehold improvements and plans, such as the Combined Sewer Overflow Update plan and the Comprehensive Ditch and Culvert plan. 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 treated as a special item 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 - 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

Composite rates based on year of addition are used for depreciating the laterals, mains, and outfalls asset group. For most assets, it is SPU's policy to begin depreciation in the year following acquisition and to record a full year's depreciation in the year of disposition. This does not apply to heavy equipment, for which depreciation begins in the month following the equipment's in-service date to more accurately allocate equipment costs to various activities.

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 bonds 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.

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 does not have any deferred inflows of resources as of December 31, 2014 and 2013.

Environmental Liabilities - The Fund has accrued a liability for pollution remediation activities in accordance with GASB Statement No. 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.

**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)

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 9 for site descriptions.

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 to be 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.

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.

**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)

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 - Certain expenses of the Fund are reported on the Statement of Revenue, Expenses and Change in Net Position by functional category. The types of work performed within each category are as follows:

- **Planning and development** - Provides planning services and other related costs prior to the start of capital projects.
- **Utility systems management** - Accounts for the overall management of the Fund's infrastructure assets, assuring they are properly designed, constructed, operated, and protected.
- **Field operations** - Operates and maintains the Fund's drainage and wastewater systems.
- **Project delivery** - Provides project management and engineering services to the Fund and executes the Fund's capital projects from start to completion.
- **Customer services** - Invoices the Fund's customers for services provided and is the primary point of contact for customers.

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, amortization of debt expenses, and sale of 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.

**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)

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, 2014 and 2013 are related to external infrastructure costs and certain other charges.

Unrestricted net position is the portion that is not "net investment in capital assets" or "restricted."

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, 2014 and 2013.

Accounting Changes - GASB has issued Statement No. 68, *Accounting and Financial Reporting for Pensions*. The primary objective of this statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This statement is effective for periods beginning after June 15, 2014. The Fund is evaluating the impact of this standard on the financial statements, but anticipates recording amounts for the unfunded portion of the pension plan. At this time, those amounts are not yet known.

GASB has issued Statement No. 72, *Fair Value Measurement and Application*, to provide guidance for determining a fair value measurement for financial reporting purposes. This statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. The statement is effective for periods beginning after June 15, 2015. The Fund is evaluating the impact of this standard on the financial statement.

Use of Estimates - The preparation of the financial statements in conformity 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, accrued sick leave, capitalized interest, depreciation, environmental liabilities, risk liabilities, and other contingencies. Changes in these estimates and assumptions may have a material impact on the financial statements.

**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)

Significant Risks and Uncertainties - 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.

Note 2 - Cash and Investments

Custodial Credit Risk - Deposits - As of December 31, 2014 and 2013, the City's pool contained cash on deposit with the City's custodial banks in the amounts of \$18,026,085 and \$12,431,810, respectively. The deposits in excess of \$250,000 in 2014 and 2013 were uninsured and uncollateralized. As such, these deposits were exposed to custodial credit risk, which is the risk that the deposits may not be returned to the City in the event of a bank failure. The City attempts to minimize exposure to custodial credit risk for deposits by requiring the depository bank to have sufficient capital to support the activity of the City. In addition, banks having a deposit relationship with the City are required to provide financial statements for the City's use in reviewing the bank's financial condition.

All deposits not covered by FDIC insurance are under the regulation of the Washington State Public Deposit Protection Commission (the "Commission") established in RCW 39.58 for public depository financial institutions. The Commission requires a pledge agreement and a trustee for each public depository financial institution. The trustee ensures eligible collateral defined as securities and designated for the benefit of public depositors, as described in RCW 39.58.050 (5) and (6), are segregated from all other assets. Eligible collateral is utilized by the trustee when the Commission has determined a loss, net of deposit insurance, has been incurred by a public depository financial institution.

Investments - As of December 31, the City's pooled investments were as follows:

	<u>2014</u>		<u>2013</u>	
	<u>City Pool</u>	<u>Weighted Average Maturity (Days)</u>	<u>City Pool</u>	<u>Weighted Average Maturity (Days)</u>
U.S. Government Agencies	\$ 721,680,286	1408	\$ 853,631,386	1141
Commercial Paper	349,418,008	43	154,962,668	47
U.S. Government Obligations	252,188,265	800	227,659,850	902
State and Local Governments	227,247,608	976	156,812,737	818
Repurchase Agreements	73,811,651	2	44,756,478	2
Total	<u>\$ 1,624,345,818</u>		<u>\$ 1,437,823,119</u>	
Portfolio Weighted Average Maturity		896		914

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 2 - Cash and Investments (Continued)

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

	2014	2013
Operating cash and equity in pooled investments	\$ 101,300,976	\$ 74,502,511
Restricted cash and equity in pooled investments	99,431,825	47,873,429
Total	\$ 200,732,801	\$ 122,375,940
Balance as a percentage of City pool cash and investments	12.4%	8.5%

Interest Rate Risk - Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. In general, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The City manages this risk by limiting the average maturity of investments to five years. However, the Fund's investments are selected for greater liquidity in order to support the Fund's cash flow needs and therefore typically have much shorter average maturities.

Credit Risk - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In accordance with the City's investment policy, investments in commercial paper purchased on the secondary market are limited to those with maturities not longer than 180 days from purchase and with the highest rating by at least two nationally recognized statistical rating organizations ("NRSROs"). As of December 31, 2014 and 2013, the City's investments in commercial paper were rated P-1 or Aaa by Moody's Investors Service and AA+, A-1 or A-1+ by Standard & Poor's Rating Service.

The City also purchases obligations of government-sponsored enterprises which are eligible as collateral for advances to member banks as determined by the Board of Governors of the Federal Reserve System. These include, but are not limited to, debt securities of Federal Home Loan Bank, Federal National Mortgage Association, Wells Fargo, and Federal Home Loan Mortgage Corporation. As of December 31, 2014, these investments were rated Aaa by Moody's Investors Service and AAA or AA+ by Standard & Poor's Rating Service. As of December 31, 2013, these investments were rated Aaa by Moody's Investors Service and AA+ by Standard & Poor's Rating Service.

Concentration of Credit Risk - The City's investment policy limits concentration of credit risk for the City's investments as a whole, inclusive of the Fund's investments. These policy limits vary for each investment category.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 2 - Cash and Investments (Continued)

The City's investments in which five percent or more is invested in any single issuer, as of December 31, are as follows:

Issuer	2014		2013	
	Fair Value	Percent of Total Investments	Fair Value	Percent of Total Investments
United States Government	\$ 252,188,265	16%	\$ 227,659,850	16%
Federal National Mortgage Association	\$ 249,771,922	15%	\$ 329,389,682	23%
Federal Home Loan Mortgage Corp	\$ 160,445,200	10%	\$ 285,535,430	20%
Federal Farm Credit Bank	\$ 121,677,087	7%	**	**
Freddie Mac Multifamily Securities	\$ 108,129,281	7%	\$ 107,594,143	7%
Federal Home Loan Bank	\$ 81,656,795	5%	\$ 86,497,845	6%
Wells Fargo	\$ 73,811,651	5%	**	**

** Investment did not represent 5% or more of investments as of December 31, 2013.

Note 3 - Capital Assets

Capital asset activity consisted of the following for the year ended December 31, 2014:

	Beginning Balance	Additions and Transfers In	Retirements and Transfers Out	Ending Balance
Buildings	\$ 14,139,381	\$ 103,269	\$ -	\$ 14,242,650
Structures	161,246,619	9,310,558	(122,560)	170,434,617
Machinery and equipment	671,159,243	37,149,911	(5,713,391)	702,595,763
Computer systems	56,125,960	3,336,000	(5,672,568)	53,789,392
Total capital assets, excluding land	902,671,203	49,899,738	(11,508,519)	941,062,422
Less accumulated depreciation	(286,171,599)	(21,193,248)	10,449,439	(296,915,408)
	616,499,604	28,706,490	(1,059,080)	644,147,014
Construction in progress	128,551,817	95,329,506	(45,515,396)	178,365,927
Land and land rights	19,474,903	291,905	-	19,766,808
Other property	969,893	588,353	-	1,558,246
Capital assets, net	\$ 765,496,217	\$ 124,916,254	\$ (46,574,476)	\$ 843,837,995

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 3 - Capital Assets (Continued)

Capital asset activity consisted of the following for the year ended December 31, 2013:

	Beginning Balance	Additions and Transfers In	Retirements and Transfers Out	Ending Balance
Buildings	\$ 14,092,883	\$ 46,498	\$ -	\$ 14,139,381
Structures	156,718,161	4,528,458	-	161,246,619
Machinery and equipment	640,463,045	30,922,811	(226,613)	671,159,243
Computer systems	49,954,131	6,395,330	(223,501)	56,125,960
Total capital assets, excluding land	861,228,220	41,893,097	(450,114)	902,671,203
Less accumulated depreciation	(265,807,013)	(20,657,041)	292,455	(286,171,599)
	595,421,207	21,236,056	(157,659)	616,499,604
Construction in progress	83,224,105	87,254,552	(41,926,840)	128,551,817
Land and land rights	19,583,084	545,387	(653,568)	19,474,903
Other property	902,844	67,049	-	969,893
Capital assets, net	<u>\$ 699,131,240</u>	<u>\$ 109,103,044</u>	<u>\$ (42,738,067)</u>	<u>\$ 765,496,217</u>

During 2014 and 2013, the Fund capitalized interest costs relating to construction of \$6,842,037 and \$4,501,589, respectively.

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 \$18,642,989 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, 2014 and 2013 were \$618,895,000 and \$525,280,000, respectively. Revenue bonds outstanding as of December 31, 2014 and 2013 consisted of the following Municipal Drainage and Wastewater bonds:

Name of Issue	Issuance Date	Maturity Years	Interest Rates	Original Issue Amount	Bonds Outstanding, 2014	Bonds Outstanding, 2013
2004 parity bonds	10/28/04	2005-2034	2.25-5.125%	\$ 62,010,000	\$ -	\$ 8,870,000
2006 parity refunding bonds	11/1/06	2007-2037	4.0-5.0%	121,765,000	79,485,000	100,115,000
2008 parity bonds	4/16/08	2009-2038	4.0-5.0%	84,645,000	75,720,000	77,360,000
2009A parity bonds	12/17/09	2017-2039	4.2-5.5%	102,535,000	102,535,000	102,535,000
2009B parity refunding bonds	12/17/09	2010-2027	2.0-4.0%	36,680,000	19,745,000	23,225,000
2012 parity refunding bonds	6/27/12	2012-2042	2.0-5.0%	222,090,000	208,230,000	213,175,000
2014 parity refunding bonds	7/10/14	2015-2044	3.0-5.0%	133,180,000	133,180,000	-
				<u>\$ 762,905,000</u>	<u>\$ 618,895,000</u>	<u>\$ 525,280,000</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)

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

<u>Years Ending December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 18,215,000	\$ 29,156,128	\$ 47,371,128
2016	19,080,000	28,370,953	47,450,953
2017	20,000,000	27,529,553	47,529,553
2018	20,910,000	26,578,765	47,488,765
2019	21,905,000	25,550,146	47,455,146
2020 - 2024	116,050,000	111,342,148	227,392,148
2025 - 2029	132,560,000	81,114,360	213,674,360
2030 - 2034	124,065,000	48,640,951	172,705,951
2035 - 2039	102,350,000	21,463,706	123,813,706
2040 - 2044	43,760,000	4,192,100	47,952,100
	<u>\$ 618,895,000</u>	<u>\$ 403,938,810</u>	<u>\$ 1,022,833,810</u>

The following table shows the revenue bond activity during the year ended December 31, 2014:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds payable					
Revenue bonds	\$ 525,280,000	\$ 133,180,000	\$ (39,565,000)	\$ 618,895,000	\$ 18,215,000
Add (deduct) deferred amounts:					
Issuance premiums	38,460,159	10,702,403	(2,578,861)	46,583,701	-
Issuance discounts	(594,011)	-	23,760	(570,251)	-
Total bonds payable	<u>\$ 563,146,148</u>	<u>\$ 143,882,403</u>	<u>\$ (42,120,101)</u>	<u>\$ 664,908,450</u>	<u>\$ 18,215,000</u>

The following table shows the revenue bond activity during the year ended December 31, 2013:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds payable					
Revenue bonds	\$ 540,495,000	\$ -	\$ (15,215,000)	\$ 525,280,000	\$ 15,825,000
Add (deduct) deferred amounts:					
Issuance premiums	39,879,863	-	(1,419,704)	38,460,159	-
Issuance discounts	(617,771)	-	23,760	(594,011)	-
Total bonds payable	<u>\$ 579,757,092</u>	<u>\$ -</u>	<u>\$ (16,610,944)</u>	<u>\$ 563,146,148</u>	<u>\$ 15,825,000</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)

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. In 2014, \$23,740,000 bonds were defeased and \$49,950,000 were redeemed as shown below:

<u>Name of Issue</u>	<u>Amount Outstanding at December 31, 2013</u>	<u>Additions</u>	<u>Redemptions</u>	<u>Amount Outstanding at December 31, 2014</u>
2004 Parity	\$ 42,540,000	\$ 7,410,000	\$ (49,950,000)	\$ -
2006 Parity	-	16,330,000	-	16,330,000
	<u>\$ 42,540,000</u>	<u>\$ 23,740,000</u>	<u>\$ (49,950,000)</u>	<u>\$ 16,330,000</u>

As of December 31, 2013, \$42,540,000 of defeased bonds were not redeemed yet, as shown below:

<u>Name of Issue</u>	<u>Amount Outstanding at December 31, 2012</u>	<u>Additions</u>	<u>Redemptions</u>	<u>Amount Outstanding at December 31, 2013</u>
2004 Parity	<u>\$ 42,540,000</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 42,540,000</u>

In July 2014, the Fund issued \$133,180,000 of Drainage and Wastewater Improvement and Refunding Revenue Bonds with varying annual principal payments due beginning 2015 and ending in 2044, at interest rates ranging from 3.0 percent and 5.0 percent. A portion of the proceeds were used to fully refund 2004 bond and partially refund 2006 bonds. As a result of the refunding, the Fund reduced total debt service requirements by \$2.7 million resulting in an economic gain (difference between the present value of the debt service payments on the old and new debts) of \$2.2 million.

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 2014, net revenue available for debt service, as defined by the bond covenants, was 298% of annual debt service. The Fund was in compliance with all debt covenants as of December 31, 2014.

**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 non-cancelable operating lease commitments for real and personal property, with payments of \$100,237 and \$100,325 in 2014 and 2013, respectively. Rents are paid as they become due and payable.

Minimum lease payments under the leases for the years ended December 31, are as follows:

2015	\$	97,489
2016		83,755
2017		30,994
2018		30,994
2019		30,994
2020		5,166
		<hr/>
	\$	279,392
		<hr/> <hr/>

Note 6 - Retirement and Other Postemployment Benefit Plans

Pension Costs - All permanent Fund employees are eligible to participate in the Seattle City Employees' Retirement System (the "System"), a cost-sharing public employee retirement system operated by the City. The System is a single-employer defined benefit plan in which benefits vest after five years of covered service. City employees may retire after 30 years of service regardless of age; after age 52, with 20 or more years of service; after age 57, with 10 or more years of service, and after age 62, with five or more years of service. The System also provides death and disability benefits. These benefit provisions and all other requirements are established by City ordinances.

City employees are required to contribute 10.03% of their annual base salaries to the System. The City's contribution rate increased to 14.31% for 2014 from 12.89% for 2013. 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, 2014, 2013 and 2012, were \$6,210,209, \$5,401,854, and \$4,323,607, 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, telephone: (206) 386-1293, or www.seattle.gov/retirement/annual_report.htm.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 6 - Retirement and Other Postemployment Benefit Plans (Continued)

Employer contributions for the City are as follows (dollars in millions):

Year Ended December 31,	City Required Contribution	City Actual Contribution	Percentage Contributed
2012	\$ 62.4	\$ 62.4	100%
2013	\$ 76.9	\$ 76.9	100%
2014	\$ 89.8	\$ 89.8	100%

Actuarial data and assumptions

Valuation date	January 1, 2014
Actuarial cost method	Entry age
Amortization method	Level percent
Remaining amortization period	30 years, open
Asset valuation method	5-Year Smoothing Method
Investment rate of return	7.5%
Projected general wage inflation	4.0%
Postretirement benefit increases	1.5%

Schedules of funding progress are as follows (dollars in millions):

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Liabilities (AAL) Entry Age ¹ (b)	Unfunded AAL (UAAL) ² (b-a)	Funded Ratio (a/b)	Covered Payroll ³ (c)	UAAL as a % of Covered Payroll ((b-a)/c)
January 1, 2012	\$ 1,954.3	\$ 2,859.3	\$ 905.0	68.3%	\$ 557.0	162.5%
January 1, 2013	\$ 1,920.1	\$ 3,025.3	\$ 1,105.2	63.5%	\$ 567.8	194.6%
January 1, 2014	\$ 2,094.3	\$ 3,260.1	\$ 1,165.8	64.2%	\$ 597.9	195.0%

¹ Actuarial present value of benefits less actuarial present value of future normal costs based on entry age actuarial cost method.

² Actuarial accrued liabilities less actuarial value of assets.

³ Covered payroll includes compensation paid to all active employees on which contributions are calculated.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 6 - Retirement and Other Postemployment Benefit Plans (Continued)

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

Eligible retirees (younger than age 65) may contribute to the medical plan and any additional health care programs contemplated or amended by ordinance of the Seattle City Council and as provided in Seattle Municipal Code 4.50.020.

The Seattle City Council authorizes the obligations of the plan members and the City as employer by passing ordinances and amendments regarding contributions to the plans. Eligible retirees self-pay 100% of the premiums based on blended rates which were established by including the experience of retirees with the experience of active employees for underwriting purposes. The plan is financed on a pay-as-you-go basis, and the City was required to contribute \$1.0 million in 2014 and \$3.0 million in 2013.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 6 - Retirement and Other Postemployment Benefit Plans (Continued)

The table below summarizes the City's annual cost, expected contributions to the plan, and changes in the net other post employment benefit obligation ("OPEB") for fiscal years ended December 31, 2014 and 2013. These calculations are based on the most recent actuarial valuation data available, dated January 1, 2014. The Fund has accrued \$2,505,202 to the plan as of December 31, 2014, as a reasonable estimate of expected contributions.

	<u>2014</u>	<u>2013</u>
Annual required contribution	\$ 4,392,000	\$ 8,452,000
Interest on net OPEB obligation	1,542,000	1,534,000
Adjustment to annual required contribution	<u>(2,403,000)</u>	<u>(2,253,000)</u>
Annual OPEB cost (expense)	3,531,000	7,733,000
Contribution (employer-paid benefits)	<u>(1,006,000)</u>	<u>(2,972,000)</u>
Increase in net OPEB obligation	2,525,000	4,761,000
Net OPEB obligation, beginning of year	<u>44,303,000</u>	<u>39,542,000</u>
Net OPEB obligation, end of year	<u>\$ 46,828,000</u>	<u>\$ 44,303,000</u>
Fund's allocated share of city liability	<u>\$ 2,505,202</u>	<u>\$ 2,378,401</u>

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. Actuarial calculations are based on the types of benefits provided under the terms of the plan and on the pattern of shared costs between the employer and plan members, at the time of each valuation. 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.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 6 - Retirement and Other Postemployment Benefit Plans (Continued)

Significant methods and assumptions are as follows:

Actuarial data and assumptions

Valuation date	January 1, 2014
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	30 years, open
Discount rate	3.48%
Health care cost trend rates - medical	Traditional and Preventive Plans: 8%, decreasing by 0.5% for each year for two years; 16% in year 2017 and decreasing to 7.2% in 2018 Group Health Standard and Deductible Plans: 7.5%, decreasing by 0.5% for the next three years
Participation	40% of Active Employees who retire participate.
Mortality	General Service Actives based on the RP-2000 Employees Tables for Males and Females, with ages set back six years and General Service Retirees based on the RP-2000 Combined Healthy Males with ages set back two years and Females, with ages set back one year.
Marital status	45% of members electing coverage are assumed to be married or to have a registered domestic partner. Male spouses are assumed to be two years older than their female spouses.
Other considerations	Active employees with current spousal and/or dependent coverage and are under Group Health Standard or Group Health Deductible are assumed to elect same plan and coverage after retirement. Of those under City of Seattle Traditional or City of Seattle Preventative, 50% are assumed to switch to the Group Health Standard Plan, while the other 50% will continue coverage under the same plan.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 6 - Retirement and Other Postemployment Benefit Plans (Continued)

Schedules of funding progress are as follows (dollars in millions):

Actuarial Valuation Date	Actuarial Value of Assets (a)	AAL Entry Age (b)	UAAL (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percent of Covered Payroll ((b-a)/c)
January 1, 2012	\$ -	\$ 74.7	\$ 74.7	0.0%	\$ 891.6	8.4%
January 1, 2013	\$ -	\$ 78.9	\$ 78.9	0.0%	\$ 942.0	8.4%
January 1, 2014	\$ -	\$ 41.8	\$ 41.8	0.0%	\$ 1,003.5	4.2%

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.

For 2014 and 2013, 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, 0.931% and 0.675%, respectively. Claims expected to be paid within one year are \$1,928,051 and \$1,922,207 as of December 31, 2014 and 2013, respectively. The schedules below present the changes in the liability for workers' compensation claims and other claims (risk financing liabilities) as of December 31:

	2014	2013
Beginning liability, undiscounted	\$ 8,650,953	\$ 10,634,695
Payments	(1,085,110)	(975,738)
Incurred claims and change in estimate	1,414,866	(1,008,004)
Ending liability, undiscounted	<u>\$ 8,980,709</u>	<u>\$ 8,650,953</u>
Ending liability, discounted (recorded balance at December 31)	<u>\$ 8,680,215</u>	<u>\$ 8,424,705</u>

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

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 8 - Compensated Absences

The Fund has recorded a liability for earned but unused compensatory, merit, 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, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Beginning liability	\$ 4,523,566	\$ 4,400,088
Additions	5,122,248	4,623,070
Reductions	<u>(4,574,457)</u>	<u>(4,499,592)</u>
Ending liability	<u>\$ 5,071,357</u>	<u>\$ 4,523,566</u>

Note 9 - 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 on a Remedial Investigation (“RI”) and Feasibility Study (“FS”) to evaluate the risk to human health and the environment within the six mile superfund area, identify the possible early action clean-up sites, and generally evaluate the feasibility of clean-up options for use in the ultimate remedial actions that the EPA will require. The RI and FS are complete. On November 2, 2012, the EPA and Ecology approved the Lower Duwamish Waterway Group’s FS which provides sufficient information to support selection of a remedy for this Site. 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.

Specific “early action sites” have been cleaned separately up under Administrative Orders on Consent (“AOC”). The Fund, together with other PRPs, has voluntarily agreed to clean-up two early action sites identified during the RI under EPA issued AOC: Slip 4 and T-117. Slip 4 cleanup is complete; T-117 will be completed by 2016.

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 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. No specific requirements for remediation by PRPs have been made by the EPA as of the date of this report. The RI is complete and the FS is anticipated to be completed by 2016.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 9 - Environmental Liabilities (Continued)

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 RI is expected to be completed in 2015 followed by the FS in late 2015. A Clean-up Action Plan is expected from the Department of Ecology in about 2016.

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.

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. Estimated outlays were based on current cost and no adjustments were made for discounting or inflation. 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 or regulations.

**SEATTLE PUBLIC UTILITIES -
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NOTES TO FINANCIAL STATEMENTS**

Note 9 - Environmental Liabilities (Continued)

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 \$4.0 million and \$4.8 million as of December 31, 2014 and 2013, respectively. During 2014, the Fund received an environmental cost recovery of \$0.7 million from Seattle City Light related to the T117 "early action site" along the Lower Duwamish Waterway.

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

	<u>2014</u>	<u>2013</u>
Beginning environmental liability, net of recovery	\$ 65,461,101	\$ 61,535,109
Payments or amortization	(2,514,388)	(1,903,351)
Incurred environmental liability	<u>4,733,688</u>	<u>5,829,343</u>
Ending environmental liability, net of recovery	<u>\$ 67,680,401</u>	<u>\$ 65,461,101</u>

Note 10 - 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 2014, the Fund borrowed \$546,319, which included capitalized interest on a water pollution control revolving fund loan from the Washington State Department of Ecology for design and construction of a stormwater facility in the Capitol Hill area of Seattle. The Fund borrowed \$1,334,279 including capitalized interest in 2013. Amounts borrowed under this agreement accrue interest at 2.6% per annum and are to be repaid by November 2033.

In 2013, the Fund made an additional draw of \$425,582 on a public works trust fund loan from the Washington State Department of Commerce for construction and site improvements in the Midvale area of Seattle. Amounts borrowed under this agreement accrue interest at 0.5% per annum and are to be repaid by June 2031.

**SEATTLE PUBLIC UTILITIES -
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NOTES TO FINANCIAL STATEMENTS**

Note 10 - Loans (Continued)

Loans outstanding as of December 31, 2014 and 2013 are as follows:

Description	Maturity Years	Interest Rate	Amount Borrowed	Loans Outstanding 2014	Loans Outstanding 2013
Midvale	2013-2031	0.25%	4,000,000	\$ 3,600,102	\$ 3,811,873
Thornton Creek Natural Drainage Systems	2006-2024	0.5%	3,700,000	1,958,824	2,154,706
High Point Natural Drainage Systems	2010-2029	1.5%	2,679,413	2,050,056	2,175,685
South Park Flood Control and Local Drainage Program	2007-2025	0.5%	3,400,000	2,168,351	2,365,473
Ballard Green Streets ARRA Project	2011-2020	2.9%	603,209	398,029	457,898
Thornton Creek Water Quality Project	2011-2030	1.5%	6,983,021	5,733,208	6,059,334
Capital Hill Water Quality Project	2014-2033	2.6%	1,880,598	1,858,863	1,334,279
			<u>\$ 23,246,241</u>	<u>\$ 17,767,433</u>	<u>\$ 18,359,248</u>

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

Years Ending December 31,	Principal	Interest	Total
2015	\$ 1,201,646	\$ 202,574	\$ 1,404,220
2016	1,212,401	191,045	1,403,446
2017	1,223,366	177,585	1,400,951
2018	1,234,547	163,909	1,398,456
2019	1,245,948	150,014	1,395,962
2020-2024	6,102,306	548,905	6,651,211
2025-2029	4,446,272	238,639	4,684,911
2030-2033	1,100,947	31,260	1,132,207
	<u>\$ 17,767,433</u>	<u>\$ 1,703,931</u>	<u>\$ 19,471,364</u>

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

	2014	2013
Net loans, beginning of year	\$ 18,359,248	\$ 17,693,988
Loan proceeds	546,319	1,759,861
Principal payments	<u>(1,138,134)</u>	<u>(1,094,601)</u>
Net loans, end of year	<u>\$ 17,767,433</u>	<u>\$ 18,359,248</u>
Loans due within one year	<u>\$ 1,201,646</u>	<u>\$ 1,116,399</u>
Loans, noncurrent	<u>\$ 16,565,787</u>	<u>\$ 17,242,849</u>

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS**

Note 11 - Notes and Contracts Receivable

The Fund has an agreement with the Seattle Housing Authority for the recovery of the remaining unreimbursed cost of the Fund's contributions of public infrastructure to the New Holly redevelopment project. As of December 31, 2014, the Seattle Housing Authority receivable was \$1,204,147.

In addition, the Fund has an agreement with private individuals for a sewer connection charge contract. The receivable was \$6,320 at December 31, 2014. Also, as part of the settlement agreement related to cleanup costs caused by improper construction of the stormwater detention system, Schneider Homes had a remaining receivable of \$25,000 as of December 31, 2014.

Notes and contracts receivable are composed of the following as of December 31:

	<u>2014</u>	<u>2013</u>
Seattle Housing Authority receivable	\$ 1,204,147	\$ 1,252,189
Dalcerro receivable	6,320	7,320
Schneider Homes receivable	25,000	-
Total notes and contracts receivable	<u>1,235,467</u>	<u>1,259,509</u>
Due within one year	<u>(76,378)</u>	<u>(49,042)</u>
Total non-current notes and contracts receivable	<u>\$ 1,159,089</u>	<u>\$ 1,210,467</u>

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 \$139,728,735 and \$137,656,267 for fiscal years 2014 and 2013, respectively.

Note 13 - Restatement of Financial Covenant

Subsequent to the original issuance on April 30, 2015 of the financial statements as of and for the years ended December 31, 2014 and 2013, an error was identified related to the disclosure of certain financial covenant information for the Fund. The calculation of net revenue available for debt service was revised as a result of a clarification of certain terms and information related to the underlying bond ordinance. In the previously issued financial statements, the Financial Covenant section of Note 4 disclosed a net revenue available for debt service of 297%, which has been revised to 298%.

OTHER INFORMATION (UNAUDITED)

**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>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
Population Served	612,000	612,100	616,500	626,600	640,500
Billed Wastewater Revenues	\$ 184,107	\$ 203,590	\$ 236,935	\$ 244,476	\$ 242,844
Billed Wastewater Volume (MG)					
Residential	7,824	7,400	7,707	7,594	7,408
Commercial	13,049	12,803	13,217	13,218	13,243
Total	<u>20,873</u>	<u>20,203</u>	<u>20,924</u>	<u>20,812</u>	<u>20,651</u>
Gallons Used per Day per Capita	93.4	90.4	93.0	91.0	88.3

Drainage and Wastewater - 2014 Accounts and Billed Revenues

Customer Accounts	<u>Drainage</u>	<u>Wastewater</u>
Residential	147,995	153,986
Commercial	<u>65,471</u>	<u>18,673</u>
Total	<u><u>213,466</u></u>	<u><u>172,659</u></u>
	<u>Drainage</u>	<u>Wastewater</u>
Billed Revenue		
Residential	\$ 48,830,896	\$ 85,855,948
Commercial	<u>44,951,223</u>	<u>154,344,087</u>
Total	<u><u>\$ 93,782,119</u></u>	<u><u>\$ 240,200,035</u></u>

**SEATTLE PUBLIC UTILITIES -
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(An Enterprise Fund of the City of Seattle)
OTHER INFORMATION (UNAUDITED)**

Major Wastewater Customers - 2014 Annual Billed Revenues and Volumes

<u>Name</u>	<u>Revenue</u>	<u>Volume</u>
University of Washington	\$ 6,441,062	674,406
Seattle Housing Authority	\$ 2,398,811	279,849
City of Seattle	\$ 3,153,242	283,563
King County	\$ 1,501,553	124,749
Seattle Tunnel Partners	\$ 1,331,683	113,948
Port of Seattle	\$ 1,320,486	178,329
Darigold	\$ 1,093,193	78,390
The Boeing Company	\$ 890,240	81,650
Harborview Medical Center	\$ 855,200	78,918
Swedish Medical Group	\$ 850,532	88,952

Major Drainage Customers - 2014 Annual Billed Revenues and Acreage

<u>Name</u>	<u>Revenue</u>	<u>Acres</u>
City of Seattle	\$ 5,662,105	4,947
Port of Seattle	\$ 3,747,917	974
Seattle Public Schools	\$ 1,822,202	685
King County	\$ 1,733,622	598
BNSF Rwy Co.	\$ 1,351,034	414
University of Washington	\$ 1,492,508	570
United States Government	\$ 809,085	293
Seattle Housing Authority	\$ 803,697	299
Union Pacific Railroad Co.	\$ 559,750	154
Seattle Community Colleges	\$ 333,456	158

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
OTHER INFORMATION (UNAUDITED)**

Wastewater Rates

	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>
Volume rate per ccf	\$ 8.98	\$ 10.28	\$ 10.68	\$ 11.65	\$ 11.75	\$ 11.84

Note: 1 CCF equals 748 gallons. Wastewater rate increased 0.9% and 9.1% in 2014 and 2013, respectively.

Drainage Rates

Flat Rate per Parcel	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	% Impervious Space
Single Family Residential*						
< 3,000 sq. ft.	\$ 134.06	\$ 149.33	\$ 164.05	\$ 180.96	\$ 198.83	
3,000 - 4,999 sq. ft.	\$ 173.10	\$ 192.79	\$ 212.92	\$ 234.87	\$ 258.06	
5,000 - 6,999 sq. ft.	\$ 234.94	\$ 261.66	\$ 289.11	\$ 318.92	\$ 350.40	
7,000 - 9,999 sq. ft.	\$ 298.32	\$ 332.23	\$ 365.97	\$ 403.70	\$ 443.55	
Rate per 1,000 sq. ft.						
Undeveloped						0 - 15%
Regular	\$ 19.72	\$ 21.96	\$ 23.31	\$ 25.71	\$ 28.25	
Low Impact	\$ 12.35	\$ 13.76	\$ 13.65	\$ 15.06	\$ 16.54	
Light						16 - 35%
Regular	\$ 29.62	\$ 32.98	\$ 36.05	\$ 39.76	\$ 43.69	
Low Impact	\$ 23.47	\$ 24.14	\$ 28.35	\$ 31.27	\$ 34.36	
Medium						36 - 65%
Regular	\$ 42.89	\$ 47.76	\$ 52.35	\$ 57.75	\$ 63.45	
Low Impact	\$ 34.43	\$ 38.35	\$ 42.11	\$ 46.45	\$ 51.04	
High	\$ 56.57	\$ 63.01	\$ 70.23	\$ 77.48	\$ 85.12	66 - 85%
Very High	\$ 66.90	\$ 74.49	\$ 83.08	\$ 91.65	\$ 100.69	86 - 100%

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