



WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Basic Financial Statements and Other Information

June 30, 2016

(With Independent Auditors' Report Thereon)

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Table of Contents

	Page
Independent Auditors' Report	1
Management's Discussion and Analysis – Unaudited	3
Basic Financial Statements:	
Balance Sheet	13
Statement of Revenues, Expenses, and Changes in Fund Net Position	14
Statement of Cash Flows	15
Notes to Basic Financial Statements	16
Other Information – Unaudited	
Schedule 1 – Detailed Schedule of Certain Operating Expenses	35
Schedule 2 – Schedule of Costs for Howard Bend Water Sales	36



KPMG LLP
Suite 900
10 South Broadway
St. Louis, MO 63102-1761

Independent Auditors' Report

The Honorable Mayor and
Board of Aldermen
City of St. Louis, Missouri:

Report on the Financial Statements

We have audited the accompanying financial statements of the Water Division of the City of St. Louis, Missouri, an enterprise fund of the City of St. Louis, Missouri, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Water Division of the City of St. Louis, Missouri's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Water Division of the City of St. Louis, Missouri, as of June 30, 2016, and the changes in its financial position and its cash flows thereof for the year then ended in accordance with U.S. generally accepted accounting principles.



Emphasis of Matters

As discussed in note 1, the basic financial statements of the Water Division of the City of St. Louis, Missouri present only the financial position and the changes in financial position, and cash flows of the Water Division of the City of St. Louis, Missouri, an enterprise fund of the City of St. Louis, Missouri, and do not purport to, and do not, present fairly the financial position of the City of St. Louis, Missouri as of June 30, 2016, the changes in its financial position, or, where applicable, its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles. Our opinion is not modified with respect to this matter.

As discussed in note 1(n), effective July 1, 2015, the Water Division of the City of St. Louis, Missouri implemented Governmental Accounting Standards Board (GASB) No. 72, *Fair Value Measurement and Application*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the information in the Management's Discussion and Analysis on pages 3 through 12 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Water Division of the City of St. Louis, Missouri's basic financial statements. The other information included in Schedules 1 and 2 are presented for purposes of additional analysis and are not a required part of the basic financial statements. The other information in Schedules 1 and 2 has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on them.

KPMG LLP

St. Louis, Missouri
December 9, 2016

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Management's Discussion and Analysis – Unaudited

June 30, 2016

(Dollars in thousands)

This section presents Management's Discussion and Analysis (MD&A) of the financial condition and activities of the Water Division of the City of St. Louis, Missouri (Water Division) for the City of St. Louis, Missouri (the City) as of and for the fiscal year ended June 30, 2016. This information should be read in conjunction with the financial statements that follow this section. All dollar amounts are in thousands.

Overview and Financial Highlights

The Water Division is an enterprise fund of the City. As such, its revenues are dedicated to the completion of its mission to provide the finest quality water and customer service at reasonable prices to the residents, businesses, and industry within the City, as well as to its wholesale customers.

The retail water billing system is split between flat rate and metered customers. Most residential customers (79,308) are billed quarterly on a flat rate basis. This flat rate system comprises charges for water-using devices such as toilets, bathtubs, showers, the number of rooms in the building, and a charge for outside water use. All businesses, industries, and some residential customers are charged on the metered rate structure. This is a declining block rate structure composed of a quantity charge and a readiness-to-serve charge that is tied to the meter size. Metered users (12,821) are read and billed quarterly.

At fiscal year-end, the Water Division supplied wholesale water to other water districts/political subdivisions through four separate contracts: one in St. Louis county and three in St. Charles county.

- The Water Division pumped 47.6 billion gallons of treated water in fiscal year 2016. This represents a 9.2% increase from fiscal year 2015.
- Metered revenue increased by \$411 or 2% during fiscal year 2016.
- The number of flat rate customers in fiscal year 2016 increased by 146, or 0.18%, however, flat rate revenue decreased by \$185 or 1%.
- Wholesale water revenue increased by \$2,173, or 64%, during fiscal year 2016.
- Other revenue increased by \$297, or 10%, during fiscal year 2016.
- Operating expenses increased by \$3,098, or 7%, during fiscal year 2016.
- Operating income decreased by \$402, or 5%, during fiscal year 2016.
- The overall change in net position for fiscal year 2016 was \$4,639 a decrease of \$231, or 5%, compared to fiscal year 2015.

Overview of the Financial Statements

The MD&A section of this audit report is an overview of the basic financial statements presented herein. Supplementary or reformatted information is presented to better describe the financial condition and performance of the water system. The Water Division's financial statements are prepared on an accrual basis in accordance with U.S. generally accepted accounting principles set forth by the Governmental Accounting Standards Board (GASB). The Water Division is an enterprise fund of the City. As such, the Water Division relies entirely on the funds it generates and which are dedicated to its operation.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Management's Discussion and Analysis – Unaudited

June 30, 2016

(Dollars in thousands)

Revenues are recognized when earned and expenses are recognized when incurred. Capitalized assets (excluding land) are depreciated over their useful lives. Through the City, the Water Division has authority to issue revenue bonds, secured by the revenues of the water system.

The basic financial statements include a balance sheet; a statement of revenues, expenses, and changes in fund net position; a statement of cash flows and notes to the basic financial statements. The balance sheet provides information regarding the type and amount of resources and obligations at year-end. The statement of revenues, expenses, and changes in fund net position reflects the results of operation of the water system during the year, as well as how net position changed over the year. The statement of cash flows presents changes in cash and cash equivalents that resulted from operating, financing, or investing activities.

The notes to the basic financial statements contain important information including required disclosures and other information essential for a complete understanding of the financial data presented in the various statements.

Net Position

This table is a summary of the Water Division's net positions as of June 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>	<u>Dollar change</u>	<u>Percentage change</u>
Assets:				
Other assets	\$ 57,917	54,398	3,519	6%
Capital assets	155,548	150,081	5,467	4
Deferred outflow of resources	<u>5,293</u>	<u>1,545</u>	<u>3,748</u>	<u>243</u>
Total assets and deferred outflow of resources	<u>\$ 218,758</u>	<u>206,024</u>	<u>12,734</u>	<u>6%</u>
Liabilities:				
Long-term liabilities	\$ 24,813	17,939	6,874	38
Other liabilities	15,407	13,869	1,538	11
Deferred inflow of resources	<u>449</u>	<u>766</u>	<u>(317)</u>	<u>(41)</u>
Total liabilities and deferred inflow of resources	<u>\$ 40,669</u>	<u>32,574</u>	<u>8,095</u>	<u>25%</u>
Net position:				
Net investment in capital assets	\$ 150,430	147,793	2,637	2
Restricted for debt service	979	966	13	1
Unrestricted	<u>26,680</u>	<u>24,691</u>	<u>1,989</u>	<u>8</u>
Total net position	<u>\$ 178,089</u>	<u>173,450</u>	<u>4,639</u>	<u>3%</u>

Other assets increased by \$3,519, or 6%, while capital assets increased by \$5,467, or 4%, due to an increase in spending of ordinance funds and capital projects for system improvements.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Management's Discussion and Analysis – Unaudited

June 30, 2016

(Dollars in thousands)

The increase in long-term liabilities of \$6,874, or 38%, is primarily due to increase in net pension liability of 4,266, or 47%. This resulted in a net pension liability of \$13,273. Deferred outflow of resources increased by \$3,748, or 243%, while deferred inflow of resources decreased by \$317, or 41%.

The preceding table shows that 84.5% of Water Division net position in fiscal year 2016 are invested in capital assets such as land, buildings, reservoirs, basins, transmission and distribution mains, and equipment, less the related debt outstanding used to acquire those capital assets. These capital assets are used to provide water service to all customers of the Water Division. These capital assets were either cash financed, contributed capital, or acquired through the issuance of revenue bonds.

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

The Water Division's revenues, expenses, and changes in fund net position for the fiscal years ended June 30, 2016 and 2015 are summarized as follows:

	<u>2016</u>	<u>2015</u>	<u>Dollar change</u>	<u>Percentage change</u>
Operating revenues	\$ 56,538	53,842	2,696	5%
Operating expenses	(49,494)	(46,396)	(3,098)	(7)
Operating income	7,044	7,446	(402)	(5)
Nonoperating revenues, net	871	196	675	344
Income before capital contributions and transfers	7,915	7,642	273	4
Capital contributions	—	343	(343)	(100)
Transfers out	(3,276)	(3,115)	(161)	(5)
Increase in net position	4,639	4,870	(231)	(5)
Net position, beginning of year	173,450	176,283	(2,833)	(2)
Cumulative effect of change in accounting principle	—	(7,703)	7,703	(100)
Net position, beginning of year, as adjusted	173,450	168,580	4,870	3
Net position, end of year	\$ 178,089	173,450	4,639	3%

The Water Division's net position increased by \$4,639.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

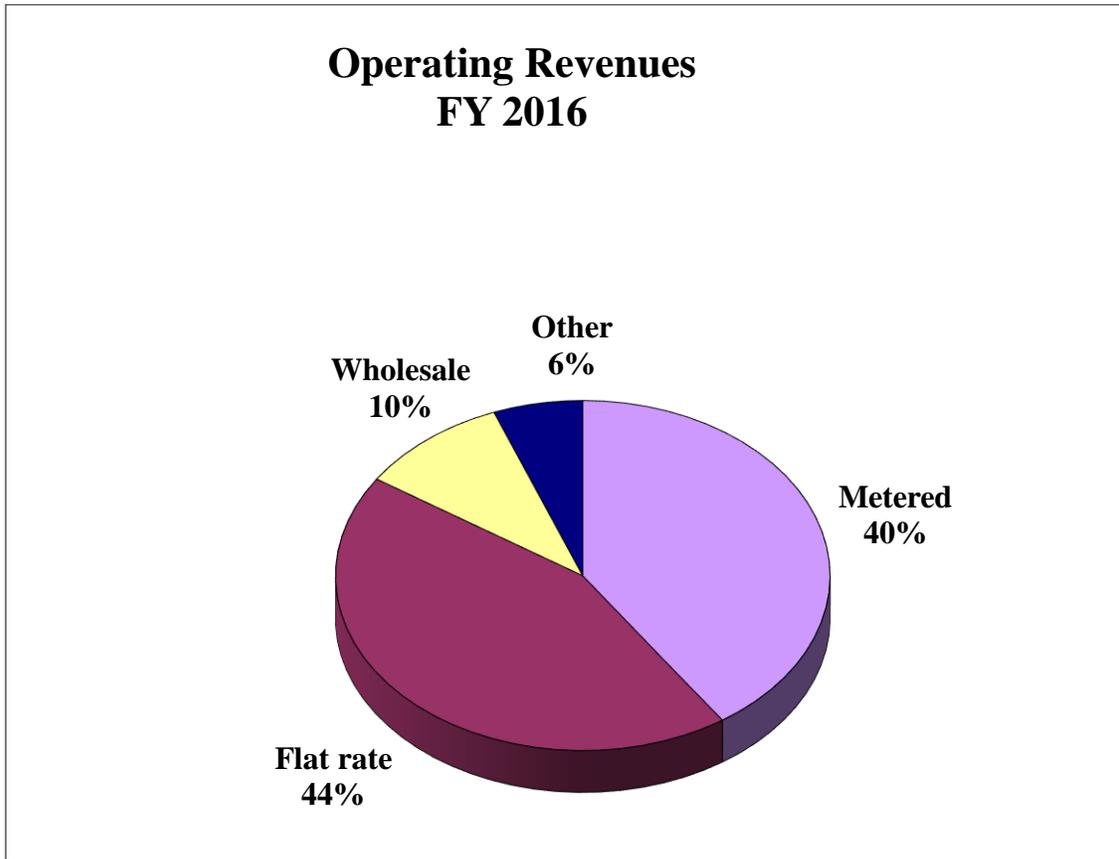
Management's Discussion and Analysis – Unaudited

June 30, 2016

(Dollars in thousands)

Revenues

The chart below depicts the four sources of operating revenue for the Water Division for fiscal year 2016 and each source's percentage contribution to total operating revenues:



WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
 (An Enterprise Fund of the City of St. Louis, Missouri)

Management's Discussion and Analysis – Unaudited

June 30, 2016

(Dollars in thousands)

The table below summarizes the sources of total revenues (operating and nonoperating) for the Water Division for fiscal years 2016 and 2015. This comparison details the change in dollars and percent between the two fiscal years by component revenue source.

	<u>2016</u>	<u>2015</u>	<u>Dollar change</u>	<u>Percentage change</u>
Operating revenues:				
Metered	\$ 22,687	22,276	411	2%
Flat rate	24,974	25,159	(185)	(1)
Wholesale	5,568	3,395	2,173	64
Other	<u>3,309</u>	<u>3,012</u>	<u>297</u>	<u>10</u>
Total operating revenues	<u>56,538</u>	<u>53,842</u>	<u>2,696</u>	<u>5</u>
Nonoperating revenues:				
Investment earnings	147	42	105	250
Miscellaneous, net	<u>956</u>	<u>557</u>	<u>399</u>	<u>72</u>
Total nonoperating revenues	<u>1,103</u>	<u>599</u>	<u>504</u>	<u>84</u>
Total revenues	\$ <u>57,641</u>	<u>54,441</u>	<u>3,200</u>	<u>6%</u>
Capital contributions	\$ —	343	(343)	(100)%

Metered water revenues increased by \$411, or 2%, while flat rate revenue decreased by \$185, or 1%. Metered customers increased by 12 accounts, or 0.09%. The decrease in flat rate revenue is mostly the result of canceled bills on vacant properties. During fiscal year 2016, more concerted efforts of home inspections were performed by Customer Service meter employees.

Wholesale revenue increased by \$2,173, or 64%. Other revenues increased by \$297, or 10%, compared to fiscal year 2015 as completed reimbursable projects increased in fiscal year 2016.

Investment earnings increased by \$105, or 250%, as investments were held all throughout fiscal year 2016 compared to fiscal year 2015.

Miscellaneous revenues, (net) increased by \$504, or 84%, due to increase in revenues on delinquent bills.

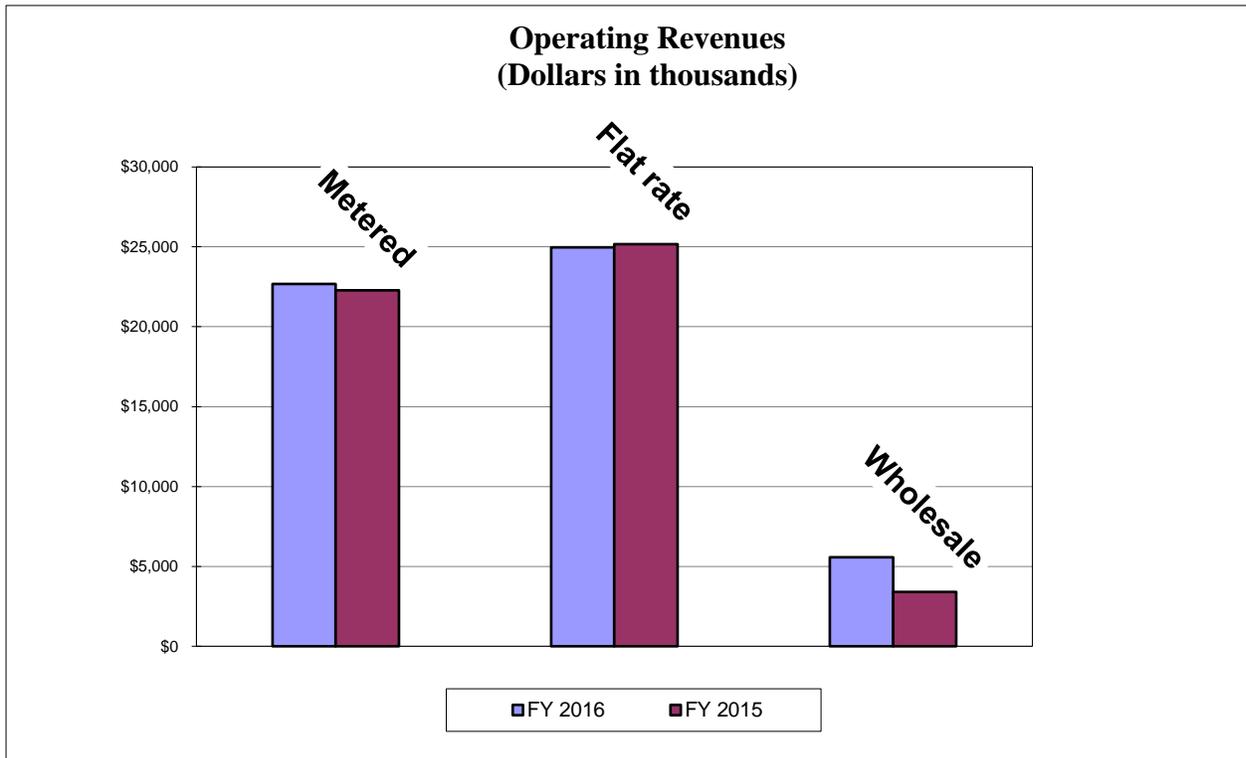
WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Management's Discussion and Analysis – Unaudited

June 30, 2016

(Dollars in thousands)

The chart below graphically displays the changes in the metered, flat rate, and wholesale revenue components of operating revenues from fiscal year 2015 to fiscal year 2016.



WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Management's Discussion and Analysis – Unaudited

June 30, 2016

(Dollars in thousands)

Expenses

The table below summarizes the Water Division's expenses for fiscal years 2016 and 2015:

	<u>2016</u>	<u>2015</u>	<u>Dollar change</u>	<u>Percentage change</u>
Operating expenses:				
Supply and purification	\$ 16,965	15,179	1,786	12%
Transmission and distribution	9,996	9,617	379	4
Power and pumping	8,262	7,902	360	5
Depreciation	5,301	5,039	262	5
Administrative and general	2,480	2,978	(498)	(17)
Interfund service used	2,944	2,020	924	46
Customer accounting	1,946	1,843	103	6
Cost of service line maintenance	746	1,033	(287)	(28)
Collector of revenue's fee, net	823	767	56	7
Cost of community service	31	18	13	72
Total operating expenses	<u>49,494</u>	<u>46,396</u>	<u>3,098</u>	<u>7%</u>
Nonoperating expenses:				
Interest expense on long-term obligations	228	233	(5)	(2)
Loss on disposal of capital assets	4	170	(166)	(98)
Total nonoperating expenses	<u>232</u>	<u>403</u>	<u>(171)</u>	<u>(42)</u>
Total expenses	<u>\$ 49,726</u>	<u>46,799</u>	<u>2,927</u>	<u>6%</u>
Transfers to City of St. Louis, Missouri	\$ 3,276	3,115	161	5%

Operating expenses in fiscal year 2016 compared to fiscal year 2015 increased by \$3,098, or 7%. Although there was a merit increase of 1.5% or higher in salaries and wages for fiscal year 2016, an increase of \$938, or 76%, for pension expense accounted for most of personnel services overall increase of \$1,290, or 8%. Additionally, chemicals and purchased power increased due to increase in pumping by 4 billion gallons or 9.2%. Support services and other services decreased by \$596, or 9%, and \$495, or 8%, respectively as labor workforce shifted to servicing construction projects.

The increase in supply and purification occurred in three main areas. Chemicals increased by \$1,360, or 22%, and materials and supplies increased by \$247, or 34%, due to increase in pumping. Pension expense increased by \$316, or 153%. Support services decreased by \$161, or 6%.

Power and pumping expenses increased by \$360, or 5%. Purchased power increased by \$548, or 17%, while materials and supplies increased by \$249, or 75%. Offsetting the increases were the decreases in support services and other services of \$497, or 27%.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Management's Discussion and Analysis – Unaudited

June 30, 2016

(Dollars in thousands)

Transmission and distribution expenses increased by \$379, or 4%. A significant increase in these expenses occurred in salaries and wages, which went up by \$512, or 7%. The increase was due to increase of \$345, or 117%, in pension expense and increase of \$167, or 3%, in salaries and wages due to merit increase and overtime. Offsetting the increase in operating expenses was the increase of amount capitalized or allocated to other accounts of \$193, or 4%. Depreciation increased by \$82, or 31%, due to an increase in replacement of rolling stocks and other capital assets in fiscal year 2016.

Interfund services used increased by \$924, or 46%. This increase was mainly due to an increase in payments to workers' compensation insurance and administration. Workers' compensation costs are managed by the Public Facilities Protection Corporation (PFPC), an internal service-fund of the City of St. Louis, Missouri. The Water Division reimburses PFPC for these paid claims on a cost-reimbursement basis. Payments to PFPC for workers' compensation expenses and IBNR plus reserve increased by \$873, or 229%. Reimbursement to the City for services it provides to the Water Division through cost allocation increased by \$76, or 9%. Services provided by the Street Department increased by \$26, or 27%, while Equipment repair services decreased by \$51, or 9%.

Customer accounting expenses remained relatively unchanged, increasing by only \$103, or 6%. This increase was mostly due to increase in pension expense.

Service line maintenance costs decreased \$287, or 28%, as the number of service lines repaired decreased in 2016 compared to 2015.

The collector of revenue's fee increased by \$56, or 7%.

General Trends and Significant Events

Ordinance 68694 authorized a 12% across-the-board water rate increase that became effective July 1, 2010. There has been no rate adjustment since then. This increase, coupled with continuing cost containment efforts, has helped ensure that the net revenues test required by the Indenture of Trust for fiscal year 2016 was properly met.

In July 2010, the City passed Ordinance 68698, which authorized the City to charge \$11 per month per dwelling unit for residential solid waste service. The Water Division's billing system continues to be used to invoice the solid waste charge on a combined utility bill that includes the solid waste charge and water service charge. All payments are kept separate and distinct. Payments for the solid waste charge are never deposited into water revenue.

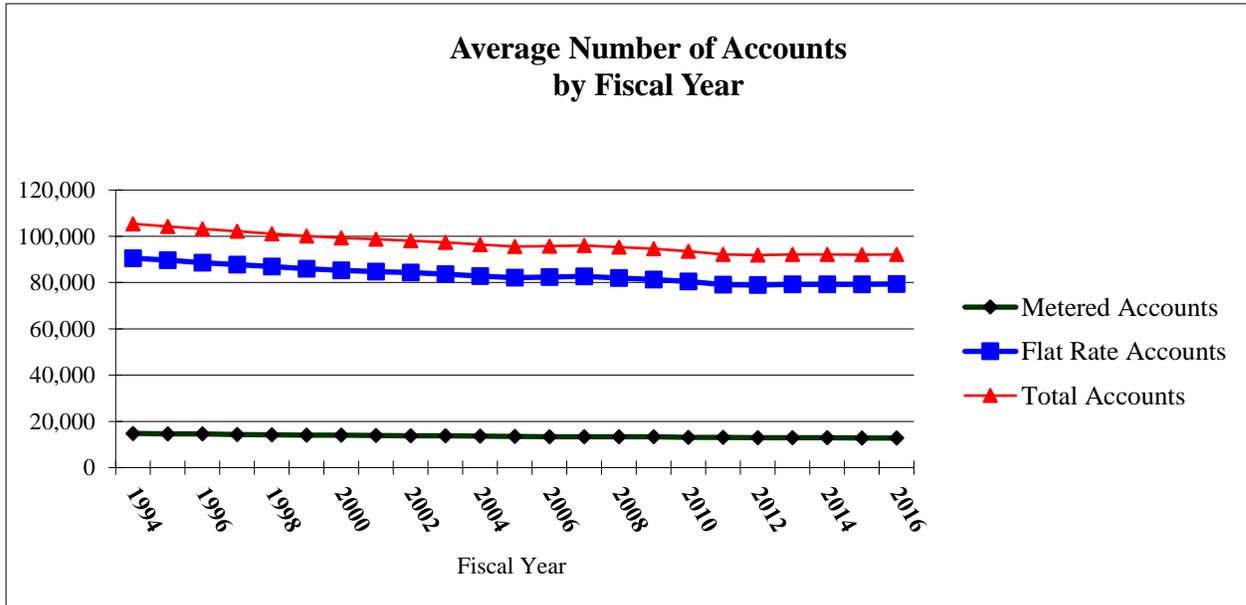
WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Management's Discussion and Analysis – Unaudited

June 30, 2016

(Dollars in thousands)

The chart below depicts the number of flat rate and metered accounts over the last 20 years.



Rate Covenant

In the Indenture of Trust pertaining to the Series 2013 Water Revenue Refunding Bonds (Series 2013 Bonds) of the Water Division, the City covenants that as long as bonds remain outstanding, the City will adopt or continue in effect water rates at least sufficient to produce net revenues for the next succeeding fiscal year at least equal to one hundred ten percent (110%) of the amount of the principal and interest coming due on all bonds during the next succeeding fiscal year.

Additionally, if the City has not adjusted water rates within a 24-month period since the last adjustment, the City covenants that it shall engage a consulting engineer to perform a water rate study for the purpose of determining net revenues for the next succeeding two-year period.

If the study indicates that a rate adjustment is necessary to comply with the rate covenants, the City agrees to make the necessary adjustments. As there has been no water rate change since July 2010, a water rate study was completed in fiscal year 2015 per the requirement. The completed water rate study and the current net revenue calculation both indicated that water revenues were sufficient so that no water rate increase was required by the covenants.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Management's Discussion and Analysis – Unaudited

June 30, 2016

(Dollars in thousands)

Capital Assets and Long-Term Debt

Total capital assets being depreciated increased \$5,829, or 2%, from fiscal year 2015 to fiscal year 2016. The increase primarily reflects additional net capital spending of \$4,089 on water mains, lines, and accessories throughout the water distribution system. Capital assets also increased by \$1,740 due to purchases of replacement rolling stocks, construction and maintenance equipment, and various completed projects throughout the water plants.

During fiscal year 2014, and pursuant to authority granted in Ordinance 69504, the City authorized the Water Revenue Refunding Bonds (State of Missouri-Direct Loan Program) Series 2013, in an aggregate principal amount to not exceed \$9,500. This drawdown loan is used to fund projects associated with the extension, improvement, purchase, acquisition, construction, and enlargement of the City's Waterworks System. The revenue bonds mature annually through fiscal year 2034 with a fixed rate of 1.56%. At June 30, 2016, the Water Division drew down \$5,721 of the loan.

Requests for Additional Information

The financial information presented in this document is intended to provide a general overview of the Water Division's finances. Any questions regarding the information provided in this report should be addressed to the Finance Office, City of St. Louis Water Division, 1640 South Kingshighway, St. Louis, Missouri 63110.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Balance Sheet

June 30, 2016

(Dollars in thousands)

Assets and Deferred Outflow of Resources

Current assets:	
Cash and investments:	
Restricted cash	\$ 229
Unrestricted cash	19,515
Unrestricted investments	17,991
Accounts receivable, net	7,005
Unbilled water revenue	6,005
Supplies and materials	2,114
Other receivable	74
Total current assets	<u>52,933</u>
Noncurrent assets:	
Cash and investments:	
Restricted cash	3,229
Unrestricted investments	1,202
Capital assets, net:	
Nondepreciable	9,237
Depreciable	146,311
Intangible assets, net	553
Total noncurrent assets	<u>160,532</u>
Deferred outflow of resources	<u>5,293</u>
Total assets and deferred outflow of resources	<u>\$ 218,758</u>

Liabilities, Deferred Inflow of Resources, and Net Position

Current liabilities:	
Payable from unrestricted assets:	
Accounts and wages payable	\$ 4,922
Other accrued liabilities	4,088
Unearned revenue	1,767
Due to City of St. Louis, Missouri	4,153
Total current liabilities payable from unrestricted assets	<u>14,930</u>
Payable from restricted assets:	
Current maturities of water revenue bonds payable	412
Accrued interest payable	65
Total current liabilities payable from restricted assets	<u>477</u>
Total current liabilities	<u>15,407</u>
Noncurrent liabilities:	
Water revenue bonds payable	4,706
Customer deposits – payable from restricted assets	2,479
Net pension liability	13,273
Other liability to the City of St. Louis, Missouri	2,865
Sick leave liability	1,490
Total noncurrent liabilities	<u>24,813</u>
Deferred inflow of resources	<u>449</u>
Total liabilities and deferred inflow of resources	<u>40,669</u>
Net position:	
Net investment in capital assets	150,430
Restricted for debt service	979
Unrestricted	26,680
Total net position	<u>178,089</u>
Total liabilities, deferred inflow of resources, and net position	<u>\$ 218,758</u>

See accompanying notes to basic financial statements.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Statement of Revenues, Expenses, and Changes in Fund Net Position

Year ended June 30, 2016

(Dollars in thousands)

Operating revenues:	
Metered	\$ 22,687
Flat rate	24,974
Wholesale	5,568
Other	<u>3,309</u>
Total operating revenues	<u>56,538</u>
Operating expenses:	
Supply and purification	16,965
Transmission and distribution	9,996
Power and pumping	8,262
Depreciation (not allocated to other operating expenses)	5,301
Administrative and general	2,480
Interfund services used	2,944
Customer accounting	1,946
Cost of service line maintenance	746
Collector of revenue's fee, net	823
Cost of community service	<u>31</u>
Total operating expenses	<u>49,494</u>
Operating income	<u>7,044</u>
Nonoperating revenues (expenses):	
Investment earnings	147
Interest expense on long-term obligations	(228)
Miscellaneous, net	956
Loss on disposal of capital assets	<u>(4)</u>
Total nonoperating revenues, net	<u>871</u>
Income before transfers	<u>7,915</u>
Transfers to the City of St. Louis, Missouri	<u>(3,276)</u>
Total transfers	<u>(3,276)</u>
Increase in net position	4,639
Total net position, beginning of year	<u>173,450</u>
Total net position, end of year	<u>\$ 178,089</u>

See accompanying notes to basic financial statements.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Statement of Cash Flows
Year ended June 30, 2016
(Dollars in thousands)

Cash flows from operating activities:	
Receipts from customers and users	\$ 54,655
Payments to suppliers of goods and services	(21,189)
Payments to employees	(17,222)
Payments for interfund services used	<u>(3,558)</u>
Net cash provided by operating activities	<u>12,686</u>
Cash flows from noncapital financing activities:	
Interest and principal paid on share of bond pension liability	(264)
Transfers to other funds of the City of St. Louis, Missouri	<u>(3,100)</u>
Net cash used in noncapital financial activities	<u>(3,364)</u>
Cash flows from capital and related financing activities:	
Acquisition and construction of capital assets	(11,200)
Interest paid on water revenue bonds	(25)
Principal paid on water revenue bonds	(404)
Proceeds from DNR reimbursements relating to revenue bond series 2013	3,234
Other capital and financing activities	<u>1,236</u>
Net cash used in capital and related financing activities	<u>(7,159)</u>
Cash flows from investing activities:	
Purchase of investments	(25,971)
Proceeds from maturities of investments	25,956
Interest income on cash and investments	<u>85</u>
Net cash provided by investing activities	<u>70</u>
Net increase in cash and cash equivalents	<u>\$ 2,233</u>
Cash and cash equivalents at beginning of year:	
Unrestricted	\$ 17,241
Restricted	<u>3,499</u>
	<u>\$ 20,740</u>
Cash and cash equivalents at end of year:	
Unrestricted	\$ 19,515
Restricted	<u>3,458</u>
	<u>\$ 22,973</u>
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ 7,044
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	5,729
Changes in assets and liabilities:	
Accounts receivable, net	(1,034)
Unbilled water revenue	(601)
Supplies and materials	161
Accounts and wages payable	811
Other accrued liabilities	391
Unearned revenue	(102)
Due to/from City of St. Louis, Missouri	209
Customer deposits	(54)
Increase in net pension liability	201
Pension bond liability	<u>(69)</u>
Total adjustments	<u>5,642</u>
Net cash provided by operating activities	<u>\$ 12,686</u>
Supplemental disclosures of noncash activities:	
Loss on disposal of capital assets	\$ 4

See accompanying notes to basic financial statements.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

(1) Summary of Significant Accounting Policies

(a) Reporting Entity

The basic financial statements include only the Water Division of the City of St. Louis, Missouri (the Water Division). The Water Division represents a separate enterprise fund of the City of St. Louis, Missouri (the City), and therefore, the basic financial statements of the Water Division are not intended to present the financial position, changes in financial position, and cash flows of the City as a whole in conformity with U.S. generally accepted accounting principles.

(b) Basis of Accounting

Governmental enterprise funds are used to account for operations of governmental entities that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that costs (expenses, including depreciation) of providing goods and services to the general public on a continuing basis be financed or recovered primarily through user charges.

The Water Division prepares its basic financial statements in accordance with U.S. generally accepted accounting principles for governmental enterprise funds that are similar to those for commercial enterprises. Accordingly, the economic resources measurement focus and accrual basis of accounting are used, whereby expenses are recorded when incurred and revenues when earned. Unbilled water revenues are accrued based on estimated billings for service provided through the end of the current fiscal year. In reporting its financial activity, the Water Division applies all applicable Governmental Accounting Standards Board (GASB) pronouncements.

Enterprise funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with an enterprise fund's ongoing operations. The principal operating revenues of the Water Division are charges to customers for water service. Operating expenses include the cost of services, administrative expenses, and depreciation. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

(c) Accounts Receivable, Net

Accounts receivable at June 30, 2016 consist of \$8,675 due from metered and flat rate customers and \$1,686 due from other customers. Such amounts are recorded net of an allowance for uncollectible accounts of \$3,356.

(d) Unbilled Water Revenue

The Water Division records the estimated amount of accrued, but unbilled, water revenue. This is a result of the Water Division billing its metered customers after the three-month billing cycle of water usage. At June 30, 2016, unbilled water revenue amounted to \$6,005.

(e) Supplies and Materials

Supplies and materials are valued using a moving average cost.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

(f) Capital Assets, Net

Capital assets were originally recorded in the accounts in 1958 and were based on an engineering study of the historical cost of properties constructed by employees of the Water Division. Accumulated depreciation, at the date the assets were recorded, was established after a review by a consulting firm.

Additions to capital assets subsequent to 1958 are recorded at historical cost. Provisions for depreciation of the capital assets are computed on a straight-line basis over the estimated useful lives of the assets and are charged to operating expenses. The estimated useful lives of depreciable assets are as follows:

	<u>Years</u>
Buildings and structures	44–55
Pumping equipment	28–44
Hydrants, transmission mains, and lines	50–100
Meters	33
Other equipment	5–25

Net interest costs on funds borrowed to finance the construction are capitalized and depreciated over the life of the related asset.

(g) Intangible Assets, Net

Intangible assets consist of software development costs and are amortized on the straight-line method over five years.

(h) Accounts and Wages Payable

Accounts and wages payable at June 30, 2016 comprises \$2,423 of accrued salaries and benefits and \$2,499 due to vendors and contractors.

(i) Vacation and Sick Leave Benefits

Under the terms of the City's personnel policy, employees of the City are granted vacation and sick leave. The vacation liability reflects the amounts attributable to employee services already rendered and are cumulative. The liability totaled \$1,906 as of June 30, 2016 and is included in accounts and wages payable.

Employees who have unused sick leave balances may, at retirement, elect to receive payment for one-half of the sick leave balance. As an estimate of the portion of sick leave that will result in termination payments, a liability has been recorded on the accompanying basic financial statements and represents one-half of the accumulated sick leave balances for those employees who will be eligible to retire within five years. The liability totaled \$1,490 as of June 30, 2016 and is classified as a noncurrent liability.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

(j) Unearned Revenue

The Water Division recognizes revenue associated with a service line maintenance surcharge in the period the related costs are incurred. Accordingly, the Water Division recognized surcharge revenue of \$746 during the year ended June 30, 2016, which is reported within other operating revenues. Unearned service line maintenance revenue amounted to \$242 at June 30, 2016.

The Water Division maintains a restricted cash account for amounts collected for service line maintenance. Interest earned is recorded in this cash account and the account balance is restricted solely for service line maintenance.

The Water Division records unearned revenue for amounts billed but not yet earned. This is the result of the Water Division billing its flat rate customers in advance of actual water usage. Revenue billed but not yet earned amounted to \$1,525 at June 30, 2016.

(k) Customer Deposits

The Water Division requires that metered customers deposit an amount approximately equal to an estimated billing for one cycle. These deposits are refunded to the customer, along with accrued interest on the deposits, when certain criteria have been met. The Water Division also holds deposits for construction-related work that are applied against the billing for work performed.

(l) Net Position

Net position is displayed in three components as follows:

(i) Net Investment in Capital Assets

This consists of capital assets, net of accumulated depreciation, less the outstanding balances of any bonds, notes, or other borrowings that are attributable to the acquisition and construction of those assets.

(ii) Restricted

This consists of net position that is legally restricted by outside parties or by law through constitutional provisions or enabling legislation. Net position restricted by statutory restrictions represents tax and other revenue sources that are required by statute to be expended only for specific purpose or purposes.

(iii) Unrestricted

This consists of net position that does not meet the definition of "restricted" or "net investment in capital assets." Included within unrestricted assets are the following components, which have been approved by City ordinance:

- (a) *Construction Funds* – City ordinances provide that amounts appropriated from the Water Contingent Account shall be held in the Construction Fund from which they shall be disbursed for the purposes contemplated in these ordinances. The balance of this fund as of June 30,

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

2016 is \$12,077, which funds are designated for capital projects and have been approved by City ordinances.

- (b) *Customer Deposits* – City ordinances provide that amounts paid by customers as deposits on metered water accounts, construction, and unclaimed meter deposits be held in escrow until such time as they are returned to customers in the form of cash or as a credit on the applicable customer's water bill. The balance of customer deposits as of June 30, 2016 is \$2,479.
- (c) *Service Line Maintenance* – City ordinances provide that the Water Division collects a \$3.00 (in whole dollars) per quarter surcharge from flat rate and metered residential customers having six or less dwelling units. These funds are deposited in the Service Line Maintenance Account. This account, including interest earned, is used to pay for the repair of certain portions of the water lines for these customers.

(m) Statement of Cash Flows

For purposes of the statement of cash flows, cash and cash equivalents are defined as all highly liquid investments with a maturity of 3 months or less when purchased.

(n) New Accounting Pronouncements

GASB Statement No. 72, *Fair Value Measurement and Application*, was issued in February 2015. This statement addresses accounting and financial reporting issues related to fair value measurements. The statement requires disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques. The requirements of this statement are effective for the Water Division for the year ended June 30, 2016. In adopting these standards, the Water Division has revised the note disclosure to reflect the level of fair value hierarchy for investments, as well as indicated the fair value methodology. This information can be referenced in note 2.

GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, was issued in June 2015. The objective of this statement is to identify the hierarchy of generally accepted accounting principles. This statement reduces the generally accepted accounting principles (GAAP) hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified with a source of authoritative GAAP. The requirements of this statement are effective for the Water Division for the year ended June 30, 2016.

(o) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires the Water Division to make estimates and assumptions that affect the reported amounts of assets and liabilities at fiscal year-end and revenues and expenses during the reporting period. Actual results could differ from those estimates.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

(2) Cash and Investments

The Water Division applies the provisions of GASB Statement No. 72 for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the financial statements on a recurring basis. GASB Statement No. 72 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets that the entity has the ability to access at the measurement date. Level 1 investments include U.S. treasury obligations.
- Level 2 inputs are observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 investments include commercial paper and U.S. government agency obligations.
- Level 3 inputs are significant unobservable inputs for the asset. The Water Division had no Level 3 investments as of June 30, 2016.

The following table presents assets that are measured at fair value on a recurring basis at June 30, 2016:

	<u>Total</u>	<u>Quoted prices in active markets for identical assets (Level 1)</u>	<u>Significant other observable inputs (Level 2)</u>	<u>Significant unobservable inputs (Level 3)</u>
Assets:				
U.S. Treasury obligations	\$ 6,032	6,032	—	—
Certificates of deposit	1,976	1,976	—	—
U.S. government agency obligations	1,202	—	1,202	—
Commercial paper	9,983	—	9,983	—
Total	<u>\$ 19,193</u>	<u>8,008</u>	<u>11,185</u>	<u>—</u>

Investments are recorded at fair value, which is determined by closing market prices at year-end as reported by the investment custodian.

The Water Division deposits all cash with the Office of the Treasurer of the City, which maintains all banking relationships for the Water Division.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

As of June 30, 2016, the Water Division had the following cash deposits and investments:

U.S. Treasury obligations	\$	6,032
Certificates of deposit		1,976
Federal Home Loan Mortgage Corporation		1,202
Commercial paper		9,983
Cash deposits		<u>22,973</u>
Total cash and investments	\$	<u><u>42,166</u></u>

State statutes and City investment policies authorize the deposit of funds in financial institutions. For City funds, investments may be made in obligations of the U.S. government or any agency or instrumentality thereof, bonds of the State of Missouri or any city within the state with a population of 400,000 inhabitants or more, or time certificates of deposit; provided, however, that no such investment shall be purchased at a price in excess of par. In addition, the City may enter into repurchase agreements maturing and becoming payable within 90 days secured by U.S. Treasury obligations, obligations of the U.S. government agencies, or instrumentalities of any maturity as provided by law. The City's funds in the form of cash on deposit or time certificates of deposit are required to be insured or collateralized by authorized investments held in the City's name. Actual investment decisions are made by the Treasurer and the City's fiscal agents.

(a) Interest Rate Risk

The Water Division seeks to minimize its exposure to fair value losses arising from changes in interest rates by selecting investments in adherence to the Investment Policy for the City of St. Louis, Missouri (the Investment Policy). The Investment Policy provides that, to the extent possible, the City shall attempt to match its investments with anticipated cash flow requirements. Unless matched to a specific cash flow, the City will not directly invest in securities or make a time deposit with a stated maturity of more than five years from the date of purchase. The average maturity for collateral provided to the City for deposits in connection with a repurchase agreement shall not exceed five years without the written approval of the Treasurer. In connection with any outstanding bond issue, debt service reserve funds may be invested to a maximum maturity of 15 years and up to 30 years with the written approval of the Treasurer.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

The Water Division's investments (excluding cash deposits) had the following maturities (in years) on June 30, 2016:

	<u>Fair value</u>	<u>Less than 1</u>	<u>1-5</u>
U.S. Treasury obligations	\$ 6,032	6,032	—
Certificates of deposit	1,976	1,976	—
Federal Home Loan Mortgage Corporation	1,202	—	1,202
Commercial paper	9,983	9,983	—
	<u>\$ 19,193</u>	<u>17,991</u>	<u>1,202</u>

(b) Credit Risk

The City's Investment Policy limits the types of securities available for investment to collateralized public deposits, obligations of the U.S. government or its agencies, obligations of government-sponsored corporations, banker's acceptances, and commercial paper. Banker's acceptances must be rated with the highest short-term credit rating of any two Nationally Recognized Statistical Rating Organizations (NRSROs) at the time of purchase. Investments in commercial paper are limited to issuing corporations that have a total commercial paper program size in excess of \$250,000 and have long-term debt ratings "AA" or better from at least one NRSRO.

The Water Division's investments in U.S. Treasuries are explicitly guaranteed by the U.S. government and, therefore, do not require a rating. At June 30, 2016, the Federal Home Loan Mortgage Corporation investments were rated Aa2 and Aaa, respectively, by Moody's. Water Division's holdings in commercial paper were rated A-1/P-1/F1 as of June 30, 2016 by Standard & Poor's, Moody's, and Fitch, respectively.

(c) Custodial Credit Risk

For an investment, custodial credit risk is the risk that, in the event of the failure of a counterparty, the Water Division will not be able to recover the value of the investments or collateral securities that are in the possession of an outside party.

The City's Investment Policy requires that all cash deposits, time certificates of deposit, deposits with listed institutions, and repurchase agreements be covered by adequate pledged collateral. Acceptable collateral includes U.S. Treasury obligations, other interest-bearing securities guaranteed as to principal and interest by the U.S. government or an agency or instrumentality of the U.S. government, bonds of the State of Missouri, or bonds of the City. The market value of the principal and accrued interest of the collateral must equal 103% of the deposits secured, less any amount subject to federal deposit insurance. All City securities and securities pledged as collateral must be held in a segregated account on behalf of the City by an independent third party with whom the City has a current custodial agreement and has been designated by the Treasurer and Funds Committee as eligible to serve in such a capacity.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
 (An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

At June 30, 2016, all Water Division investments and all securities pledged as collateral are held by the counterparty's trust department or agent in the City's name.

(d) Concentration of Credit Risk

The Investment Policy provides that, with the exception of U.S. Treasury Securities and cash deposits, no more than 35% of the City's total investment portfolio will be invested in a single security type or with a single financial institution. The Water Division does not have a separate investment policy.

At June 30, 2016, the concentration of the Water Division's investments (excluding cash deposits) was as follows:

U.S. Treasuries	32%
Certificates of deposit	10
Federal Home Loan Mortgage Corporation	6
Commercial paper	52
	100%
	100%

(3) Restricted Assets

Cash restricted in accordance with bond provisions and City ordinances at June 30, 2016 is as follows:

Bond funds:	
Waterworks bond fund	\$ 229
Water replacement and improvement account	750
	979
Total bond funds	979
Customer deposits	2,479
	2,479
Total restricted cash	\$ 3,458

Bond fund provisions require that revenues derived from the operation of the Waterworks System be deposited in the Waterworks Revenue Account. From this account, the following allocations are made on the first business day of each month in the following order of priority:

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

Series 2013 Water Revenue Refunding Bond Funds

- (1) To the unrestricted Waterworks Operations and Maintenance Fund, an amount sufficient to pay the estimated operation and maintenance expenses during the next month.
- (2) To the Waterworks Bond Fund, an amount at least equal to the calculated 1/6 amount of interest that will come due on the next interest payment date, plus an amount at least equal to 1/6 of the aggregate principal amount of bonds that will come due on the next bond maturity date. This account shall be used only for the payment of bond principal and interest, as the same shall become due.
- (3) To the Water Replacement and Improvement Fund, an amount equal to \$25 per month until the account balance aggregates \$750. This account shall be used for making replacements, extensions, and improvements to the Waterworks System, and for the purpose of meeting unforeseen contingencies and emergencies arising in the operation of the Waterworks System of the City.
- (4) The remaining balance in the Waterworks Revenue Fund is deposited into the unrestricted Water Contingent Fund. This money shall be used for paying the cost of the operation, maintenance, and repair of the Waterworks System; paying the cost of extending, improving, or making replacements to the Waterworks System; preventing default in, anticipating payments into, or increasing the amounts in the other accounts; paying any gross receipts tax now or hereafter levied by the City; paying the principal or the interest on any subordinate or junior lien bonds; paying any redemption premium due on the bonds; or any other lawful purpose for use by the Waterworks System.

(4) Capital Assets

The following table shows the changes in capital assets for the fiscal year ended June 30, 2016:

	Balances June 30, 2015	Additions	Retirements	Transfers	Balances June 30, 2016
Capital assets being depreciated:					
Buildings and structures	\$ 42,155	—	—	—	42,155
Reservoirs	35,172	—	—	—	35,172
Boiler plant equipment	661	—	—	—	661
Pumping equipment	10,923	—	—	254	11,177
Purification basins and equipment	43,753	—	—	—	43,753
Water mains, lines, and accessories	134,462	3,293	(180)	976	138,551
Equipment	17,915	103	(105)	41	17,954
Motor vehicle equipment	9,224	1,478	(719)	688	10,671
Total capital assets being depreciated	<u>294,265</u>	<u>4,874</u>	<u>(1,004)</u>	<u>1,959</u>	<u>300,094</u>

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

	Balances June 30, 2015	Additions	Retirements	Transfers	Balances June 30, 2016
Less accumulated depreciation:					
Buildings and structures	\$ (27,000)	(662)	—	—	(27,662)
Reservoirs	(12,629)	(731)	—	—	(13,360)
Boiler plant equipment	(647)	(3)	—	—	(650)
Pumping equipment	(9,416)	(233)	—	—	(9,649)
Purification basins and equipment	(18,397)	(938)	—	—	(19,335)
Water mains, lines, and accessories	(60,318)	(1,741)	172	—	(61,887)
Equipment	(14,830)	(840)	104	—	(15,566)
Motor vehicle equipment	(5,806)	(581)	713	—	(5,674)
	<u>(149,043)</u>	<u>(5,729)</u>	<u>989</u>	<u>—</u>	<u>(153,783)</u>
	<u>145,222</u>	<u>(855)</u>	<u>(15)</u>	<u>1,959</u>	<u>146,311</u>
Capital assets not being depreciated:					
Land	1,238	—	—	—	1,238
Construction in progress	3,621	6,341	—	(1,963)	7,999
	<u>4,859</u>	<u>6,341</u>	<u>—</u>	<u>(1,963)</u>	<u>9,237</u>
Total capital assets not being depreciated	<u>4,859</u>	<u>6,341</u>	<u>—</u>	<u>(1,963)</u>	<u>9,237</u>
	<u>\$ 150,081</u>	<u>5,486</u>	<u>(15)</u>	<u>(4)</u>	<u>155,548</u>

Construction in progress consists primarily of various improvements to the Waterworks System.

(5) Employees' Retirement System of the City of St. Louis

The Water Division participates in the Employees Retirement System of the City of St. Louis (Employees System), a cost-sharing, multiple-employer public defined benefit pension plan.

(a) Plan Description

All Water Division employees become members of the Employees System upon employment, with the exception of employees hired after attaining age 60.

The Employees System issues a publicly available financial report that includes financial statements and required supplementary information. The Employees System financial statements are prepared using the accrual basis of accounting. That report may be obtained by writing to the Employees Retirement System of the City of St. Louis; 1114 Market Street, Suite 900; St. Louis, Missouri 63101.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

The Employees System provides for defined benefit payments for retirement, death, or disability to eligible employees or their beneficiaries based upon creditable service, final average compensation, and a benefit compensation base. Benefits vest to employees covered by the Employees System after the employee has attained five years of creditable service. Employees retire with full retirement benefits after the age of 65 or if the employee's age and creditable service combined equal or exceed 85 years. Employees may retire and receive a reduced benefit after age 60 with five years of creditable service; age 55 with at least 20 years of creditable service; or at any age with 30 years of creditable service. The monthly pension benefits of all retirees or their beneficiaries are adjusted according to the changes in the Consumer Price Index of the U.S. Department of Labor. Increases are limited each year, with total increases to retirees or their beneficiaries limited to 25%.

On June 8, 2000, the Mayor of the City approved an ordinance passed by the Board of Aldermen, authorizing a Deferred Retirement Option Plan (DROP), which became effective January 1, 2001. This plan states that when members reach retirement age, they are allowed to work for five additional years and defer receipt of their retirement allowance. The calculation of average salary for retirement benefits will not include the additional years of service after normal retirement age. The amount that would have been received as retirement benefit is put in a special DROP account monthly. The DROP account will not be adjusted for cost of living increases. The DROP account earns interest at the actuarial valuation rate of return or at the 10-year U.S. Treasury Bond yield as of September 30 for DROP participants enrolling February 1, 2003 and thereafter. After the members completely terminate employment, the member can withdraw amounts from the DROP account in a lump sum or according to a deferred retirement payment plan.

(b) Funding Policy

The Employees System's funding policy provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are sufficient to accumulate assets to pay benefits due. If contributions are necessary, level percentage of payroll employer contribution rates are determined using the projected unit credit actuarial cost method.

Employer contribution rates are established annually by the Board of Trustees of the Employees System based on an actuarial study. The Board of Trustees established the required employer contributions rate based on active member payroll of 13.89%, effective July 1, 2015.

Employees who became members of the Employees System prior to October 14, 1977, and continued to make contributions, may make voluntary contributions to the Employees System equal to 3% of their compensation until the employee's compensation equals the maximum annual taxable earnings under the Federal Social Security Act. Thereafter, employees may contribute 6% of their compensation for the remainder of the calendar year.

The Water Division's contributions to the Employees System for the year ended June 30, 2016 were \$1,975.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

(c) Net Pension Liability

The Water Division reported a liability of \$13,273 for its proportionate share of the net pension liability as of June 30, 2016. The net pension liability was measured as of September 30, 2015 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of October 1, 2015. The Water Division's proportion of the net pension liability was based on the Water Division's share of contributions to the Employees System relative to the contributions of all Employees System participating employers. As of September 30, 2015, the Water Division's collective proportion was 5.84%, which was an increase of 0.02% from its proportion as of September 30, 2014.

The following were some of the significant actuarial assumptions used in the valuation of the Employees System:

Valuation date	October 1, 2015
Actuarial cost method	Entry age normal cost method
Amortization method	Rolling 20-year level dollar amortization of unfunded liability
Remaining amortization period	20 years as of October 1, 2014
Asset valuation method	5-year smoothed market
Inflation rate	3.125%
Discount rate	7.50%
Projected salary increases	3.50% plus merit component based on employee's years of service
Mortality	1994 Group Annuity Mortality Table

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

The long-term expected rate of return on the Employees System investments was determined using a building-block approach and a forward-looking model in which best estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These rates of return 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. For each major asset class that is included in the pension plan's target asset allocation as of September 30, 2015, these best estimates are summarized in the following table:

Asset class	Target allocation	Long-term expected real rate of return
Private equity	5.00%	8.25%
Real estate	10.00	5.00
Hedge funds	10.00	4.50
Master limited partnerships	7.50	6.00
International equity	21.50	6.84
Domestic equity	21.00	5.05
Fixed income	25.00	2.25
	100.00%	

The discount rate used to measure the total pension liability was 7.50%. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that contributions will be made at rates equal to the difference between actuarially determined contribution rates and the employee rate. Based on those assumptions, the pension plans fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability. For the October 1, 2015 actuarial valuation, a 7.50% discount rate was used. The sensitivity of the net pension liability to changes in the discount rate for the year ended June 30, 2016 for the Water Division is as follows:

	Rate	Net Pension Liability
1% decrease	6.50%	\$ 18,933
Current rate	7.50	13,273
1% increase	8.50	8,434

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
 (An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

Pension Plan Fiduciary Net Position – Detailed information about the pension plan’s fiduciary net position is available in the separately issued Employees System financial report.

(d) Pension Expense

For the year ended June 30, 2016, the Water Division recognized pension expense of \$2,176. Annual pension expense consists of service cost, interest, and administrative expenses on the pension liability less employee contributions and projected earnings on pension plan investments. The difference between actual and expected earnings is recorded as a deferred outflow/inflow of resources and recognized in pension expense over a five-year period.

(e) Deferred Outflows/Inflows of Resources Related to Pension

In accordance with GASB Statements No. 68, the Water Division recognizes differences between actual and expected experience with regard to economic or demographic factors, changes of assumptions about future economic or demographic factors, the difference between actual and expected investment returns, changes in proportion, and contributions subsequent to the measurement date as deferred outflows/inflows of resources. At June 30, 2016, the Water Division reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources as follows:

	Deferred outflows of resources	Deferred inflows of resources
Differences between expected and actual experience	\$ —	(212)
Net difference between projected and actual earnings on pension plan investments	3,824	—
Changes of assumptions	—	(199)
Changes in proportion	20	(38)
Water Division contributions subsequent to the measurement date	1,449	—
Total	\$ 5,293	(449)

The \$1,449 reported as deferred outflows of resources related to pensions resulting from the Water Division’s contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending June 30, 2017.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

The Water Division recognizes differences between actual and expected investment performance included in deferred outflows/inflows of resources on a straight-line basis over five years. Differences between expected and actual experience on actuarial assumptions are amortized over the average expected remaining service life of the Employee System's employees. The following table summarizes the future recognition of these items:

Year ending June 30	Recognition
2017	\$ 741
2018	741
2019	956
2020	957
2021	—
Thereafter	—
	\$ 3,395

During fiscal year 2008, the City of St. Louis Municipal Finance Corporation issued \$46,700 in Taxable Leasehold Revenue and Refunding Bonds Series 2007 (Pension Funding Project) to fund the Employees System. While the Water Division is not legally responsible for these bonds, \$3,269 of the proceeds was allocated to the Water Division. A \$2,865 liability is reflected as other noncurrent long-term liabilities on the balance sheet and is payable to the City of St. Louis by June 30, 2037.

(6) Change in Noncurrent Liabilities

The following table shows the changes in noncurrent liabilities for the fiscal year ended June 30, 2016:

	Balance June 30, 2015	Additions	Reductions	Balance June 30, 2016	Due within one year
Revenue bonds payable (note 7)	\$ 2,288	3,234	(404)	5,118	412
Net pension liability (note 5)	9,007	4,266	—	13,273	—
Customer deposits	2,533	2,114	(2,168)	2,479	—
Other liability to the City of St. Louis, Missouri (note 5)	2,934	—	(69)	2,865	—
Accrued vacation and sick time benefits	3,439	148	(191)	3,396	1,906
Total	\$ 20,201	9,762	(2,832)	27,131	2,318

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

(7) Water Revenue Refunding Bonds

Water revenue bonds outstanding at June 30, 2016 are payable solely from and secured by, a pledge of net revenues from the operation of the Water Division and are as follows:

Series 2013 Water Revenue Refunding Bonds, 1.56%, drawdown loan, payable in varying amounts through January 1, 2034	\$ 5,118
Less current maturities	(412)
	\$ 4,706

(a) Series 2013 Water Revenue Refunding Bonds

In November 2013, the Water Division issued \$9,500 (not to exceed) in Water Revenue Bonds (Series 2013 Bonds) through the Missouri Department of Natural Resources Direct Loan Program. This bond issue is a drawdown loan with a fixed interest rate of 1.56% to fund various projects at the water treatment plants and throughout the distribution system. In total, as of June 30, 2016, the Water Division drew down \$5,721 of the loan.

Debt service requirements to maturity of the 2013 Series Water Revenue Bonds are as follows:

	Principal	Interest	Total
For the year ending June 30:			
2017	\$ 412	80	492
2018	422	73	495
2019	430	67	497
2020	439	60	499
2021	448	53	501
2022–2026	2,385	158	2,543
2027–2028	582	10	592
	\$ 5,118	501	5,619

Principal and Interest payments are due semiannually on January 1 and July 1.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

(8) Transactions with the City

During the fiscal year ended June 30, 2016, the City charged the Water Division \$2,944 for services rendered by various City departments. This amount is included in the Water Division's operating expenses as interfund services used. At June 30, 2016, \$643 was due to the City for services rendered. The Water Division also furnishes water to the fire department, parks department, and most other departments at no charge; while the related cost of all of the water cannot be determined since most of the water provided is not metered, those City buildings that are metered used \$561 worth of service for the year ended June 30, 2016. No reduction from the amount the Water Division owed to the City for services rendered was allowed for this water service provided by the Water Division to the City.

In addition, throughout the year, the Collector of Revenue of the City of St. Louis, Missouri (the Collector) deducts a 4% gross receipts charge from collections made on behalf of the Water Division. At June 30, 2016, \$355 was due to the City. Each year, the Collector computes actual costs incurred relating to services that it provided to the Water Division and refunds any excess deduction. During the year ended June 30, 2016, the Water Division paid \$823, net of refunds to the Collector for services rendered.

The Water Division also pays a 6% tax on monthly gross receipts, which is applicable to all public utilities. During the year ended June 30, 2016, the Water Division recorded amounts accrued or paid to the City of \$3,276. This amount is reflected as transfers to the City in the accompanying basic financial statements. No payment in lieu of property taxes is made. At June 30, 2016, \$310 was due to the City for gross receipts tax.

(9) Contingencies

The Water Division has identified certain of its structures as having asbestos in place. As part of its continuing process of upgrading facilities, the costs for removal of the asbestos material and restoration or replacement of the affected areas are being included in budgets for capital projects. No mandatory time requirement is in effect. The removal plan would be accelerated by changes in plans for remodeling, if any.

There is an aggregate of general liability claims outstanding of \$90, which the City Counselor's office has determined there is a reasonable possibility that a loss contingency may be incurred but no accrual has been made within the basic financial statements because the loss is not probable.

At June 30, 2016, the Water Division has \$704 in gain contingencies related to damages caused by others to Water Division properties that are not reflected within the basic financial statements because such transactions may not be recognized as revenue prior to realization.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

(10) Risk Management

The Water Division is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Water Division participates in the Public Facilities Protection Corporation (PFPC), an internal service fund of the City. The purpose of PFPC is to account for risks in which the City is self-insured, primarily workers' compensation, unemployment benefits, certain general liability, and various other claims and legal actions. All self-insured workers' compensation claims liabilities and payments are recorded in PFPC. The Water Division reimburses PFPC for workers' compensation claims on a cost-reimbursement basis. At June 30, 2016, the Water Division owed the PFPC \$2,845 for unreimbursed workers' compensation claims and is included in Due to City of St. Louis, Missouri on the balance sheet.

(11) Wholesale Water Contracts

The Water Division has entered into contracts for the sale of water to the following parties: the cities of St. Charles, Missouri and St. Peters, Missouri; the Missouri American Water Company (the Company); and the Public Water Supply District No. 2 of St. Charles County, Missouri. The parties have agreed to pay for water at a rate based on certain costs incurred at the Howard Bend Water Treatment Plant.

Additionally, the Water Division and the Company have amended their agreement whereby the Company has agreed to purchase a minimum quantity of water per month from the Water Division. The Water Division renewed this contract, which is effective December 2015 and will expire in 2045.

(12) Pledged Revenue

The Water Division has pledged specific revenue streams to secure the repayment of the Series 2013 Bonds. The following table lists those revenues along with the purpose of the debt, the term of the commitment, the approximate proportion of the pledged revenue to revenue collected of the revenue stream as estimated at June 30, 2016, the current fiscal year principal and interest on the debt and the amount of pledged revenue earned during the current fiscal year:

<u>Type of revenue pledged</u>	<u>General purpose for debt</u>	<u>Term of pledged commitment</u>	<u>Proportion of pledged revenue to revenue collected</u>	<u>Principal and interest for the year ended June 30, 2016</u>	<u>Revenue recognized for the year ended June 30, 2016</u>
All Water Division revenues	Funding of various water division infrastructures	through 2016	0.8%	\$ 437	56,538

As of June 30, 2016, the remaining principal and interest requirement is \$5,619 payable through January 2028 (fiscal year 2028). The proportion of pledged revenue to revenue collected is estimated at 0.8% at June 30, 2016.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Notes to the Basic Financial Statements

June 30, 2016

(Dollars in thousands)

(13) Subsequent Events

In October 2016, the Water Division drew down an additional \$2,132 of the Series 2013 Water Revenue Refunding Bonds.

In November 2016, the final draw down request of \$1,647 was submitted to Missouri Department of Natural Resources relating to the Series 2013 Water Revenue Refunding Bonds. This satisfies the loan draw down requirement of not to exceed \$9,500.

OTHER INFORMATION – UNAUDITED

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
 (An Enterprise Fund of the City of St. Louis, Missouri)
 Detailed Schedule of Certain Operating Expenses – Unaudited
 Year ended June 30, 2016
 (Dollars in thousands)

Supply and purification:		
Salaries and wages	\$	4,470
Support services		2,687
Other services		1,362
Materials and supplies		964
Depreciation		50
Chemicals		7,432
		<u>16,965</u>
Less amounts capitalized or allocated to other accounts		<u>—</u>
Total supply and purification	\$	<u><u>16,965</u></u>
Transmission and distribution:		
Salaries and wages	\$	7,540
Support services		882
Other services		3,607
Materials and supplies		3,308
Depreciation		347
		<u>15,684</u>
Less amounts capitalized or allocated to other accounts		<u>(5,688)</u>
Total transmission and distribution	\$	<u><u>9,996</u></u>
Power and pumping:		
Salaries and wages	\$	2,075
Support services		1,440
Other services		405
Materials and supplies		582
Depreciation		10
Purchased power		3,750
		<u>8,262</u>
Less amounts capitalized or allocated to other accounts		<u>—</u>
Total power and pumping	\$	<u><u>8,262</u></u>
Administrative and general:		
Salaries and wages	\$	1,511
Support services		154
Other services		638
Materials and supplies		85
Depreciation		3
Bad debt expense		92
		<u>2,483</u>
Less amounts allocated to other accounts		<u>(3)</u>
Total administrative and general	\$	<u><u>2,480</u></u>
Customer accounting:		
Salaries and wages	\$	1,276
Support services		560
Other services		36
Materials and supplies		58
Depreciation		18
		<u>1,948</u>
Less amounts capitalized or allocated to other accounts		<u>(2)</u>
Total customer accounting	\$	<u><u>1,946</u></u>

See accompanying independent auditors' report.

WATER DIVISION OF THE CITY OF ST. LOUIS, MISSOURI
(An Enterprise Fund of the City of St. Louis, Missouri)

Schedule of Costs for Howard Bend Water Sales – Unaudited

Year ended June 30, 2016

(Dollars in thousands)

I. Direct Costs of Supply and Purification – Howard Bend	
Labor	\$ 2,229
Chemicals	2,516
Support services	842
Other materials and services	833
	<u>6,420</u>
	\$ <u>6,420</u>
II. Direct Costs of Power and Pumping – Howard Bend	
Power	\$ 1,519
Labor	635
Support services	354
Other materials and services	363
	<u>2,871</u>
	\$ <u>2,871</u>
III. General Office Expenses – Power and Pumping	\$ 1,007
IV. General Office Expenses – Supply and Purification	\$ 915
V. Reservoir Maintenance	\$ 62
VI. Administration and Finance Costs	
City services	\$ 1,003
Labor	1,511
Other services and miscellaneous	726
Support services	154
	<u>3,394</u>
	\$ <u>3,394</u>
VII. Specified Labor Costs	
Transmission and distribution	\$ 7,540
Supply and purification	4,470
Power and pumping	2,075
Customer accounting	1,276
	<u>15,361</u>
	\$ <u>15,361</u>

Note: The Water Division of the City of St. Louis, Missouri has entered into contracts for the sale of water to the following parties: the cities of St. Charles, Missouri, and St. Peters, Missouri, the Missouri American Water Company and the Public Water Supply District No. 2 of St. Charles County, Missouri. Under the terms of these agreement, the parties have agreed to pay for water at a rate based on certain costs incurred by the Water Division as its Howard Bend Water Treatment Plant. This information is presented in accordance with the requirements of the contracts and is included for use by the parties in determining water rates charged.

See accompanying independent auditors' report.