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

SEATTLE PUBLIC UTILITIES – WATER FUND (AN ENTERPRISE FUND OF THE CITY OF SEATTLE)

December 31, 2017 and 2016

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Report of Independent Auditors

To the Director of Seattle Public Utilities
Water Fund
Seattle, Washington

Report on the Financial Statements

We have audited the accompanying financial statements of Seattle Public Utilities – Water Fund (the Fund), which comprise the statements of net position as of December 31, 2017, and 2016, 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 we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Seattle Public Utilities – Water Fund as of December 31, 2017, and 2016, 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

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the schedule of Seattle Public Utilities' proportionate share of the net pension liability and schedule of Seattle Public Utilities' contributions, listed in the table of contents, be presented to supplement the financial statements. 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 basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The other information presented on pages 45 – 48 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
May 4, 2018

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 Water Fund (the Fund) for the fiscal years ended December 31, 2017 and 2016. The revenues, expenses, assets, deferred outflows of resources, liabilities, and deferred inflows of resources of Seattle's water system are recorded in the Water 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 like 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 13 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, 2017 and 2016, on all the Fund's assets, deferred outflows of resources, liabilities and deferred inflows of resources. The difference between assets combined with deferred outflows of resources and liabilities combined with deferred inflows of resources is reported as net position. They also provide information about the nature and amounts of investments in resources (assets and deferred outflows of resources), obligations to the Fund's creditors (liabilities and deferred inflows of resources), and provide the basis for assessing the liquidity and financial flexibility of the Fund.

The statements of revenues, expenses, and changes in net position present changes in the Fund's net position for the years ended December 31, 2017 and 2016. 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, 2017 and 2016, and to provide answers to questions about sources, uses, and impacts to cash, these statements report cash receipts, cash payments, and net changes in cash resulting from operations, investing and financing activities for the reporting period.

Notes to the financial statements – The notes are an integral part of the financial statements. They provide additional disclosures that are essential to a full understanding of the data provided in the financial statements, such as for certain estimates and financing details. The notes to the financial statements begin on page 18 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, 2017 and 2016, the Fund's assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources, resulting in surpluses in total net position of $454.6 million and $403.4 million, respectively. In 2017, the Fund's change in net position was an increase of $51.2 million (12.7%) as compared to 2016 with an increase of $43.3 million (12%). The following summary statement of net position present the assets and deferred outflows of resources of the Fund and show the mix of liabilities, deferred inflows of resources and net position used to acquire these assets:

Summary Statement of Net Position

	December 31,		
	2017	2016	2015
ASSETS			
Current assets	$ 93,650,376	$ 77,560,250	$ 78,167,413
Capital assets, net	1,304,616,463	1,276,574,052	1,241,010,581
Other	205,025,295	118,596,788	142,883,299
Total assets	1,603,292,134	1,472,731,090	1,462,061,293
DEFERRED OUTFLOWS OF RESOURCES	36,512,109	46,224,058	39,308,608
Total assets and deferred outflows of resources	$ 1,639,804,243	$ 1,518,955,148	$ 1,501,369,901
LIABILITIES			
Current liabilities	$ 82,783,767	$ 80,507,282	$ 84,602,668
Revenue bonds	915,683,095	856,408,050	899,911,354
Other	133,267,841	135,491,770	121,553,555
Total liabilities	1,131,734,703	1,072,407,102	1,106,067,577
DEFERRED INFLOWS OF RESOURCES			
Revenue stabilization fund	46,511,311	40,957,140	35,193,116
Deferred inflows - pension	6,997,750	2,225,903	-
Total deferred inflows of resources	53,509,061	43,183,043	35,193,116
NET POSITION			
Net investment in capital assets	473,343,322	435,253,916	388,808,815
Restricted	13,045,244	12,787,668	12,526,734
Unrestricted	(31,828,087)	(44,676,581)	(41,226,341)
TOTAL NET POSITION	454,560,479	403,365,003	360,109,208
Total liabilities, deferred inflows of resources and net position	$ 1,639,804,243	$ 1,518,955,148	$ 1,501,369,901

Financial Analysis (continued)

2017 Compared to 2016

Assets – Current assets increased $16.1 million (20.7%) from 2016. This is primarily due to increases in operating cash of $15.5 million, unbilled revenue of $1.2 million, due from other governments of $1.3 million and $0.1 million in materials and supplies inventory. The increase was offset by decreases in accounts receivable, net of allowance for doubtful accounts of $1.7 million, interest and dividends of $0.1 million and due from other funds of $0.2 million.

Capital assets increased $28.0 million (2.2%) from 2016. Construction in progress and other plant assets increased $48.3 million; increase is mostly due to infrastructure improvements, rehabilitation, facility improvements and water reservoir coverings. This change was offset by $20.3 million increase in accumulated depreciation (Note 3).

Other assets increased $86.4 million (72.9%) from 2016. The largest portion of the change was due to an increase in restricted cash and equity in pooled investments of $91.2 million, due to the issuance of the 2017 Water System Improvement and Refunding Revenue Bonds (Note 4). This increase was offset by decreases of $3.5 million in conservation costs, $0.5 million in regulatory assets, $0.4 million in notes and contracts receivable and $0.4 million in other charges and long-term prepayments.

Deferred outflows of resources – Deferred outflows of resources decreased by $9.7 million (a negative 21.0%) from 2016. This change resulted from a $5.4 million decrease in amortization of deferred loss on advanced refunding of older bonds, offset by a gain on the 2017 refunding. Pension contributions and changes in assumptions related to pension accounting also decreased $4.3 million.

Liabilities – Current liabilities increased $2.3 million (2.8%) from 2016. This change mostly resulted from increases of $1.0 million in interest payable, $1.7 million in current portion of bonds payable, $0.5 million in salaries, benefits and payroll taxes payable and $0.9 million in loans payable. These increases were offset by decreases of $1.0 million in accounts payable and $0.8 million in due to other funds.

Other liabilities decreased $2.2 million (negative 1.6%) over 2016. The largest portion of this decrease, $6.4 million, resulted from the decrease in the Fund's net pension liability and $3.0 million decrease in the noncurrent portion of the HCP liability. These decreases were offset by increases of $5.2 million in loans, $1.8 million in claims payable, $0.1 million in unfunded other post-retirement benefits and $0.1 million in compensated absences payable.

Deferred inflows of resources – Deferred inflow of resources increased by $10.3 million (23.9%) from 2016. This increase is due to a net deposit of $5.2 million to the revenue stabilization account, and $0.3 million interest earned on the account, and $4.8 million change in difference between employer contribution and proportionate share of employer contributions.

Financial Analysis (continued)

Net position – Net investment in capital assets was the largest portion of the Fund's net position ($473.3 million or 104.1%). This amount reflects the Fund's investment in capital assets such as land, buildings, and equipment, less accumulated depreciation and any related outstanding debt used to acquire those assets. The Fund uses these assets to provide services to customers; consequently, these assets are not available for future spending. Although the Fund's investment in its capital assets is reported net of related debt, the resources needed to repay the debt are provided by fees paid by customers for services provided by these assets. In 2017, net investment in capital assets increased $38.0 million from 2016 primarily from an increase in utility plant and construction in progress.

The Fund's restricted net position ($13.0 million or 2.9%) represents resources that are subject to restrictions on how they may be used. Restricted net position increased $0.3 million.

The Fund's unrestricted net position (a negative $31.8 million or 7.0%) represent resources that are not subject to external restrictions and may be used to meet the Fund's obligations to creditors. This portion decreased $12.8 million in 2017 as compared to 2016. The main component of this change is the increase in investment in capital assets.

2016 Compared to 2015

Assets – Current assets decreased $0.6 million (a negative 0.8%) from 2015. This is primarily due to a decrease in operating cash of $3.2 million. The decrease was offset by increases in accounts receivable, net of allowance for doubtful accounts of $1.0 million, unbilled revenues of $0.7 million, materials and supply inventory of $0.6 million and due from other governments of $0.4 million.

Capital assets increased $35.6 million (2.9%) from 2015. Construction in progress and other plant assets increased $82.2 million; increase is mostly due to infrastructure improvements, rehabilitation, facility improvements and water reservoir coverings. This increase was offset by $46.6 million increase in accumulated depreciation (Note 3).

Other assets decreased $24.3 million (a negative 17%) from 2015. The largest portion of the change was due to a decrease in restricted cash and equity in pooled investments of $23.2 million, which was used to fund plant assets and construction in progress.

Deferred outflows of resources – Deferred outflows of resources increased by $6.9 million (17.6%) from 2015. This increase is due to $8.5 million increase for pension contributions and changes in assumptions related to pension accounting. This increase was offset by a decrease of $1.6 million in deferred loss on advanced refunding of bonds.

Liabilities – Current liabilities decreased $4.1 million (a negative 4.8%) from 2015. This change mostly resulted from decreases of $2.8 million in accounts payable, $2.3 million in current portion of bonds payable, $1.2 million in salaries, benefits and payroll taxes payable and $0.4 million in interest payable. These decreases were offset by increases of $3.0 million in due to other funds.

Other liabilities increased $13.9 million (11.5%) over 2015. The largest portion of this increase, $10.4 million, resulted from the increase in the Fund's net pension liability. Additional increases included $2.4 million in loans, $0.9 million in claims payable and $0.6 million in the noncurrent portion of the HCP liability. These increases were offset by a decrease of $0.5 million in compensated absences payable.

Deferred inflows of resources – Deferred inflow of resources increased by $8.0 million (22.7%) from 2015. This increase is due to a deposit of $5.8 million to the revenue stabilization account, interest earned on the account, and $2.2 million change in pension employer contributions.

Net position – Net investment in capital assets was the largest portion of the Fund's net position ($435.3 million or 107.9%). This amount reflects the Fund's investment in capital assets such as land, buildings, and equipment, less accumulated depreciation and any related outstanding debt used to acquire those assets. The Fund uses these assets to provide services to customers; consequently, these assets are not available for future spending. Although the Fund's investment in its capital assets is reported net of related debt, the resources needed to repay the debt are provided by fees paid by customers for services provided by these assets. In 2016, net investment in capital assets increased $46.4 million from 2015 primarily from an increase in utility plant and construction in progress.

The Fund's restricted net position ($12.8 million or 3.2%) represents resources that are subject to restrictions on how they may be used. Restricted net position increased $0.3 million primarily due to increases of $0.7 million for conservation programs, which was offset by a decrease of $0.4 million in other charges.

The Fund's unrestricted net position (a negative $44.7 million or 11.1%) represent resources that are not subject to external restrictions and may be used to meet the Fund's obligations to creditors. This portion increased $3.5 million in 2016 as compared to 2015. The two main components for this change include increases in investment in capital assets and net pension liability as required by GASB Statement No. 68 for reporting pensions (Note 9).

Financial Analysis (continued)

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

	December 31, 2017	December 31, 2016	December 31, 2015
Operating revenues	$ 262,896,454	$ 251,363,807	$ 251,977,342
Operating expenses	(201,886,191)	(196,640,704)	(193,606,066)
Net operating income	61,010,263	54,723,103	58,371,276
Other expenses, net of other revenues	(31,879,002)	(29,860,684)	(30,559,620)
Fees, contributions, and grants	22,064,215	18,393,376	10,393,558
Change in net position	$ 51,195,476	$ 43,255,795	$ 38,205,214

2017 Compared to 2016

Operating revenues increased approximately $11.5 million (4.6%) over 2016. This change was driven by increases in direct service revenue of $10.4 million and wholesale revenue of $3.1 million resulting from increased consumption. These increases were offset by a decrease of $2.0 million in other revenues.

Operating expenses increased $5.2 million (2.7%) from 2016. Notable factors affecting this change include increases of $2.2 million in general and administrative services, $2.2 million in taxes, $1.0 million in project delivery services, $0.7 million in field operation services, $0.3 million in customer services, and $0.3 million in utility systems management. These increases were offset by decreases of $0.7 million in planning and development services and $0.8 million in depreciation and amortization expenses.

Other expenses, net of other revenues increased by $2.0 million (6.8%) over 2016. The change was primarily due to increases in interest expense of $2.7 million, investment income of $1.4 million and amortization of bond premiums, discounts and refunding loss of $0.7 million. These increases were offset by a decrease in gain on sale of capital assets of $1.4 million.

Capital fees, contributions and grants increased by $3.7 million (20%) over 2016 primarily due to increases in donated plant of $1.4 million, capital contributions for other meters and services of $1.3 million, $0.8 million in capital grants, $0.3 million in private contract water main and $0.1 million in hydrants. These increases were offset by a decrease in agencies/inter-local of $0.1 million.

Financial Analysis (continued)

2016 Compared to 2015

Operating revenues decreased approximately $0.6 million (a negative 0.2%) over 2015. This change was driven by a decrease in direct service revenue of $2.2 million resulting from a decline in consumption and $1.0 million decrease in other revenues. These decreases were offset by increases of $0.8 million in wholesale revenue and $1.7 million transfer to the revenue stabilization account.

Operating expenses increased $3.0 million (1.6%) from 2015. Notable factors affecting this change include increases of $2.6 million in general and administrative services, $1.8 million in depreciation and amortization expense, $0.7 million in utility systems management and $0.6 million in planning and development. These increases were offset by decreases of $1.9 million in field operations and $0.9 million in taxes.

Other expenses, net of other revenues, decreased by $0.7 million (a negative 2.3%) over 2015. The change was primarily due to decreases in interest expense of $2.5 million, gain on sale of capital assets of $2.1 million and $0.2 million in interest income. These decreases were offset by increases in bond related amortization of $0.3 million and other, net of $0.2 million.

Capital fees, contributions and grants increased by $8.0 million (77.0%) over 2015 primarily due to increases in donated plant of $6.0 million, capital contributions for other meters and services of $2.4 million and $0.9 million in capital grants. These increases were offset by decreases in capital contributions for connection charges of $1.0 million and hydrants of $0.3 million.

Capital Assets

The following table summarizes capital assets, net of accumulated depreciation, by major asset category as of December 31, 2017, 2016, and 2015:

Summary of Capital Assets, Net of Accumulated Depreciation

	December 31, 2017	December 31, 2016	December 31, 2015
Land and land rights	$ 48,319,324	$ 45,137,867	$ 44,453,438
Buildings	130,740,269	133,985,132	137,638,742
Structures	259,961,223	244,589,121	246,598,683
Machinery and equipment	806,533,435	748,597,693	722,853,338
Computer systems	20,428,194	22,990,354	12,865,870
Construction in progress	36,970,991	79,610,858	75,006,536
Other property	1,663,027	1,663,027	1,593,974
Capital assets, net of accumulated depreciation	$ 1,304,616,463	$ 1,276,574,052	$ 1,241,010,581

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

2017 Compared to 2016

The Fund's investment in capital assets for the year ended December 31, 2017 was $1.3 billion, net of accumulated depreciation. This represents an increase of $28.0 million (2.2%) compared to 2016. Highlights of the Fund's major capital assets placed in service during 2017 include the following:

- Morse Lake Pump Plant totaling $37.9 million
- Water infrastructure improvements and rehabilitation totaling $25.2 million.
- Alaskan Way Viaduct and Seawall totaling $19.9 million.
- Reservoir covering and improvement totaling $11.5 million

Capital Assets (continued)

As of December 31, 2017, the Fund had $37.0 million in construction work in progress. Major projects under construction are the following:

- Regional Facility, Cedar Falls, totaling $7.4 million
- Technology infrastructure improvements totaling $6.7 million
- Water system improvements and rehabilitation totaling $6.0 million
- Alaskan Way Viaduct and Seawall totaling $3.5 million.
- Dam Safety totaling $2.2 million
- First Hill Streetcar project totaling $2.1 million

2016 Compared to 2015

The Fund's investment in capital assets for the year ended December 31, 2016 was $1.3 billion, net of accumulated depreciation. This represents an increase of $35.6 million (2.9%) compared to 2015. Highlights of the Fund's major capital assets placed in service during 2016 include the following:

- Technology infrastructure improvements totaling $16.4 million
- Distribution infrastructure system improvements totaling $13.2 million
- Water infrastructure improvements and rehabilitation totaling $12.2 million.
- Alaskan Way Viaduct and Seawall totaling $10.7 million.
- Reservoir covering and improvement totaling $4.8 million

As of December 31, 2016, the Fund had $79.6 million in construction work in progress. Major projects under construction are the following:

- Morse Lake Pump Plant Project totaling $37.9 million.
- Alaskan Way Viaduct and Seawall totaling $19.0 million.
- Water system improvements and rehabilitation totaling $2.7 million.

Capital Assets (continued)

- Reservoir covering and improvement totaling $2.6 million.
- Regional Facility, Cedar Falls, totaling $2.2 million
- Business and technology infrastructure upgrades totaling $2.0 million.

Debt Administration

The Fund's debt primarily consists of bonded debt and loans. Bonded debt is secured solely by water system revenues and provides financing for capital improvements. Loans issued by the Washington State Agencies for certain capital improvements are unsecured. The Fund's credit ratings on its bonds were Aa1 and AA+ by Moody's Investors Service Inc. and Standard & Poor's Rating Services, respectively. Additional details about the Fund's revenue bonds and loans are in Notes 4 and 10 of this report.

2017 Compared to 2016

At December 31, 2017, the Fund had $858.2 million in bonded debt and $30.9 million in loans, as compared to $810.0 million and $24.8 million, respectively, at December 31, 2016. Bonded debt increased a net $48.2 million, attributed to the issuance of the 2017 water system improvement and refunding revenue bonds and scheduled payments of debt principal on existing bonds. Loans also increased $6.1 million due to additional loan proceeds for the Morse Lake Pump Project, offset by scheduled principal payments on existing loans.

2016 Compared to 2015

At December 31, 2016, the Fund had $810.0 million in bonded debt and $24.8 million in loans, as compared to $851.6 million and $22.3 million, respectively, at December 31, 2015. Bonded debt decreased $41.6 million, attributed to scheduled payments of debt principal on existing bonds. However, loans increased $2.4 million due to additional draw downs on the loan for the Morse Lake Pump Project, offset by scheduled principal payments on existing loans.

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, WA 98124-4018, telephone (206) 684-3000.

Statements of Net Position

	December 31, 2017	December 31, 2016
ASSETS		
CURRENT ASSETS		
Operating cash and equity in pooled investments	$ 54,637,435	$ 39,106,002
Receivables		
Accounts, net of allowance	13,643,663	15,316,610
Interest and dividends	834,322	984,287
Unbilled revenues	15,679,001	14,533,548
Notes and other contracts	-	19,850
Due from other funds	746,581	908,089
Due from other governments	2,296,306	952,798
Materials and supplies inventory	5,741,476	5,667,474
Prepayments and other current assets	71,592	71,592
Total current assets	93,650,376	77,560,250
NONCURRENT ASSETS		
Restricted cash and equity in pooled investments	163,252,748	72,093,856
Prepayments long-term	1,018,594	1,090,187
Notes and contracts receivable	-	374,721
Conservation costs	28,731,758	32,191,814
Regulatory assets	9,943,884	10,472,770
Other charges	2,078,311	2,373,440
Capital assets		
Land and land rights	48,319,324	45,137,867
Plant in service, excluding land	2,009,173,197	1,921,380,333
Less accumulated depreciation	(791,510,076)	(771,218,033)
Construction in progress	36,970,991	79,610,858
Other property, net	1,663,027	1,663,027
Total noncurrent assets	1,509,641,758	1,395,170,840
Total assets	1,603,292,134	1,472,731,090
DEFERRED OUTFLOWS OF RESOURCES		
Unamortized loss on advanced refunding	22,460,860	27,855,673
Pension contributions and changes in assumptions	14,051,249	18,368,385
Total deferred outflow of resources	36,512,109	46,224,058
Total assets and deferred outflows of resources	$ 1,639,804,243	$ 1,518,955,148

See accompanying notes.

Seattle Public Utilities – Water Fund
(An Enterprise Fund of the City of Seattle)
Statements of Net Position

	December 31, 2017	December 31, 2016
LIABILITIES		
CURRENT LIABILITIES		
Accounts payable	$ 6,485,953	$ 7,485,706
Salaries, benefits, and payroll taxes payable	3,970,605	3,461,792
Compensated absences payable	418,239	389,596
Due to other funds	7,769,803	8,608,550
Due to other governments	124,831	-
Interest payable	12,942,096	11,927,881
Taxes payable	755,267	694,210
Revenue bonds due within one year	41,020,000	39,345,000
Claims payable	2,028,452	2,151,385
Habitat conservation program liability	710,410	967,601
Loans payable, due within one year	2,049,935	1,124,987
Other	4,508,176	4,350,574
Total current liabilities	82,783,767	80,507,282
NONCURRENT LIABILITIES		
Compensated absences payable	4,411,236	4,355,516
Claims payable	5,251,274	3,488,652
Habitat conservation program liability	4,823,148	7,791,650
Loans	28,876,558	23,654,493
Unfunded other post retirement benefits	2,824,163	2,718,526
Net pension liability	86,689,301	93,080,303
Other noncurrent liabilities	392,161	402,630
Revenue bonds	858,215,000	809,950,000
Less bonds due within one year	(41,020,000)	(39,345,000)
Bond premiums	98,488,095	85,803,050
Total noncurrent liabilities	1,048,950,936	991,899,820
Total liabilities	1,131,734,703	1,072,407,102
DEFERRED INFLOWS OF RESOURCES		
Rate stabilization fund	46,511,311	40,957,140
Deferred inflows-pension	6,997,750	2,225,903
Total deferred inflows of resources	53,509,061	43,183,043
NET POSITION		
Net investment in capital assets	473,343,322	435,253,916
Restricted for		
Other charges	4,770,363	4,640,073
Conservation costs	4,082,777	4,012,209
Habitat conservation program	4,192,104	4,135,386
Unrestricted	(31,828,087)	(44,676,581)
Total net position	454,560,479	403,365,003
Total liabilities, deferred inflows of resources and net position	$ 1,639,804,243	$ 1,518,955,148

See accompanying notes.

Statements of Revenues, Expenses, and Changes in Net Position

	Years Ended December 31, 2017	2016
OPERATING REVENUES		
Charges for services and other revenues	$ 262,896,454	$ 251,363,807
OPERATING EXPENSES		
Planning and development	1,499,027	2,140,901
Utility systems management	15,740,872	15,350,256
Field operations	30,218,321	29,501,690
Project delivery	7,776,076	6,788,784
Customer services	8,279,594	7,990,599
General and administrative	43,698,026	41,534,069
City business and occupation taxes	32,924,420	31,347,395
Other taxes	10,746,447	10,142,634
Depreciation and other amortization	51,003,408	51,844,376
Total operating expenses	201,886,191	196,640,704
OPERATING INCOME	61,010,263	54,723,103
NON OPERATING REVENUES (EXPENSES)		
Investment income	4,090,237	2,635,432
Interest expense	(39,631,539)	(36,918,271)
Amortization of bond premiums	4,625,318	4,158,304
Amortization of bond refunding loss	(1,392,301)	(1,596,996)
Gain (loss) on sale of capital assets	(1,020,213)	405,518
Contributions and grants	125,356	264,979
Other, net	1,324,140	1,190,350
Total nonoperating revenues (expenses)	(31,879,002)	(29,860,684)
Income before capital contributions and grants	29,131,261	24,862,419
Capital contributions and grants	22,064,215	18,393,376
CHANGE IN NET POSITION	51,195,476	43,255,795
NET POSITION		
Beginning of year	403,365,003	360,109,208
End of year	$ 454,560,479	$ 403,365,003

See accompanying notes.

Seattle Public Utilities – Water Fund
(An Enterprise Fund of the City of Seattle)
Statements of Cash Flows

	Years Ended December 31, 2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from customers	$ 270,798,927	$ 257,433,858
Cash paid to suppliers	(40,174,131)	(31,926,217)
Cash paid to employees	(63,102,936)	(67,426,477)
Cash paid for taxes	(43,406,266)	(41,717,865)
Net cash provided by operating activities	124,115,594	116,363,299
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Noncapital grants received	22,463	283,113
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from the sales of bonds and other long-term debt	223,548,639	3,562,390
Principal payments on long-term debt	(40,507,002)	(42,442,027)
Bond refunding	(107,055,166)	-
Capital expenditures and other charges paid	(70,111,922)	(76,611,083)
Interest paid on long-term debt	(40,699,960)	(40,549,603)
Build America Bonds Federal Interest Subsidy	1,987,997	1,990,132
Capital fees and grants received	12,440,324	9,887,269
Debt issuance costs	(718,125)	-
Proceeds from sale of capital assets	1,415,278	519,166
Net cash used in capital and related financing activities	(19,699,937)	(143,643,756)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest received on investments	2,252,205	622,696
NET INCREASE (DECREASE) IN CASH AND EQUITY IN POOLED INVESTMENTS	106,690,325	(26,374,648)
CASH AND EQUITY IN POOLED INVESTMENTS		
Beginning of year	111,199,858	137,574,506
End of year	$ 217,890,183	$ 111,199,858
CASH AT THE END OF THE YEAR CONSISTS OF		
Operating cash and equity in pooled investments	$ 54,637,435	$ 39,106,002
Noncurrent restricted cash and equity in pooled investments	163,252,748	72,093,856
Total cash at the end of the year	$ 217,890,183	$ 111,199,858

See accompanying notes.

	Years Ended December 31, 2017	Years Ended December 31, 2016
RECONCILIATION OF NET OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Net operating income	$ 61,010,263	$ 54,723,103
Adjustments to reconcile net operating income to net cash provided by operating activities		
Adjustment for net pension liability	2,697,981	4,108,985
Depreciation and amortization	51,003,408	51,844,376
Nonoperating revenues and expenses	2,530,555	2,540,994
Changes in operating assets and liabilities		
Accounts receivable	1,672,947	(918,185)
Unbilled revenues	(1,145,453)	(699,203)
Due from other funds	161,507	(14,625)
Due from other governments	(594,969)	471,537
Materials and supplies inventory	(74,002)	(565,828)
Other assets	466,163	90,522
Accounts payable	(999,753)	(2,776,709)
Salaries, benefits, and payroll taxes payable	508,812	(1,187,678)
Compensated absences payable	84,363	(552,939)
Due to other funds	(838,747)	2,962,694
Due to other governments	124,831	-
Claims payable	1,639,689	791,758
Taxes payable	61,058	(52,128)
Regulatory liability - revenue stabilization fund	5,554,171	5,764,025
Credits and other	252,770	(167,400)
Total adjustments	63,105,331	61,640,196
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 124,115,594	$ 116,363,299
NONCASH TRANSACTIONS		
Contributed infrastructure	$ 8,978,246	$ 7,620,582

Note 1 – Operations and Summary of Significant Accounting Policies

Operations – The City of Seattle, Seattle Public Utilities – Water Fund (the Fund) is a public utility enterprise fund of the City of Seattle (the City). The Fund was established to account for activities of the water system operated by Seattle Public Utilities (SPU). The water system, established in 1890, provides water to the greater Seattle area through direct service to customers and through purveyors, such as suburban water districts and municipalities. The activities of the water system include protection of available water supply, transmission of water to customers, development of water conservation programs, evaluation of new water sources, and management of the City's water system assets, which include the Tolt and Cedar River Watersheds, water pipes, pumping stations, and treatment plants.

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

SPU receives certain services from other departments and agencies of the City, including information technologies and some that are normally considered to be general and administrative. The Fund is charged a share of these costs and during 2017 and 2016, paid $21,637,823 and $13,002,147, respectively, to the City for its share of these services. The $8.6 million increase is largely attributable to the consolidation of Seattle Information Technology (IT). Additionally, the Fund pays a business and occupation utility tax to the City's General Fund. The Fund paid $32,924,420 and $31,347,395 for these taxes in 2017 and 2016, respectively.

The utility billing function is co-managed by SPU, Seattle City Light (SCL) and Seattle IT. SPU provides customer service through the call center and walk-in center. SCL and Seattle IT operates and manages the billing system. SPU and SCL bill and reimburse each other for these services. SPU reimburses Seattle IT for the information technologies services mentioned above. Within SPU, the costs and reimbursements were shared among its three utility funds (Water, Drainage and Wastewater, and Solid Waste). The Fund received reimbursements related to the call center and walk-in center of $2,056,243 and $2,104,912 in 2017 and 2016, respectively. The Fund paid $25,968 and $191,928 for the utility billing services in 2017 and 2016, respectively. These costs do not include reimbursements to Seattle IT for the Fund's share of capital costs for the Customer Care and Billing System (CCB) completed in 2016.

Water services provided to other City departments and agencies are billed at rates prescribed by City ordinances. The Fund collected $4,589,174 and $4,534,032 in 2017 and 2016, respectively, from the City for water services provided.

The Fund is subject to regulation by the City and the State of Washington. Service rates are authorized by ordinances passed by the Seattle City Council (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 (U.S. GAAP) 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.

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

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

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

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. Accounts receivable is shown net of allowances for doubtful accounts. The Fund also accrues an estimated amount for services that have been provided but not billed. Notes and contracts receivable arise from written agreements or contracts with public organizations and private individuals.

Due from/to other funds and governments – Activity between funds 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.

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, 2017, and 2016, the Fund's allowance for doubtful accounts was $363,652 and $375,616, respectively.

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

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.

Regulatory assets – 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 and loan 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.

Revenue Stabilization Fund – The Revenue Stabilization Fund (RSF) was established by City Ordinance 122841 to reduce year-to-year variation in rates. Amounts deposited into the RSF are excluded from the statements of revenues, expenses, and changes in net position and treated as a credit in accordance with GASB Statement No. 62. There was a net deposit to the RSF of $5.2 million in 2017. The RSF is included in the “Revenue Stabilization Account” identified in the Fund’s bond covenants. These covenants provide that withdrawals and deposits from the “Revenue Stabilization Account” shall augment or reduce adjusted net revenue available for the payment of debt service. In 2016, a deposit of $5.3 million was made and there were no withdrawals. In 2017, there was a deposit of $13.5 million and a withdrawal of $8.3 million made to the RSF.

Conservation costs – Conservation program costs that result in long-term benefits and reduce or postpone other capital expenditures or have a legal requirement are included in noncurrent assets and amortized over their expected useful lives, commencing when each program is in place. The conservation program costs are amortized over their expected useful lives of ten years. Certain costs related to the Habitat Conservation Plan (HCP) are included in the noncurrent assets and amortized through 2050, the year in which the plan expires. An incidental take permit was issued to the City by the federal government approving the HCP for 50 years. Costs of administering the conservation and HCP programs are expensed as incurred.

Other charges – Other charges include costs such as the Water System Plan, leasehold improvements, and the Tolt Levee modification. The Fund amortizes these charges over a 2- to 33-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 capitalize assets with a cost of $5,000 or more. The Fund receives donated assets such as water mains from developers and other governmental 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.

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

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

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

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

Buildings and fixtures	10 to 50 years
Earthen source of supply developments	100 years
Transmission and distribution pipelines, reservoirs, and tanks	15 to 100 years
Water mains	33 to 57 years
Pumps, wells, and treatment equipment	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 transmission and distribution pipelines, water mains asset group, reservoirs, and tanks. 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. As a result of implementing GASB Statement No. 68 and No. 71, the Fund has also recorded deferred outflows of resources for certain pension activities including, the difference between projected and actual experience, the difference between projected and actual earnings on investments, and contributions made subsequent to the measurement date (Note 9).

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

In addition to liabilities, the Statements 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. As a result of implementing GASB Statement No. 68 and No. 71, the Fund has also recorded deferred inflows of resources for changes in proportion and differences between employer contributions and proportionate share of contributions. The Fund has a revenue stabilization account which qualifies for reporting in this category.

BPA account – In 2003, the Bonneville Power Administration (BPA) purchased an easement in the amount of $6.0 million from the Fund to construct a power transmission line through the Cedar River Watershed. This $6.0 million, together with $657,149 in timber sales related to the easement, were deposited into the BPA account and classified as restricted assets. At December 31, 2017 and 2016, the cash balance in the BPA account was $465,836 and $458,211, respectively. Monies in the BPA account are considered a portion of the “Revenue Stabilization Account” described in bond covenants, and therefore shall augment or reduce adjusted net revenue available for the payment of debt service. The Fund will recognize the revenues deposited in the BPA account in the calculation of adjusted net revenues available for the payment of debt service as they are withdrawn to fund certain activities in the Cedar River Watershed.

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. The Fund records a liability for estimated sick leave payments.

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.

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

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

Operating revenues – The Fund provides water service to wholesale and retail customers and recognizes revenue when such service is provided. Wholesale customers (Purveyors) are under contract with the Fund, and rates are set based on cost allocation criteria stipulated in the contracts.

Service rates for all customers are authorized by ordinances passed by the City Council. Service revenues are recorded through cycle billings rendered to customers monthly or bimonthly. The Fund accrues and records unbilled water service revenues in the financial statements for services provided from the date of the last billing to year end.

Operating expenses – Certain expenses of the Fund are reported on the Statements of Revenues, Expenses, and Changes 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 water system.

- **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 15.54% of Fund revenues, net of certain credits and certain revenues. In addition, the Fund paid a 5.029% public utility tax to the State on a certain portion of revenues identified as utility revenues. The Fund also paid business and occupation tax to the City at the rate of 0.219% and to the State at the rate of 1.5% for certain other non-utility revenues.

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

Other 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 utility and are of a recurring nature. Major items are investment and interest income, interest expense, gains or losses on the sale of assets, and amortization of debt expenses.

Net position – The Statements of Net Position report all financial and capital resources. The difference between assets, deferred outflows of resources, liabilities, and deferred inflows of resources is net position. There are three components of net position: net investment in capital assets, restricted, and unrestricted.

Net investment in capital assets, consists of capital assets, less 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, 2017, are mainly related to conservation costs, HCP and certain other charges.

Unrestricted net positions are those that are 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 bond. The IRC requires that earnings on gross proceeds of any revenue bonds that are more than the amount prescribed will be surrendered to the Internal Revenue Service. As such, the Fund would record such a rebate as a liability. The Fund has included this information within the required supplementary information.

Accounting standard changes – GASB has issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. The primary objective of this statement is for the Fund to record its proportionate share of its defined other post-employment obligations for inactive and retired employees who receive benefits from the Fund. This statement is effective periods beginning after June 15, 2017. The Fund is evaluating the impact of this standard on the financial statements but anticipates recording amounts for the unfunded portion of the obligation. At this time, the amounts are not yet known.

GASB has issued Statement No. 82, *Pension Issues-an Amendment of GASB Statements No. 67, No. 68 and No. 73*. The statement requires issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee ("plan member") contribution requirements. This statement is effective for reporting periods beginning after June 15, 2016, except for the requirements for the selection of assumptions that deviate from the guidance in an Actuarial Standard of Practice in which the requirements are effective for an employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017. The Fund has included this within the required supplementary information provided.

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

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, risk liabilities, post-retirement benefits, pension liability, and other contingencies. Changes in these estimates and assumptions may have a material impact on the financial statements.

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, water conditions, weather and natural disaster-related disruptions, collective bargaining labor disputes, fish and other endangered species act issues, Environmental Protection Agency regulations, federal government regulations or orders concerning the operation, maintenance, and licensing of facilities.

Note 2 – Cash and Equity in Pooled Investments

Per Seattle Municipal Code, SMC 5.06.010 Investment Authority, the Director of Finance and Administrative Services (FAS) is authorized to invest all moneys in the City Treasury. Cash resources of all City funds are combined into a common investment pool that is managed by FAS. Each fund's share of the pooled investments is included in the participating fund's balance sheet under the caption "Cash and Equity in Pooled Investments." The pool operates like a demand deposit account in that all City funds may deposit cash at any time and also withdraw cash up to their respective fund balance out of the pool without prior notice or penalty.

Custodial credit risk – deposits – The custodial credit risk of deposits is the risk that in the event of bank failure of one of the City's depository institutions, the City's deposits or related collateral securities may not be returned in a timely manner. As of December 31, 2017, the City did not have custodial credit risk. The City's deposits are covered by insurance provided by the Federal Deposit Insurance Corporation (FDIC) and the National Credit Union Association (NCUA) as well as protection provided by the Washington State Public Deposit Protection Commission (PDPC) as established in RCW 39.58. The PDPC makes and enforces regulations and administers a program to ensure public funds deposited in banks and thrifts are protected if a financial institution becomes insolvent. The PDPC approves which banks, credit unions, and thrifts can hold state and local government deposits and monitors collateral pledged to secure uninsured public deposits. This secures public treasurers' deposits when they exceed the amount insured by the FDIC or NCUA by requiring banks, credit unions, and thrifts to pledge securities as collateral.

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

Credit risk – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Some of the City's Pooled investments have credit risk from holdings in commercial paper, corporate notes, and taxable municipal bonds. The City may not hold more than 50% of the Pool's total assets in these credit sensitive sectors. State statute defines the investments in commercial paper and corporate notes as a "credit portfolio". The credit portfolio may not exceed 25 percent of the Pool's market value. Credit investments must be diversified by sector and industry. No single issuer shall exceed 3 percent of the Pool's market value. Commercial Paper investments may not have maturities exceeding 270 days and must hold the highest short-term credit rating by all the major credit rating agencies that rate the issuer at the time of purchase. Corporate notes must mature within 5.5 years from the time of purchase and must be rated at least weak single-A or better by all the major rating agencies that rate the note at the time of purchase. No single issuer rated AA or better may exceed 3 percent of the Pool's market value. No single issuer rated in the single-A category may exceed 2 percent of the Pool's market value. Municipal bonds must have a credit rating of weak single-A or better by all the major rating agencies that rate the issuer at the time of purchase. No single issuer may exceed 5 percent of the Pool's market value.

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, 2017, these investments were rated Aaa by Moody's Investors Service and AA+ or AA- by Standard & Poor's Rating Service. As of December 31, 2017, these investments were rated Aaa by Moody's Investors Service and AA+ by Standard & Poor's Rating Service.

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.

Investments – The City reports its investments at fair value and categorizes its fair value measurements within the fair value hierarchy established by U.S. GAAP. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction amongst market participants at the measurement date (an exit price). Fair value is a market-based measurement for a particular asset or liability based on assumptions that market participants would use in pricing the asset or liability. Such assumptions include observable and unobservable inputs of market data, as well as assumptions about risk and the risk inherent in the inputs to the valuation technique.

Valuation techniques to determine fair value should be consistent with one or more of three approaches: the market approach, cost approach, and income approach. The City uses a combination of the market and cost approach for the valuation of pooled investments.

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

The City’s overnight repurchase agreement with Wells Fargo Bank, N.A. and investment in the State of Washington Local Government Investment Pool (LGIP) are accounted for at cost. The LGIP is an external investment pool and is measured at a net asset value (NAV) per share of $1. The remainder of the City’s investments are purchased in the over-the-counter U.S. bond market and accounted for at market.

The City uses market pricing for its over-the-counter investments as provided by its contractual custodial agent, Wells Fargo Institutional Retirement & Trust, and its third-party investment accounting vendor FIS AvantGard LLC. Both Wells Fargo and FIS contract with Interactive Data Pricing and Reference Data, Inc. for securities pricing.

As a basis for considering market participant assumptions in fair value measurements, GASB Statement No. 72 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels as follows:

Level 1 – inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Fund can access at the measurement date.

Level 2 – inputs are inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 – inputs are unobservable inputs for the asset or liability. Valuation adjustments such as for nonperformance risk or inactive markets could cause an instrument to be classified as Level 3 that would otherwise be classified as Level 1 or Level 2.

As of December 31, 2017 and 2016, the City’s pooled investments were categorized within the fair value hierarchy as follows:

Investments	Fair Value as of December 31, 2017	Fair Value Measurements Using: Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Weighted Average Maturity (Days)
U.S. Government Agency Securities	$ 693,621,813	$ -	$ 693,621,813	$ -	887
U.S. Treasury and U.S. Government-Backed Securities	475,683,801	463,218,182	12,465,619	-	489
Municipal Bonds	366,132,818	-	366,132,818	-	1,858
Commercial Paper	251,665,039	-	251,665,039	-	32
U.S. Government Agency Mortgage-Backed Securities	243,661,069	-	243,661,069	-	450
Repurchase Agreements	138,385,200	138,385,200	-	-	1
Local Government Investment Pool	120,655,354	-	120,655,354	-	-
Bank Note	47,987,867	-	47,987,867	-	293
	$ 2,337,792,961	$ 601,603,382	$ 1,736,189,579	$ -	
Weighted Average Maturity of the City’s Pooled Investments					936

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

Investments	Fair Value as of December 31, 2016	Fair Value Measurements Using: Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Weighted Average Maturity (Days)
Bank Note	$ 48,132,770	$ -	$ 48,132,770	$ -	658
Commercial Paper	204,474,875	-	204,474,875	-	90
Local Government Investment Pool	45,382,406	-	45,382,406	-	-
Municipal Bonds	306,457,925	-	306,457,925	-	1,692
Repurchase Agreements	50,446,235	50,446,235	-	-	2
U.S. Government Agency Mortgage-Backed Securities	261,378,071	-	-	-	
U.S. Government Agency Securities	553,815,643	-	553,815,643	-	920
U.S. Treasury and U.S. Government-Backed Securities	287,802,378	275,300,476	12,501,902	-	472
	$ 1,757,890,303	$ 325,746,711	$ 1,432,143,592	$ -	

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

	2017	2016
Cash and equity in pooled investments	$ 54,637,435	$ 39,106,002
Restricted cash and equity in pooled investments	163,252,748	72,093,856
Total	$ 217,890,183	$ 111,199,858
Balance as a percentage of City Pool cash and investments	9.3%	6.3%

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.

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

Issuer	2017 Fair Value	2017 Percent of Total Investments	2016 Fair Value	2016 Percent of Total Investments
United States Government	$ 475,683,801	20%	$ 287,802,378	16%
Federal National Mortgage Association	339,104,849	15%	302,419,724	17%
Federal Farm Credit Bank	259,982,939	11%	190,087,160	11%
Federal Home Loan Bank	168,930,820	7%	139,856,360	8%
Wells Fargo	138,385,200	6%	**	**
Local Government Investment Pool	120,655,354	5%	**	**
Federal Home Loan Mortgage Corp	**	**	93,916,723	5%
Freddie Mac Multifamily Securities	**	**	88,913,747	5%

** Investment did not represent 5% or more of investments as of December 31, 2017, or 2016.

Note 3 – Capital Assets

Capital asset activity consisted of the following for the year ended December 31, 2017:

	Beginning Balance	Additions and Transfers In	Retirements and Transfers Out	Ending Balance
Buildings	$ 192,867,352	$ 1,930,582	$ (879,313)	$ 193,918,621
Structures	319,033,737	23,774,429	(350,000)	342,458,166
Machinery and equipment	1,289,006,757	91,335,097	(19,325,489)	1,361,016,365
Computer systems	120,472,487	2,544,083	(11,236,525)	111,780,045
Total capital assets - excluding land	1,921,380,333	119,584,191	(31,791,327)	2,009,173,197
Less accumulated depreciation	(771,218,033)	(47,706,082)	27,414,039	(791,510,076)
	1,150,162,300	71,878,109	(4,377,288)	1,217,663,121
Construction in progress	79,610,858	70,045,277	(112,685,144)	36,970,991
Land and land rights	45,137,867	3,206,657	(25,200)	48,319,324
Other property	1,663,027	-	-	1,663,027
Capital assets, net	$ 1,276,574,052	$ 145,130,043	$ (117,087,632)	$ 1,304,616,463

Capital asset activity consisted of the following for the year ended December 31, 2016:

	Beginning Balance	Additions and Transfers In	Retirements and Transfers Out	Ending Balance
Buildings	$ 192,068,170	$ 799,182	$ -	$ 192,867,352
Structures	312,491,380	6,542,357	-	319,033,737
Machinery and equipment	1,235,836,353	57,369,236	(4,198,832)	1,289,006,757
Computer systems	104,130,938	16,341,549	-	120,472,487
Total capital assets - excluding land	1,844,526,841	81,052,324	(4,198,832)	1,921,380,333
Less accumulated depreciation	(724,570,208)	(49,056,230)	2,408,404	(771,218,033)
	1,119,956,633	31,996,094	(1,790,428)	1,150,162,300
Construction in progress	75,006,536	73,704,215	(69,099,893)	79,610,858
Land and land rights	44,453,438	684,429	-	45,137,867
Other property	1,593,974	69,053	-	1,663,027
Capital assets, net	$ 1,241,010,581	$ 106,453,791	$ (70,890,321)	$ 1,276,574,052

During 2017 and 2016, the Fund capitalized interest costs relating to construction of $2,082,637 and $3,195,590, 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 set aside $20,753,817 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, 2017, and 2016, were $858,215,000 and $809,950,000, respectively.

Note 4 – Revenue Bonds (continued)

Revenue bonds outstanding as of December 31, 2017 and 2016, consisted of the following Municipal Water bonds:

Name of Issue	Issuance Date	Maturity Years	Interest Rates	Original Issue Amount	Bonds Outstanding 2017	Bonds Outstanding 2016
2006 parity, refunding bonds	10/23/06	2008-2037	4.0-5.0%	$ 189,970,000	$ -	$ 112,990,000
2008 parity, refunding bonds	12/15/08	2009-2038	4.0-5.25%	205,080,000	6,670,000	13,010,000
2010A parity, revenue bonds	1/21/10	2019-2040	4.67-5.89%	109,080,000	109,080,000	109,080,000
2010B parity, refunding revenue bonds	1/21/10	2010-2027	3.0-5.0%	81,760,000	40,885,000	46,855,000
2012 parity, refunding bonds	5/30/12	2012-2034	2.0-5.0%	238,770,000	192,560,000	204,405,000
2015 parity, refunding bonds	6/10/15	2015-2045	2.0-5.0%	340,840,000	314,335,000	323,610,000
2017 parity, refunding bonds	1/25/17	2017-2046	4.0-5.0%	194,685,000	194,685,000	-
				$ 1,360,185,000	$ 858,215,000	$ 809,950,000

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

Years Ending December 31,	Principal	Interest	Total
2018	$ 41,020,000	$ 40,272,656	$ 81,292,656
2019	43,080,000	38,260,356	81,340,356
2020	45,625,000	36,100,194	81,725,194
2021	46,235,000	33,891,504	80,126,504
2022	48,725,000	31,594,414	80,319,414
2023 - 2027	231,010,000	121,865,031	352,875,031
2028 - 2032	186,220,000	70,789,618	257,009,618
2033 - 2037	125,615,000	35,509,946	161,124,946
2038 - 2042	60,900,000	12,513,634	73,413,634
2043 - 2047	29,785,000	2,704,400	32,489,400
	$ 858,215,000	$ 423,501,753	$ 1,281,716,753

Note 4 – Revenue Bonds (continued)

The following table shows the revenue bond activity during the year ended December 31, 2017:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable					
Revenue bonds	$ 809,950,000	$ 194,685,000	$ (146,420,000)	$ 858,215,000	$ 41,020,000
Add (deduct) deferred amounts					
Issuance premiums	85,803,050	21,591,640	(8,906,595)	98,488,095	-
Total bonds payable	$ 895,753,050	$ 216,276,640	$ (155,326,595)	$ 956,703,095	$ 41,020,000

The following table shows the revenue bond activity during the year ended December 31, 2016:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable					
Revenue bonds	$ 851,565,000	$ -	$ (41,615,000)	$ 809,950,000	$ 39,345,000
Add (deduct) deferred amounts					
Issuance premiums	89,961,354	-	(4,158,304)	85,803,050	-
Total bonds payable	$ 941,526,354	$ -	$ (45,773,304)	$ 895,753,050	$ 39,345,000

In January 2017, the Fund issued $194,685,000 of Water System Improvement and Refunding Revenue Bonds with varying annual principal payments due beginning 2018 and ending in 2046, at interest rates ranging from 4.0% to 5.0%. A portion of the proceeds were used to fully refund the 2006 bonds.

As a result of the refunding, the fund reduced total debt service requirements by $20.1 million resulting in an economic gain (difference between the present value of the debt service payments on the old and new bonds) of $16.4 million.

Defeasance of debt – The Fund defeased 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. Thus, the old bonds are considered defeased, and the corresponding liabilities and trust account assets are not included in the Statement of Net Position. In 2017, $107,075,000 bonds were defeased and $146,130,000 bonds were redeemed. The remaining balance of $149,770,000 is outstanding as of December 31, 2017:

	Amount Outstanding at December 31, 2016	Additions	Redemptions	Amount Outstanding at December 31, 2017
2006 Parity	$ 39,055,000	$ 107,075,000	$ (146,130,000)	$ -
2008 Parity	149,770,000	-	-	149,770,000
	$ 188,825,000	$ 107,075,000	$ (146,130,000)	$ 149,770,000

Note 4 – Revenue Bonds (continued)

In 2016, there were no bond defeasances or redemptions. There was an outstanding balance of defeased bonds of $188,825,000 as of December 31, 2016.

	Amount Outstanding at December 31, 2015	Additions	Redemptions	Amount Outstanding at December 31, 2016
Bonds issued				
2006 Parity	$ 39,055,000	$ -	$ -	$ 39,055,000
2008 Parity	149,770,000	-	-	149,770,000
	$ 188,825,000	$ -	$ -	$ 188,825,000

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 at least equal to 125% of average annual debt service. For 2017, net revenue available for debt service, as defined by the bond covenants, was 194% of annual debt service. As of December 31, 2017, management believes the Fund was in compliance with all debt covenants. For more information, see Other Information (page 45).

Note 5 – Leases

The Fund has noncancelable operating lease commitments for real and personal property with minimum payments of $130,264 in 2017 and $330,198 in 2016. Rents are paid as they become due and payable. Minimum payments under the leases for the years ending December 31, are shown below:

	Minimum Payments
2018	$ 128,541
2019	128,963
2020	40,817
2021	12,107
2022	12,107
2023 - 2027	60,533
2028 - 2029	24,214
	$ 407,282

Note 6 – Postemployment Benefit Plans

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

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

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

Other postemployment benefits – 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 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 $2.3 and $2.0 million in 2017 and 2016, respectively.

Note 6 – Postemployment Benefit Plans (continued)

The table below summarizes the City's annual cost, expected contributions to the plan, and changes in the net OPEB obligation for fiscal years ended December 31, 2017, 2016, and 2015. These calculations are based on the most recent actuarial valuation data available, dated January 1, 2017. The Fund has accrued $2,824,163 to the plan as of December 31, 2017, as a reasonable estimate of expected contributions.

	2017	2016	2015
Annual required contribution	$ 8,090,000	$ 7,733,000	$ 4,605,000
Interest on net OPEB obligation	1,671,000	1,526,000	1,630,000
Adjustment to annual required contribution	(2,791,000)	(2,549,000)	(2,540,000)
Annual OPEB cost (expense)	6,970,000	6,710,000	3,695,000
Contribution (employer-paid benefits)	(2,289,000)	(2,018,000)	(1,141,000)
Increase in net OPEB obligation	4,681,000	4,692,000	2,554,000
Net OPEB obligation, beginning of year	54,074,000	49,382,000	46,828,000
Net OPEB obligation, end of year	$ 58,755,000	$ 54,074,000	$ 49,382,000
Fund's allocated share of city liability	$ 2,824,163	$ 2,718,526	$ 2,703,122

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.

Note 6 – Postemployment Benefit Plans (continued)

Significant methods and assumptions are as follows:

Actuarial data and assumptions	
Valuation date	January 1, 2017
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	30 years, open
Discount rate	3.09%
Health care cost trend rates - medical	Medical 6.25%, decreasing by 0.25% & 0.21% for two years; 5.79% in year 2018 and decreasing to 5.57% in 2019. Vendor Rx Report: 10.0% in 2016, decreasing by 0.5%, 0.71%, & 0.72% respectively 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, the other 50% will continue coverage under the same plan.

Note 6 – 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, 2015	$ -	$ 44.4	$ 44.4	0.0%	$ 1,037.9	4.3%
January 1, 2016	$ -	$ 65.7	$ 65.7	0.0%	$ 1,125.7	5.8%
January 1, 2017	$ -	$ 70.1	$ 70.1	0.0%	$ 1,153.8	6.1%

The Health Care Sub-fund 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 2017 and 2016, 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, 1.565% and 1.403%, respectively. Claims expected to be paid within one year are $2,028,452 and $2,151,385 at December 31, 2017 and 2016, respectively. The table below presents the changes in the liability for workers' compensation claims and other claims (risk-financing liabilities) as of December 31:

	2017	2016
Beginning liability, discounted	$ 5,640,037	$ 4,848,279
Payments	(1,041,970)	(632,665)
Incurred claims and changes in estimate	2,681,659	1,424,423
Ending liability, discounted	$ 7,279,726	$ 5,640,037

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

Note 8 – Compensated Absences

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

	2017	2016
Beginning liability	$ 4,745,112	$ 5,298,051
Additions	4,418,259	3,650,572
Reductions	(4,333,896)	(4,203,511)
Ending liability	$ 4,829,475	$ 4,745,112

Note 9 – Pension Benefit Plan

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

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

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

Member and employer contributions – Employees are required to contribute 10.03% of their annual base salaries to the System. The employer's contribution rate for the years ended December 31, 2017 and 2016, was 15.3% and 15.1%, respectively. Employer rates are established by the City Council on a biannual basis. The Fund's contributions to the System for the years ended December 31, 2017 and 2016, were $6,942,219 and $6,870,976, respectively.

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

Note 9 – Pension Benefit Plan (continued)

Pension liabilities, pension expense, and deferred outflows of resources and deferred inflows related to pensions – At December 31, 2017 and 2016, the Fund reported a liability of $86,689,301 and $93,080,303, respectively, its proportionate share of the Systems' net pension liability. The net pension liability was measured as of December 31, 2016 and 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of the date. The Fund's proportion of the net pension liability was based on a projection of the City's long-term share of contributions to the pension plan relative to the projected contributions of all participating parties, actuarially determined. At December 31, 2017 and 2016, the Fund's proportion was 6.35% and 7.16%, respectively.

For the year ended December 31, 2017 and 2016, the Fund recognized pension expense of approximately $11,216,000 and $11,900,000, respectively.

The Fund's deferred outflows and inflows of resources are as follows at December 31, 2017:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ 80,189	$ 397,935
Net difference between projected and actual earnings	7,028,841	-
Contributions made subsequent to measurement date	6,942,219	-
Changes in proportion and differences between employer contributions and proportionate share of contributions	-	6,599,815
Total	$ 14,051,249	$ 6,997,750

The Fund's deferred outflows and inflows of resources are as follows at December 31, 2016:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ 111,502	$ -
Net difference between projected and actual earnings	11,385,907	-
Contributions made subsequent to measurement date	6,870,976	-
Changes in proportion and differences between employer contributions and proportionate share of contributions	-	2,225,903
Total	$ 18,368,385	$ 2,225,903

Note 9 – Pension Benefit Plan (continued)

Amounts currently reported as deferred outflows of resources relate to actual experience and difference in actual earnings on pension investments from projected earnings and will be recognized in pension expense as follows for years ending December 31:

2018	$	804,641
2019		804,641
2020		259,089
2021		(1,619,769)
2022		(585,318)

Actuarial assumptions – The total pension liability as of December 31, 2017 was determined using the following actuarial assumptions:

Valuation date	January 1, 2016
Measurement date	December 31, 2016
Actuarial cost method	Individual Entry Age Normal
Amortization method	Level Percent, Closed
Remaining amortization period	30 years as of January 1, 2013 valuation
Asset valuation method	5-Year Smoothing Method
Inflation	3.25%
Investment rate of return	7.5% compounded annually, net of expenses
Discount rate	7.5%
Projected general wage inflation	4.0%
Postretirement benefit increases	1.5%
Mortality	Various rates based on RP-2000 mortality tables and using generational projection of improvement using Projection Scale AA.

The actuarial assumptions that determined the total pension liability as of the measurement date were based on the results of an actuarial experience study for the period January 1, 2010 through December 31, 2013.

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

Note 9 – Pension Benefit Plan (continued)

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

Best estimates of geometric real rates of return for each major asset class included in the System's target asset allocation as of December 31, 2016, are summarized in the following table:

Asset Class	Long-Term Expected Real Rate of Return
Equity: Public	4.99%
Equity: Private	6.25%
Fixed Income: Broad	0.62%
Fixed Income: Credit	3.79%
Real Assets: Real Estate	3.25%
Real Assets: Infrastructure	2.75%
Diversifying Strategies	3.25%

Sensitivity analysis – The following presents the Fund's proportionate share of the net pension liability calculated using the discounted rate of 7.5%, as well as what the employer's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (6.50%) or 1 percentage point higher (8.50%) than the current rate.

1% Decrease 6.50%	Current Discount Rate 7.50%	1% Increase 8.50%
$ 117,321,101	$ 86,689,301	$ 60,932,560

Note 10 – Loans

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

Loans outstanding as of December 31, 2017, and 2016, are as follows:

Description	Maturity Years	Interest Rate	Loan Amount	Loans Outstanding 2017	Loans Outstanding 2016
Myrtle Reservoir	2008-2025	1.5%	$ 4,040,000	$ 1,795,556	$ 2,020,000
Beacon Reservoir	2008-2026	1.5%	4,040,000	1,913,684	2,126,316
West Seattle Reservoir	2009-2027	1.5%	3,030,000	1,594,737	1,754,210
Maple Leaf	2011-2029	1.5%	3,030,000	1,936,198	2,097,548
Maple Leaf ARRA	2013-2031	1.0%	7,341,758	5,506,318	5,873,406
Morse Lake Pump Plant #1	2014-2037	1.5%	12,120,000	12,120,000	10,908,000
Morse Lake Pump Plant #2	2017-2036	1.5%	6,060,000	6,060,000	-
			$ 39,661,758	$ 30,926,493	$ 24,779,480

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

Years Ending December 31,	Principal	Interest	Total
2018	$ 2,049,935	$ 774,443	$ 2,824,378
2019	2,049,935	407,452	2,457,387
2020	2,049,935	378,539	2,428,473
2021	2,049,935	349,625	2,399,560
2022	2,049,935	320,712	2,370,646
2023 - 2027	9,588,154	1,173,220	10,761,374
2028 - 2032	6,782,876	593,371	7,376,247
2033 - 2037	4,305,789	184,192	4,489,982
	$ 30,926,493	$ 4,181,554	$ 35,108,047

Note 10 – Loans (continued)

The table below summarizes the activity for the loans for the years ended December 31:

	2017	2016
Net loans, beginning of year	$ 24,779,480	$ 22,342,079
Loan proceeds	7,272,000	3,562,390
Principal payments	(1,124,987)	(1,124,989)
Net loans, end of year	$ 30,926,493	$ 24,779,480
Loans due within one year	$ 2,049,935	$ 1,124,987
Loans, noncurrent	$ 28,876,558	$ 23,654,493

In 2014 and 2016, the Fund received approval for a loan of $12.1 million and $6.1 million, respectively, from the State of Washington for the Morse Lake Pump Plant Project. Accordingly, the Fund invoices the State for expenditures incurred related to the project and receives reimbursement. As of December 31, 2017, the Fund has withdrawn a total of $18.2 million.

Note 11 – Notes and Contracts Receivable

The Fund had 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, 2017, the Seattle Housing Authority has fully paid its outstanding balance.

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

	2017	2016
Seattle Housing Authority receivable	$ -	$ 394,570
Due within one year	-	(19,850)
Total noncurrent notes and contracts receivable	$ -	$ 374,720

Note 12 – Commitments

The Fund is required by the Washington State Department of Health (DOH) to complete a program to cover its open, above-ground distribution system reservoirs by the year 2020. The total cost of burying six reservoirs is expected to be approximately $207.2 million through the year 2022; costs beyond 2022 are not estimable as of the date of this report. As of December 31, 2017, and 2016, total cumulative costs incurred were $166.8 million and $157.9 million, respectively.

The City has wholesale contracts with Cascade Water Alliance (CWA) and twenty individual water districts and municipalities. Seventeen wholesale customers have full and partial requirements contracts which obligate the City to meet the wholesale customers' demand that is not already met by their independent sources of supply. Two wholesale customers (including CWA) have block contracts which obligate the City to provide water up to a combined maximum of 41.85 MGD per year. Two other wholesale customers have emergency intertie agreements and do not purchase water from Seattle on a regular basis. CWA contract expires in 2063 while other wholesale contracts expire in 2062.

The City also has a contract with the City of North Bend to provide untreated water supply up to an average annual amount of 1.1 MGD through 2066 for use in supplementing stream flows.

Note 13 – Habitat Conservation Program Liability

SPU has prepared a comprehensive environmental management plan for its Cedar River Watershed. The purpose of the Habitat Conservation Plan (HCP) is to protect all species of concern that may be affected by the operations of SPU and SCL in the Cedar River Watershed, while allowing the City to continue to provide high quality drinking water to the region. The federal government has accepted the HCP. The total cost of implementing the HCP is expected to be $110.4 million (in 2017 dollars) over a period of 50 years (from the year 2000 through the year 2050).

Expenditures are being funded from a combination of the Fund's operating revenues and issuance of revenue bonds. The total amount expended for the HCP through 2017 is $91.0 million. The remaining $19.4 million to complete the HCP is comprised of an $5.5 million liability and an estimate of $13.92 million for construction and operating commitments. The construction activities will add to the Fund's capital assets and the operating activities are mainly research, monitoring, and maintenance of the HCP Program that will be expensed as incurred.

Required Supplementary Information

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

	2017	2016	2015
Employer's proportion of the net pension liability	15.13%	16.37%	16.96%
Employer's proportionate share of the net pension liability	$ 197,454,529	$ 212,671,200	$ 187,919,945
Employer's covered payroll	$ 106,696,535	$ 105,031,141	$ 102,783,473
Employer's proportionate share of the net pension liability as a percentage of its covered payroll	185.06%	202.48%	182.83%
Plan fiduciary net position as a percentage of the total pension liability	65.60%	64.03%	67.70%

Schedule of Seattle Public Utilities' Contributions

	2017	2016	2015
Contractually required employer contribution	$ 16,354,089	$ 16,487,154	$ 15,170,276
Contributions in relation to the contractually required employer contribution	(16,354,089)	(16,487,154)	(15,170,276)
Employer contribution deficiency (excess)	$ -	$ -	$ -
Employer's covered payroll	$ 106,696,535	$ 105,031,141	$ 102,783,473
Employer contributions as a percental of covered payroll	15.33%	15.70%	14.76%

Other Information (Unaudited)

Water Fund Debt Service Calculation 2017

Operating Revenues	
Residential/Commercial Services	$ 195,290,908
Wholesale Services	56,209,777
Other	16,595,769
Rate Stabilization Fund	(5,200,000)
Total Operating Revenue	262,896,454
Operating Expense	
Other Operations & Maintenance	107,211,916
City Taxes	32,924,420
Other Taxes	10,746,447
Total Operating Expenses	150,882,783
Net Operating Income	112,013,671
Adjustments	
Add: Capital Contributions Connection Charge	2,735,396
Add: City Taxes	32,924,420
Add: Investment Interest	2,534,520
Less: DSRF Earnings	(342,587)
Add: BAB's Subsidy	1,966,109
Add (Less): Net Other Nonoperating Revenues/(Expenses)	1,319,162
Add: Proceeds from Sale of Assets	1,411,928
Total Adjustments	42,548,948
Net Revenue Available for Debt Service	$ 154,562,619
w/o Credit for City Taxes	$ 121,638,199
Annual Debt Service	
Annual Debt Service	$ 79,824,263
Less: DSRF Earnings	(342,587)
Adjusted Annual Debt Service	$ 79,481,676
Coverage	1.94
Coverage without taxes	1.53

Water System Operating Statistics

	2013	2014	2015	2016	2017
Population Served					
Retail	678,000	682,000	720,200	743,800	770,800
Wholesale[1]	648,000	654,000	683,400	689,400	707,200
Total Population Served	1,326,000	1,336,000	1,403,600	1,433,200	1,478,000
Water Sales Revenues ($000)[2][3]					
Retail	$ 168,126	$ 179,775	$ 187,114	$ 184,888	$ 195,291
Wholesale	56,026	53,647	52,797	53,060	56,210
Total Water Sales Revenues	$ 224,152	$ 233,422	$ 239,911	$ 237,948	$ 251,501
Billed Water Consumption (MG)[3]					
Retail	19,769	19,575	20,309	19,856	20,312
Wholesale	21,405	21,986	23,106	22,282	22,905
Total Billed Water Use	41,174	41,561	43,415	42,138	43,217
Operating Costs ($ per MG)	$ 4,248	$ 4,438	$ 4,414	$ 4,548	$ 4,675
Gallons Used per Day per Capita	85	85	85	81	80
Retail Meters in Use	190,289	191,403	192,633	194,580	195,331
Number of New Retail Meters	1,085	1,114	1,230	1,947	751
Total Water Diversions (MGD)	120.9	121.5	125.6	121.7	124
Non-Revenue	8.1	7.6	6.7	6.3	5.6
% Non-Revenue	6.7	6.3	5.3	5.1	4.5

(1) This is the estimated total population served by SPU’s water supply

(2) Revenues represent payments from customers for service provided at published rates in each year. Revenues shown are not net of transfers to the Rate Stabilization Account or other credits or deferrals of income.

(3) Per capita billed water consumption has been generally decreasing for the past 25 years. Variations in billed water use are primarily associated with year-to-year variations in temperatures and precipitation in the summer irrigation period. There has been no change in the geographic area served nor any appreciable change in the number or composition of retail customers.

Major Retail Water Customers – 2017 Annual Revenues and Volumes

The City of Seattle, University of Washington, Port of Seattle, Seattle Housing Authority, King County, Marriott International, Equity Residential Properties, Seattle Public Schools, Essex, and Nucor Steel. In aggregate, charges to these customers represented roughly 11% of total billed direct service revenue for the year.

Water Rates – Effective January 1, 2018

Effective January 1, 2018

	(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)	(k)	(l)	(m)	(n)
		Direct Service												
	RATE SCHEDULES	Inside City				Outside City				City of Shoreline / City of Lake Forest Park				
		Residential	MMRD*	Gen Svc	Fire Service	Residential	MMRD*	Gen Svc	Fire Service	Residential	MMRD*	Gen Svc	Fire Service	MMRD* w/PUT
1	Commodity Charge ($/100 Cubic Feet)													
2														
3	Offpeak Usage (Sept 16-May 15)	$5.20	$5.20	$5.20		$5.93	$5.93	$5.93		$6.31	$6.31	$6.31		$5.91
4	Peak Usage (May 16-Sept 15)													
5	Up to 5 ccf**	$5.33	$5.33	$6.59		$6.08	$6.08	$7.51		$6.46	$6.46	$7.99		$6.05
6	Next 13 ccf**	$6.59	$6.59	$6.59		$7.51	$7.51	$7.51		$7.99	$7.99	$7.99		$7.48
7	Over 18 ccf**	$11.80	$11.80	$6.59		$13.45	$13.45	$7.51		$14.31	$14.31	$7.99		$13.39
8														
9	Usage over base allowance				$20.00				$22.80				$24.30	
10														
11	Utility Credit ($/month)	$21.15		$12.38		$21.15		$12.38		$21.15		$12.38		
12														
13														
14	Base Service Charge ($/month/meter)													
15														
16	3/4 inch and less	$16.10		$16.10		$18.35		$18.35		$19.55		$19.55		
17	1 inch	$16.60		$16.60		$18.90		$18.90		$20.15		$20.15		
18	1-1/2 inch	$25.60	$25.60	$25.60		$29.20	$29.20	$29.20		$31.05	$31.05	$31.05		$29.05
19	2 inch	$28.35	$28.35	$28.35	$16.25	$32.30	$32.30	$32.30	$19.00	$34.40	$34.40	$34.40	$20.00	$32.20
20	3 inch	$104.95	$104.95	$104.95	$21.00	$119.65	$119.65	$119.65	$24.00	$127.30	$127.30	$127.30	$25.00	$119.15
21	4 inch	$150.40	$150.40	$150.40	$39.00	$171.45	$171.45	$171.45	$44.00	$182.40	$182.40	$182.40	$47.00	$170.70
22	6 inch		$185.05	$185.05	$66.00		$210.95	$210.95	$75.00		$224.40	$224.40	$80.00	$210.00
23	8 inch		$218.00	$218.00	$105.00		$249.00	$249.00	$120.00		$264.00	$264.00	$127.00	$247.00
24	10 inch		$297.00	$297.00	$152.00		$339.00	$339.00	$173.00		$360.00	$360.00	$184.00	$337.00
25	12 inch		$402.00	$402.00	$222.00		$458.00	$458.00	$253.00		$488.00	$488.00	$269.00	$457.00
26	16 inch		$477.00	$477.00			$544.00	$544.00			$579.00	$579.00		$542.00
27	20 inch		$614.00	$614.00			$700.00	$700.00			$745.00	$745.00		$697.00
28	24 inch		$771.00	$771.00			$879.00	$879.00			$935.00	$935.00		$875.00

* Master Metered Residential Development
** per residence

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