
City of Hamilton, Ohio – Wastewater System

Financial Statements

Years Ended December 31, 2013 and 2012

With Independent Auditor's Report



Dave Yost • Auditor of State

Members of Council
City of Hamilton
345 High Street
Hamilton, Ohio 45011

We have reviewed the *Independent Auditors' Report* of the City of Hamilton – Wastewater System, Butler County, prepared by Clark, Schaefer, Hackett & Co., for the audit period January 1, 2013 through December 31, 2013. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The City of Hamilton - Wastewater System is responsible for compliance with these laws and regulations.

A handwritten signature in black ink that reads "Dave Yost".

Dave Yost
Auditor of State

July 30, 2014

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INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and Members of Council
City of Hamilton, Ohio:

Report on the Financial Statements

We have audited the accompanying financial statements of the City of Hamilton, Ohio - Wastewater System, an enterprise fund of the City of Hamilton, Ohio (the Wastewater System), as of and for the year ended December 31, 2013 and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

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Opinion

In our opinion, the financial statements referred to previously present fairly, in all material respects, the financial position of the City of Hamilton, Ohio - Wastewater System as of December 31, 2013, and the change in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Prior Period Financial Statements

The financial statements of the City of Hamilton, Ohio - Wastewater System as of December 31, 2012 were audited by other auditors whose report dated June 25, 2013, expressed an unmodified opinion on those statements.

Emphasis of Matters

As described in Note 1, the financial statements present only the Wastewater System and do not purport to, and do not present fairly the financial position of the City of Hamilton, Ohio as of December 31, 2013 and 2012, and the changes in its financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 8 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.

Clark, Schaefer, Hackett & Co.

Cincinnati, Ohio
June 23, 2014

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2013 and 2012
Unaudited

The discussion and analysis of the City of Hamilton, Ohio's Wastewater System's financial performance provide an overall review of that System's financial activities for the years ended December 31, 2013 and 2012. While the intent of this discussion and analysis is to look at the system's financial performance, readers should also review the Statements of Net Position; Revenues, Expenses and Changes in Net Position; and Cash Flows to enhance their understanding of the system's fiscal performance.

Financial Highlights

Key highlights for 2013 and 2012 are as follows:

- The assets and deferred outflow of resources of the Hamilton Wastewater System exceed its liabilities at the close of 2013 and 2012, respectively, by \$31,576,306 and \$29,148,003 (net position). Of these amounts, \$8,350,117 and \$7,963,566 (unrestricted net position) for those years can be used to meet the System's ongoing obligations to customers and creditors.
- The System's total net position increased by \$2,428,303 between 2013 and 2012, representing a 8.3% increase.
- In 2013, the Wastewater System's long-term debt, net of premiums and discounts, decreased by \$2,126,631.

Wastewater System Summary

The City of Hamilton, Ohio owns and operates the Wastewater System, serving approximately 23,000 customers. The System consists of the treatment plant and sanitary sewer. The initial sludge plant was placed in service in 1959. In 1978, the Wastewater System was expanded to provide complete treatment services and an expansion of treatment facilities was completed during 2002.

The treatment plant, known as the Wastewater Reclamation Facility (WRF), is able to fully treat 32 MGD, the capacity of the WRF secondary treatment process. Wastewater flows in excess of 32 MGD receive only partial treatment. The stormwater train provides only primary treatment. The stormwater train's effluent is currently blended with fully treated flow from the wastewater train prior to disinfection, dechlorination and discharge to the Great Miami River.

This annual report consists only of the Statement of Net Position, the Statement of Revenues, Expenses and Changes in Net Position, and the Statement of Cash Flows as well as Notes to the Financial Statements for the City of Hamilton, Ohio's Wastewater System for the years ended December 31, 2013 and 2012.

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2013 and 2012
Unaudited

Reporting Hamilton's Wastewater System (Whole and Significant Fund)

The financial statements contained within this report include the City of Hamilton, Ohio's Wastewater System *only*. Readers desiring to view city-wide financial statements, as well as the impact that the Wastewater System has on the City's overall financial position and operating results, should refer to the City's Basic Financial Statements appearing in the Comprehensive Annual Financial Report for 2013 and 2012. The City of Hamilton's Wastewater System is reported as a business-type, enterprise fund and is considered a major fund for purposes of individual fund reporting. Payments made from the Wastewater Fund are restricted to Wastewater System purposes by municipal ordinance, Ohio Revised Code and indentures issued pursuant to long-term financing.

In the Statement of Net Position and the Statement of Revenues, Expenses and Changes in Net Position, the view of the system looks at all financial transactions of the Wastewater Fund and asks the question, "How did we do financially during 2013 and 2012?" These statements provide answers to that question. The statements include all assets, deferred outflow of resources and liabilities of the System using the accrual basis of accounting similar to the accounting used by private sector companies. This basis of accounting considers all of the current year's revenues and expenses regardless of when the cash is received or paid. These two statements report the System's net position and the changes in net position. The change in net position is important because it tells the reader whether, for the System, the financial position of the City has improved or diminished. However, in evaluating this position, non-financial information including the condition of capital assets will also need to be evaluated. The Notes to the Wastewater System's Financial Statements provide additional information that is essential to a full understanding of the data provided. The System provides services that have a charge based upon the amount of usage. The City's Wastewater System charges fees to recoup the cost of the entire operation of the Wastewater System as well as all capital expenses associated with these facilities.

Financial Analysis

As noted earlier, net position may serve over time as a useful indicator of financial position. In the case of the Wastewater Fund, assets and deferred outflow of resources exceeded liabilities by \$31,576,306 and \$29,148,003 as of December 31, 2013 and 2012, respectively. By far, the largest portion of the net position of the Wastewater System reflect its investment in capital assets (e.g. land, buildings, improvements, construction in progress, machinery and equipment) less any related debt used to acquire those assets that are still outstanding. The ratios of net investment in capital assets to total net position are as follows: 54.5% for 2013, 51.9% for 2012 and 53.1% for 2011. The System employs these assets in the treatment and collection of sanitary sewer flow; consequently, these assets are not readily available for future spending. The System's investment in its capital assets is reported net of related debt and it should be noted that the resources needed to repay these debts must be provided from other sources, primarily the revenues of the system, because the capital assets themselves cannot be used to liquidate the liabilities. Table 1 provides a summary of the Wastewater System's Statement of Net Position for the Years Ended December 31, 2013, 2012 and 2011.

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2013 and 2012
Unaudited

	2013	2012	2011
Current and Other Assets	\$42,066,679	\$43,216,801	\$48,714,000
Capital Assets	48,957,689	46,098,793	42,534,191
Total Assets	91,024,368	89,315,594	91,248,191
 Deferred Outflow of Resources	 426,124	 509,338	 597,617
 Long-term Liabilities	 54,789,188	 56,918,336	 59,114,830
Other Liabilities	5,084,998	3,758,593	3,892,002
Total Liabilities	59,874,186	60,676,929	63,006,832
 Net Investment in Capital Assets	 17,207,151	 15,122,814	 15,303,201
Restricted	6,019,038	6,061,623	6,182,327
Unrestricted	8,350,117	7,963,566	7,353,448
Total Net Position	\$31,576,306	\$29,148,003	\$28,838,976

As of December 31, 2013, 2012 and 2011, the Wastewater System is able to report positive balances in net position. The overall changes in net position were increases of \$2,428,303, \$309,027 and \$421,200 in 2013, 2012 and 2011, respectively. Operating revenues and expenses were fairly consistent with the previous year. Net non-operating expenses of \$2.5 million increased by \$33,063, primarily due to decreased investment earnings.

The Wastewater System reported a special item in 2013. A prior agreement between the City and International Paper required International Paper or its successor to reimburse the City for costs incurred by the City if the agreement was terminated before the end of 2022. When Smart Papers LLC ceased operations in the City in 2012, this triggered the early termination clause of the agreement, resulting in a required payment to the City from International Paper in the amount of \$2.85 million

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2013 and 2012
Unaudited

	2013	2012	2011
Operating Revenues	\$11,779,979	\$12,068,156	\$12,302,310
Operating Expenses:			
Depreciation	2,617,389	2,288,196	2,272,079
Other Operating Expenses	7,068,795	6,988,504	7,355,594
Total Operating Expenses	9,686,184	9,276,700	9,627,673
Operating income	2,093,795	2,791,456	2,674,637
Non-Operating revenues (expenses)			
Interest and fiscal charges	(2,570,192)	(2,595,927)	(2,308,786)
Other non-operating revenues	54,700	113,498	55,349
Total non-operating (expenses)	(2,515,492)	(2,482,429)	(2,253,437)
Income (loss) before special items	(421,697)	309,027	421,200
Special item-Wastewater utility reimbursement	2,850,000	-	-
Change in Net Position	2,428,303	309,027	421,200
Beginning Net Position	29,148,003	28,838,976	28,417,776
Ending Net Position	\$31,576,306	\$29,148,003	\$28,838,976

Capital Assets and Debt Administration

Capital Assets: The City's net investment in capital assets of the Wastewater System as of December 31, 2013, 2012 and 2011 amounted to \$17.2 million, \$15.1 million and \$15.3 million, respectively, (net of accumulated depreciation and related debt). This investment in capital assets includes land, buildings, improvements, construction in progress, and machinery and equipment.

Note 5 (Capital Assets) provides Wastewater System asset activity during 2013 and 2012.

Debt Administration: At the end of 2013, the City had three outstanding long-term revenue bond issues, the 2005 Wastewater System Revenue Bond totaling \$14,920,000, the 2009 Wastewater System Revenue Bonds totaling \$12,590,000 and the 2011 Wastewater System Revenue Bonds totaling \$28,530,000.

See Note 6 for a discussion of the outstanding Wastewater System bonds and related activity.

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2013 and 2012
Unaudited

Economic Factors and Future Trends

Wastewater customer classes include residential, commercial, industrial and large contract customers. The Wastewater System serves the entire City and certain adjacent areas and accounts for 99% of the wastewater treatment services within the corporate limits of the City.

Wastewater rates, as with the other City utility rates, are established by City ordinance and are not subject to the regulatory jurisdiction of the Public Utilities Commission of Ohio (PUCO) or any Federal or State regulatory body. In 2008, City Council approved a rate ordinance providing for a series of five rate increase of 5.1%, with the first increase effective February 1, 2008, and each subsequent increase, thereafter, effective January 1, for years 2009 through 2012. The City has a single rate schedule, applicable to all wastewater customers in the City, with the exception of customers that have separate agreements. At this time, there are no active separate agreements in place. The rate schedule provides for a basic billing charge; a service charge based on flow or volume of usage; a surcharge for Biochemical Oxygen Demand (BOD) in excess of 200 milligrams per liter (mg/l); and a surcharge for Suspended Solids (SS) in excess of 300 mg/l. The surcharge tolerance for SS were increased, effective July 1, 2012, from SS in excess of 250 mg/l to 300 mg/l, to more accurately reflect the cost of treatment. As with the other City utilities, there is a suburban surcharge (150%) levied on wastewater customers located outside the corporate limits of Hamilton.

The annual budget of the Wastewater System is adopted in accordance with ten-year projections developed by a rate consultant. These projects are thoroughly reviewed and updated in the Spring and Fall of each year or more often as deemed necessary by City Management.

In January 2007, the City and the Ohio EPA entered into a Modified Consent Order to address the remaining Ohio EPA issues with the Wastewater System. This Modified Consent Order required a number of reports to be filed with the Ohio EPA, including a Management, Operation and Maintenance (MOM) Report of the sanitary sewer system; an audit of the MOM Report, one year later; an Overflow Emergency Response Plan (OERP); and a System Evaluation and Capacity Assurance Plan (SECAP), with an implementation schedule. The Modified Consent Order also regulated the reporting of overflow and bypass monitoring. The City has received Ohio EPA approval of the required submitted reports and programs. In a letter dated July 11, 2009, the SECAP was approved by the Ohio EPA Director as adequate and complete. The SECAP document serves as the master plan of capital improvements to the Wastewater System to satisfy the Modified Consent Order. In 2012, a Preliminary Engineering Report, detailing changes to the SECAP, was submitted to the Ohio EPA. The changes to the SECAP were due primarily to the closure of the two paper mills in Hamilton and subsequent significant reduction in wastewater flow. The Report detailed the changes and modifications recommended for the Water Reclamation Facility and Interceptor Improvement Projects. The Report also requested a one-year extension of the completion date for these Projects, to October 1, 2015. The Ohio EPA approved the changes to the SECAP detailed in the Report.

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2013 and 2012
Unaudited

During 2013, the Wastewater System began construction of the improvements identified within the approved SECAP, including the construction of a sewer overflow interceptor along the Great Miami River. The interceptor project was bid in 2013, with an accepted bid of approximately \$12 million. It is expected to be completed in 2014. Additionally, significant improvements were required at the Water Reclamation Facility to meet the requirements of the SECAP. Phase I of these improvements began in 2011, and totaled almost \$5.1 million. Phase II of these improvements will begin in 2014, and is estimated to cost approximately \$6.5 million.

The City maintains an A1 bond rating with a stable outlook for its Wastewater System.

Requests for Information

This financial report is designed to provide our citizens, customers, taxpayers, creditors, investors and elected officials with an overview of the City of Hamilton, Ohio's Wastewater System's finances and to show accountability for the money the system receives. If you have any questions about this report or need additional information, contact the City of Hamilton Finance Department, 345 High Street, Hamilton, Ohio 45011, (513) 785-7170, or visit the City website at www.hamilton-city.org.

CITY OF HAMILTON, OHIO – WASTEWATER SYSTEM
STATEMENTS OF NET POSITION
DECEMBER 31, 2013 AND 2012

	<u>2013</u>	<u>2012</u>
ASSETS		
Current assets:		
Cash and investments	\$ 34,205,832	35,533,363
Accounts receivable (less allowance for uncollectible accounts of \$973,893 and \$1,017,896, respectively)	1,731,891	1,534,588
Interest receivable	17,271	3,010
Inventory of supplies at cost	3,058	1,647
Prepaid expenses	<u>89,589</u>	<u>82,570</u>
Total current assets	<u>36,047,641</u>	<u>37,155,178</u>
Restricted assets:		
Cash and investments	<u>6,019,038</u>	<u>6,061,623</u>
Capital assets:		
Property, plant and equipment	100,264,463	94,971,888
Construction in progress	10,267,917	10,107,471
Accumulated depreciation	<u>(61,574,691)</u>	<u>(58,980,566)</u>
Total capital assets	<u>48,957,689</u>	<u>46,098,793</u>
Total assets	<u>91,024,368</u>	<u>89,315,594</u>
DEFERRED OUTFLOW OF RESOURCES		
Deferred charge on debt refunding	<u>426,124</u>	<u>509,338</u>
LIABILITIES		
Current liabilities:		
Accounts payable	1,760,628	549,403
Accrued wages and benefits	105,208	88,139
Intergovernmental payable	25,240	33,825
Accrued interest payable	689,832	710,141
Customer deposits payable	162,246	154,254
Compensated absences payable - current portion	199,633	161,166
OWDA loans payable - current portion	17,211	16,665
Revenue bonds payable - current portion	<u>2,125,000</u>	<u>2,045,000</u>
Total current liabilities	<u>5,084,998</u>	<u>3,758,593</u>
Non-current liabilities:		
Compensated absences payable	273,304	195,275
OWDA loans payable	366,201	383,412
Revenue bonds payable	<u>54,149,683</u>	<u>56,339,649</u>
Total noncurrent liabilities	<u>54,789,188</u>	<u>56,918,336</u>
Total liabilities	<u>59,874,186</u>	<u>60,676,929</u>
NET POSITION		
Net investment in capital assets	17,207,151	15,122,814
Restricted for debt service	4,019,038	4,061,623
Restricted for rate stabilization	2,000,000	2,000,000
Unrestricted	<u>8,350,117</u>	<u>7,963,566</u>
Total net position	<u>\$ 31,576,306</u>	<u>29,148,003</u>

See notes to financial statements.

CITY OF HAMILTON, OHIO - WASTEWATER SYSTEM
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
YEARS ENDED DECEMBER 31, 2013 AND 2012

	<u>2013</u>	<u>2012</u>
Operating revenues:		
Charges for services	\$ 11,758,165	12,046,230
Other operating revenues	<u>21,814</u>	<u>21,926</u>
Total operating revenues	<u>11,779,979</u>	<u>12,068,156</u>
Operating expenses:		
Personal services	2,501,316	2,361,732
Materials and supplies	377,865	484,596
Contractual services	2,238,756	2,441,842
Depreciation	2,617,389	2,288,196
Other operating expenses	<u>1,950,858</u>	<u>1,700,334</u>
Total operating expenses	<u>9,686,184</u>	<u>9,276,700</u>
Operating income	2,093,795	2,791,456
Non-operating revenues (expenses):		
Investment earnings	54,700	113,498
Interest and fiscal charges	<u>(2,570,192)</u>	<u>(2,595,927)</u>
Total non-operating revenues (expenses)	<u>(2,515,492)</u>	<u>(2,482,429)</u>
Income (loss) before special items	(421,697)	309,027
Special items:		
Special item - Wastewater utility reimbursement	<u>2,850,000</u>	<u>-</u>
Change in net position	2,428,303	309,027
Net position - beginning of year	<u>29,148,003</u>	<u>28,838,976</u>
Net position - end of year	\$ <u>31,576,306</u>	<u>29,148,003</u>

See notes to financial statements.

CITY OF HAMILTON, OHIO - WASTEWATER SYSTEM
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2013 AND 2012

	<u>2013</u>	<u>2012</u>
Cash flows from operating activities:		
Cash received from customers	\$ 14,440,668	12,398,666
Cash paid for employee services and benefits	(2,378,023)	(2,441,886)
Cash paid to suppliers for goods and services	<u>(4,562,868)</u>	<u>(4,637,136)</u>
Net cash provided by operating activities	<u>7,499,777</u>	<u>5,319,644</u>
Cash flows from capital and related financing activities:		
Payments for capital acquisitions	(4,276,414)	(5,960,896)
Debt principal payments	(2,061,665)	(2,011,136)
Debt interest payments and fiscal charges	<u>(2,572,253)</u>	<u>(2,605,047)</u>
Net cash used by capital and related financing activities	<u>(8,910,332)</u>	<u>(10,577,079)</u>
Cash flows from investing activities:		
Interest from investments	<u>40,439</u>	<u>121,750</u>
Net change in cash and investments	(1,370,116)	(5,135,685)
Cash and investments at beginning of year	<u>41,594,986</u>	<u>46,730,671</u>
Cash and investments at end of year	\$ <u><u>40,224,870</u></u>	<u><u>41,594,986</u></u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 2,093,795	2,791,456
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	2,617,389	2,288,196
Non-Operating revenue	2,850,000	-
Changes in assets and liabilities:		
(Increase) decrease in receivables	(197,303)	311,188
(Increase) decrease in inventory	(1,411)	(19)
(Increase) decrease in prepaid items	(7,019)	42,093
Increase (decrease) in customer deposits payable	7,992	19,322
Increase (decrease) in payables	11,354	(50,509)
Increase (decrease) in accrued liabilities	133,565	(62,450)
Increase (decrease) in intergovernmental payables	<u>(8,585)</u>	<u>(19,633)</u>
Net cash provided by operating activities	\$ <u><u>7,499,777</u></u>	<u><u>5,319,644</u></u>
Schedule of noncash activities:		
Outstanding liabilities for purchase of certain capital assets	\$ 1,586,572	386,701
Change in fair value of investments	52,456	696

See notes to financial statements.

CITY OF HAMILTON, OHIO – WASTEWATER SYSTEM

Notes to Financial Statements Years Ended December 31, 2013 and 2012

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Reporting Entity – The City of Hamilton, Ohio – Wastewater System (Wastewater System) is a utility operating as a separate enterprise fund of the City of Hamilton, Ohio (City). The Wastewater System is controlled by and is dependent on the City’s executive and legislative branches. Control by or dependence on the City is determined on the basis of outstanding debt secured by revenues or general obligations of the City, obligation of the City to finance any deficits that may occur, or receipt of subsidies from the City.

Measurement Focus, Basis of Accounting and Basis of Presentation – The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of cash flows.

Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Wastewater System’s principal ongoing operations. The principal operating revenues are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting these definitions are reported as non-operating revenues and expenses.

Income Taxes – The Wastewater System, which is owned and operated by the City, is exempt from income taxes since it is a division of a municipality.

Cash and Investments – Certain Wastewater System cash and investments are held in the City Treasury and pooled for investment management purposes. The portion of these pooled funds owned by the Wastewater System is reported as cash and investments. The Wastewater System’s investments are stated at fair value. Interest earned on funds invested is distributed on the basis of the relationship of the average monthly balance of all funds, including the Wastewater System.

Inventories – Inventories are stated at the lower of cost or market based on a moving-average cost method.

Capital Assets – Expenditures that increase values or extend the useful life of the respective assets are capitalized while the costs of maintenance and repairs are charged to operating expenses. Interest costs related to the construction of property, plant and equipment are capitalized. Depreciation is calculated on a straight-line basis over the estimated useful life of the various classes of assets. The range of useful lives for computing depreciation is 3 to 75 years.

Bond Premiums and Discounts – Unamortized bond premiums and discounts are amortized on the interest method over the term of the related bonds. Amortization of bond premiums was \$94,528 and \$103,463 in 2013 and 2012, respectively. Amortization of bond discounts was \$29,562 in 2013 and \$19,916 in 2012.

Compensated Absences – The Wastewater System follows the provisions of GASB Statement No. 16, “Accounting for Compensated Absences”. Vacation and compensatory time benefits are accrued as a liability as the benefits are earned if the employees’ rights to receive compensation are attributable to services already rendered and it is probable that the Wastewater System will compensate the employees for the benefits through paid time off or some other means. Sick leave termination benefits are accrued using the vesting method. The liability includes the employees who are currently eligible to receive termination benefits and those employees for whom it is probable that they will become eligible to receive payment in the future. The amount is based on accumulated sick leave and employees’ wage rates at year-end.

Deferred Outflows of Resources – In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement reporting element, *deferred outflows of resources*, 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 Wastewater System only has one item that qualifies for reporting in this category. It is the deferred charge on refunding reported in the statements of net position. A deferred charge on refunding 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.

Net Position – Net position represents the difference between assets, liabilities, and deferred outflows of resources. Net position invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction, or improvement of those assets. Net position is reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the City or through external restrictions imposed by creditors, grantors or laws or regulations of other governments. The Wastewater System applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net position is available.

Special Items – Special items are transactions or events that are within the control of the City and that are either unusual in nature or infrequent in occurrence. In 2013, the Wastewater System reported a Special Item, which was a payment received from the International Paper Company. A prior agreement between the City and International Paper Company required the Company or its successor to reimburse the City for costs incurred by the City if the agreement was terminated before the end of 2022. When successor Smart Papers LLC ceased operations in the City in 2012, this triggered the early termination clause of the agreement, resulting in a required payment to the City from International Paper in the amount of \$2.85 million.

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 the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. CASH AND INVESTMENTS

The Wastewater System follows the practice of pooling cash and investments with the City Treasurer except for the cash and investments of certain accounts maintained by trustees. Pooled cash and investments of the Wastewater System totaled \$36,205,832 and \$37,533,363 at December 31, 2013 and 2012, respectively, and consisted of demand deposits, money market funds, U.S. government agency securities and STAR Ohio. Cash and investments held by trustees were \$4,019,038 and \$4,061,623 as of December 31, 2013 and 2012, respectively.

Star Ohio is an investment pool managed by the State Treasurer's Office, which allows governments within the State to pool their funds for investment purposes. STAR Ohio is not registered with the SEC as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in STAR Ohio are valued at STAR Ohio's share price, which is the price the investment could be sold for on December 31, 2013.

Deposits – Custodial credit risk is the risk that in the event of a bank failure, the City's deposits may not be returned to it. The City does not have a custodial risk policy. As of December 31, 2013 and 2012, approximately 98% of the City's deposits with financial institutions, including the amount of pooled deposits related to the Wastewater System, were exposed to custodial credit risk because they are considered uninsured and uncollateralized. However, the State of Ohio has established by statute a collateral pooling system for financial institutions acting as public depositories. Public depositories must pledge qualified securities with fair values greater than the total amount of all public deposits to be secured by the collateral pool. This pooled collateral covers the Wastewater System's uninsured and uncollateralized deposits.

Investments – The State of Ohio statutes, Wastewater Revenue Bond indentures, and the City Charter authorize the City to invest in obligations of the U.S. Treasury, agencies, instrumentalities, and repurchase agreements. Custodial credit risk in regards to investments is the risk that, in the event of a failure of a counter party, the City will not be able to recover the value of its investments or collateral securities that are in possession of an outside party. The City employs the use of "safekeeping" accounts to hold and maintain custody of its investments as identified within this policy and as means of mitigating this risk.

Interest rate risk is the risk that the City will incur fair value losses arising from rising interest rates. Such risk is mitigated by the investment policy by limiting investments to certain maximum maturities. As a rule, unless specified otherwise within the policy, investments are to have a maximum maturity of five years unless the investment is matched to a specific expenditure. The context of a specific investment purchase must be weighed in proportion to the remainder of the existing investment portfolio and the "prudent investor" rule to attempt to limit such risk.

The City's pooled investments, as well as the investments held by trustees specifically for the Wastewater System, are invested primarily in U.S. governmental agency securities with a credit rating of AA+ and an average maximum maturity of 4.36 years and STAR Ohio which has a credit rating of AAAm.

3. ACCOUNTS RECEIVABLE

Receivables at December 31, 2013 and 2012 consist of the following:

	<u>2013</u>	<u>2012</u>
Earned and unbilled consumer accounts	\$ 843,212	655,151
Earned and billed consumer accounts	1,862,572	1,897,333
Less allowance for uncollectible accounts	<u>(973,893)</u>	<u>(1,017,896)</u>
Total	\$ <u>1,731,891</u>	<u>1,534,588</u>

4. RESTRICTED ASSETS

Restricted assets consist of assets whose use has been restricted by bond indenture for debt service and rate stabilization. Restricted assets were \$6,019,038 and \$6,061,623 at December 31, 2013 and 2012, respectively.

5. CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2013 and 2012 was as follows:

	Balance			Balance
	1/1/13	Increases	Decreases	12/31/13
<i>Nondepreciable capital assets:</i>				
Land	\$ 2,863,793	-	-	2,863,793
Construction in progress	<u>10,107,471</u>	<u>4,780,481</u>	<u>(4,620,035)</u>	<u>10,267,917</u>
Subtotal	<u>12,971,264</u>	<u>4,780,481</u>	<u>(4,620,035)</u>	<u>13,131,710</u>
<i>Capital assets being depreciated:</i>				
Buildings and improvements	55,733,797	1,629,076	-	57,362,873
Machinery and equipment	<u>36,374,298</u>	<u>3,686,763</u>	<u>(23,264)</u>	<u>40,037,797</u>
Subtotal	<u>92,108,095</u>	<u>5,315,839</u>	<u>(23,264)</u>	<u>97,400,670</u>
Totals at historical cost	<u>105,079,359</u>	<u>10,096,320</u>	<u>(4,643,299)</u>	<u>110,532,380</u>
Less accumulated depreciation:				
Buildings and improvements	37,131,546	734,781	-	37,866,327
Machinery and equipment	<u>21,849,020</u>	<u>1,882,608</u>	<u>(23,264)</u>	<u>23,708,364</u>
Total accumulated depreciation	<u>58,980,566</u>	<u>2,617,389</u>	<u>(23,264)</u>	<u>61,574,691</u>
Capital assets, net	\$ <u>46,098,793</u>	<u>7,478,931</u>	<u>(4,620,035)</u>	<u>48,957,689</u>

	Balance 1/1/12	Increases	Decreases	Balance 12/31/12
<i>Nondepreciable capital assets:</i>				
Land	\$ 2,863,793	-	-	2,863,793
Construction in progress	4,274,201	5,833,270	-	10,107,471
Subtotal	<u>7,137,994</u>	<u>5,833,270</u>	<u>-</u>	<u>12,971,264</u>
<i>Capital assets being depreciated:</i>				
Buildings and improvements	55,733,797	-	-	55,733,797
Machinery and equipment	36,358,643	19,528	(3,873)	36,374,298
Subtotal	<u>92,092,440</u>	<u>19,528</u>	<u>(3,873)</u>	<u>92,108,095</u>
Totals at historical cost	<u>99,230,434</u>	<u>5,852,798</u>	<u>(3,873)</u>	<u>105,079,359</u>
Less accumulated depreciation:				
Buildings and improvements	36,412,396	719,150	-	37,131,546
Machinery and equipment	20,283,847	1,569,046	(3,873)	21,849,020
Total accumulated depreciation	<u>56,696,243</u>	<u>2,288,196</u>	<u>(3,873)</u>	<u>58,980,566</u>
Capital assets, net	\$ <u>42,534,191</u>	<u>3,564,602</u>	<u>-</u>	<u>46,098,793</u>

6. LONG TERM DEBT

During 2005, the City issued Wastewater System Revenue Refunding Bonds in the amount of \$25,070,000 to provide resources to refund the 1996 and 1998 Wastewater Revenue Bonds outstanding.

On September 9, 2009, the City issued \$2,125,000 in Series 2009A Wastewater System Revenue Bonds and \$11,465,000 in Series 2009B Taxable Wastewater System Build America Revenue Bonds to currently refund bond anticipation notes and provide funding for Wastewater System overflow mitigation and treatment enhancements. With the issuance of the Build America Bonds, the City will be entitled to receive an interest subsidy payment of 35% from the U.S. Treasury on any interest payment date. The Series 2009A revenue bonds fully mature in 2017 with interest from 2.25% to 3.375% per annum. The Series 2009B Build America Bonds fully mature in 2039 with interest ranging from 6.11% to 6.62% per annum.

On October 5, 2011, the City issued \$29,620,000 in Series 2011 Wastewater System Revenue Bonds to finance the Overflow Mitigation Project. The Series 2011 revenue bonds fully mature in 2041 with interest ranging from 2.00% to 5.00% per annum.

Debt activity for the year ended December 31, 2013 was as follows:

	Balance 1/1/13	Additions	Reductions	Balance 12/31/13	Due Within One Year
2005 Refunding Bonds	\$ 16,155,000	-	(1,235,000)	14,920,000	1,295,000
Series 2009A Revenue Bonds	1,390,000	-	(265,000)	1,125,000	275,000
Series 2009B Revenue BABs	11,465,000	-	-	11,465,000	-
Series 2011 Revenue Bonds	29,075,000	-	(545,000)	28,530,000	555,000
Less deferred amount					
for issuance premiums	587,649	-	(94,528)	493,121	-
for issuance discounts	(288,000)	-	29,562	(258,438)	-
OWDA loan	400,077	-	(16,665)	383,412	17,211
Total bonds	\$ <u>58,784,726</u>	<u>-</u>	<u>(2,126,631)</u>	<u>56,658,095</u>	<u>2,142,211</u>

Debt activity for the year ended December 31, 2012 was as follows:

	Balance 1/1/12	Additions	Reductions	Balance 12/31/12	Due Within One Year
2005 Refunding Bonds	\$ 17,340,000	-	(1,185,000)	16,155,000	1,235,000
Series 2009A Revenue Bonds	1,655,000	-	(265,000)	1,390,000	265,000
Series 2009B Revenue BABs	11,465,000	-	-	11,465,000	-
Series 2011 Revenue Bonds	29,620,000	-	(545,000)	29,075,000	545,000
Less deferred amount					
for issuance premiums	691,112	-	(103,463)	587,649	-
for issuance discounts	(307,916)	-	19,916	(288,000)	-
OWDA loan	416,213	-	(16,136)	400,077	16,665
Total bonds	\$ <u>60,879,409</u>	<u>-</u>	<u>(2,094,683)</u>	<u>58,784,726</u>	<u>2,061,665</u>

All property and revenue of the Wastewater System facilities have been pledged as collateral on the indebtedness. Under the terms of the revenue bond indenture, the City has agreed to certain covenants including, among other things, maintaining revenue levels and providing for operating expenses and debt service. The Mortgage Revenue Bonds are insured under a municipal bond insurance policy. Under the terms of this policy, the payments of principal and interest are guaranteed by the insurer. Maturities of mortgage revenue bonds at December 31, 2013 are as follows:

		<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014	\$	2,125,000	2,727,096	4,852,096
2015		2,200,000	2,644,371	4,844,371
2016		2,300,000	2,546,321	4,846,321
2017		2,390,000	2,451,046	4,841,046
2018		2,560,000	2,349,008	4,909,008
2019-2023		13,120,000	9,841,298	22,961,298
2024-2028		6,395,000	7,508,987	13,903,987
2029-2033		8,290,000	5,775,201	14,065,201
2034-2038		10,780,000	3,268,657	14,048,657
2039-2041		<u>5,880,000</u>	<u>527,530</u>	<u>6,407,530</u>
Total	\$	<u>56,040,000</u>	<u>39,639,515</u>	<u>95,679,515</u>

In 2010, the City entered into an agreement with the Ohio Water Development Authority (OWDA), as administrator for the U. S. Environmental Protection Agency (EPA), for the City to receive a loan for sanitary sewer improvements. The total amount loaned was \$431,837. The interest rate on the loan is 3.25%, per annum. This loan is payable from wastewater utility charges and is received by the City in increments as the project is completed.

The future financing requirements on the loan balance at December 31, 2013 was:

		<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014	\$	17,211	12,322	29,533
2015		17,775	11,759	29,534
2016		18,358	11,176	29,534
2017		18,959	10,575	29,534
2018		19,580	9,954	29,534
2019-2023		107,953	39,713	147,666
2024-2028		126,833	20,830	147,663
2029-2030		<u>56,743</u>	<u>2,323</u>	<u>59,066</u>
Total	\$	<u>383,412</u>	<u>118,652</u>	<u>502,064</u>

7. **DEFINED BENEFIT PENSION PLANS AND OTHER POSTEMPLOYMENT BENEFITS**

The Wastewater System contributes to the Ohio Public Employees Retirement System, the City of Hamilton Metropolitan Pension Plan, and post-employment life insurance.

Ohio Public Employees Retirement System (OPERS)

The OPERS administers three separate pension plans:

- The Traditional Pension Plan – a cost-sharing multiple-employer defined benefit pension plan.

- The Member-Directed Plan – a defined contribution plan in which the member invests both member and employer contributions (employer contributions vest over five years at 20% per year). Under the Member-Directed Plan, members accumulate retirement assets equal to the value of member and vested employer contributions plus any investment earnings thereon.
- The Combined Plan – a cost sharing multiple-employer defined benefit pension plan. Under the Combined Plan, employer contributions are invested by the retirement system to provide a formula retirement benefit similar in nature to the Traditional Plan benefit. Member contributions, the investment of which is self-directed by the members, accumulate retirement assets in a manner similar to the Member-Directed Plan.

OPERS provides retirement, disability, survivor and death benefits, and annual cost of living adjustments to members and of the Traditional Plan and Combined Plan. Members of the Member-Directed Plan do not qualify for ancillary benefits. The authority to establish and amend benefits is provided by state statute per Chapter 145 of the Ohio Revised Code. OPERS issues a stand-alone financial report that may be obtained by writing to the Ohio Public Employees Retirement System, 277 East Town Street, Columbus, Ohio 43215-4642.

Plan members are required to contribute 10.0% of their annual covered salary. The City was required to contribute 14.0% of covered payroll for employees. The Gas System's required contributions to OPERS for the years ended December 31, 2013, 2012, and 2011 were approximately \$235,000, \$254,000, and \$250,000 respectively, equal to the required contributions for each year.

OPERS maintains a cost-sharing multiple employer defined benefit post-employment healthcare plan, which includes a medical plan, prescription drug program and Medicare Part B premium reimbursement, to qualifying members of both the Traditional Pension and the Combined Plans. Members of the Member-Directed Plan do not qualify for ancillary benefits, including post-employment health care coverage.

In order to qualify for post-employment health care coverage, age-and-service retirees under the Traditional Pension and Combined Plans must have 10 or more years of qualifying Ohio service credit. Health care coverage for disability benefit recipients and qualified survivor benefit recipients is available. The health care coverage provided by OPERS meets the definition of an Other Post Employment Benefit (OPEB) as described in GASB Statement 45.

The Ohio Revised Code permits, but does not mandate, OPERS to provide OPEB benefits to its eligible members and beneficiaries. Authority to establish and amend benefits is provided in Chapter 145 of the Ohio Revised Code.

The Ohio Revised Code provides the statutory authority requiring public employers to fund post retirement health care coverage through their contributions to OPERS. A portion of each employer's contribution to OPERS is set aside for the funding of post retirement health care benefits. Employer contribution rates are expressed as a percentage of the covered payroll of active members. In 2013, the City contributed 14.0% of covered payroll. The Ohio Revised Code currently limits the employer contribution to a rate not to exceed 14.0% of covered payroll. Active members do not make contributions to the OPEB Plan.

The OPERS' Post Employment Health Care plan was established under, and is administrated in accordance with, Internal Revenue Code 401(h). Each year, the OPERS Retirement Board determines the portion of the employer contribution rate that will be set aside for funding of postemployment health care benefits. The portion of employer contributions allocated to health care for members in the Traditional and Combined Plans was 1.0% during calendar year 2013. The OPERS Retirement Board is also authorized to establish rules for the retiree, or their surviving beneficiaries, to pay a portion of the health care benefits provided. Payments amounts vary depending on the number of covered dependents and the coverage selected. The portion of the Wastewater System's contributions that were used to fund post employment benefits was approximately \$17,000, \$73,000 and \$71,000 for 2013, 2012, and 2011, respectively.

Changes to the health care plan were adopted by the OPERS Retirement Board on September 19, 2012, with a transition plan commencing January 1, 2014. With the recent passage of pension legislation under SB 343 and the approved health care changes, OPERS expects to be able to consistently allocate 4% of the employer contributions toward the health care fund after the end of the transition period.

Metropolitan Pension Plan

Employees of the City who were not included under the Ohio Public Employees Retirement System (OPERS) prior to May 15, 1962 and who were included under a Group Annuity Contract of the Metropolitan Life Insurance Company participate in the City of Hamilton Metropolitan Pension Plan, a single-employer defined benefit pension plan.

Upon retirement, plan participants are entitled to a supplemental retirement benefit paid by the City, equal to the difference between OPERS benefits that would have been payable to such employee had the employee been covered by OPERS during the full period of employment and actual OPERS benefits received. Benefit provisions of the plan are established and may be amended by the City Council through ordinance. All current participants in the Metropolitan Pension Plan are retired from service with the City.

For 2013, the portion of the Wastewater System's annual pension cost was \$50,028. The Wastewater System contributed 78.7%, or \$39,361, resulting in a net pension obligation of \$19,880. The net pension obligation for the prior year was \$9,213. The Wastewater System's portion of the total unfunded accrued liability at year end was \$264,613.

For 2012, the portion of the Wastewater System's annual pension cost was \$55,782. The Wastewater System contributed 83.5%, or \$46,568, resulting in a net pension obligation of \$9,213. The net pension obligation for the prior year was \$5,665. The Wastewater System's portion of the total unfunded accrued liability at year end was \$313,174.

The actuarial valuation date was December 31, 2013 and the accrued liability was calculated using the entry age normal cost method. The Metropolitan Pension Plan currently has no assets. The amortization method used was level dollar and the amortization period was 7 years.

Retiree Life Insurance

The City provides post-employment life insurance coverage through the Hartford Insurance Company. The insurance coverage provided is considered an other post-employment benefit (OPEB) as described in GASB Statement No. 45.

Eligible employees are grouped into two classes. Employees who retired prior to March 1, 1977 are eligible to receive \$2,000 in life insurance benefits. Employees who retired after March 1, 1977 are eligible to receive \$4,000 in life insurance benefits. Benefit provisions of the plan are established and may be amended by City Council through ordinance.

For 2013, the portion of the Wastewater System's annual OPEB cost was \$11,592. The Wastewater System contributed 87.1%, or \$10,093, resulting in a net OPEB obligation of \$3,115. The net OPEB obligation for the prior year was \$1,617. The Wastewater System's portion of the total unfunded accrued liability at year end was \$164,032.

For 2012, the portion of the Wastewater System's annual OPEB cost was \$11,346. The Wastewater System contributed 85.8%, or \$9,736, resulting in a net OPEB obligation of \$1,610. The net OPEB obligation for the prior year was \$1,617. The Wastewater System's portion of the total unfunded accrued liability at year end was \$164,697.

The actuarial valuation date was December 31, 2013 and the accrued liability was calculated using the entry age normal cost method. The City's post-employment life-insurance plan currently has no assets.

8. CONTINGENT LIABILITIES

Various claims and lawsuits are pending against the City involving the Wastewater System. The City believes that the ultimate disposition of such claims and lawsuits will not have a material adverse effect on the financial position of the Wastewater System.

The Ohio Environmental Protection Agency (EPA) alleged, in previous years, that sanitary sewer overflows from the City's sanitary sewer collection system were violations of the Federal Clean Water Act and analogous State law. Federal agencies have pursued similar enforcement actions nationally against public wastewater treatment systems. The City contested this action and the initial remedial measures proposed by the State. Negotiations to resolve the enforcement action through the entry of a mutually agreeable Consent Decree began in 1997. In January 2007 a proposed Consent Decree was executed with the Ohio EPA in which the City agreed to undertake certain remedial measures to eliminate and/or reduce sanitary sewer overflow occurrences. On July 11, 2009 the Ohio EPA approved a System Evaluation and Capacity Assurance Plan (SECAP) which is the master plan of capital improvements for the Consent Decree. In 2010 and 2011, three sanitary sewer projects were constructed which eliminated the sanitary sewer overflows at three locations in the sanitary sewer collection system. Beginning in 2013, an interceptor project has been in progress to mitigate sanitary sewer overflows from the last two known sanitary sewer overflow locations in the sanitary sewer collection system. In addition, construction of improvements is underway at the Water Reclamation Facility to enhance its ability to provide secondary treatment of wastewater prior to discharging into the Great Miami River. Finally, detailed engineering design and preparation of construction drawings by an engineering firm have just been initiated for increasing the capacity of the Water Reclamation Facility for compliance with the SECAP.

9. RELATED PARTY TRANSACTIONS

The Wastewater System purchases electricity from the City's Electric System. Purchases of \$494,529 and \$480,728 were made in both 2013 and 2012 from the Electric System and are included in operating expenses.

The City allocates the cost of certain administrative services. In addition, the City established internal service funds which provide services to various City departments. Charges to the Wastewater System for these services were approximately \$2,039,000 and \$1,880,000 in 2013 and 2012, respectively, and are included in other operating expenses.

10. RISK MANAGEMENT

The City is exposed to various risks of loss related to torts and liability, damage to and theft of or destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City maintains comprehensive insurance coverage, for all City departments including the Wastewater System, with private carriers for real property, building contents, vehicle, property and general liability insurance, police professional liability, and public officials errors and omissions insurance. Vehicle policies include liability coverage for bodily injury and property damage. Claim payments have not exceeded coverage in the past three years. There was no decline in the level of coverage from the prior year.

11. CONTRACTUAL COMMITMENTS

At December 31, 2013, the Wastewater System had contractual commitments in the amounts of approximately \$11,355,000 related to property, plant and equipment improvements and additions, as well as various other contract and agreements to provide or receive services related to the Wastewater System operations.

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Dave Yost • Auditor of State

CITY OF HAMILTON- WASTEWATER SYSTEM

BUTLER COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

**CERTIFIED
AUGUST 19, 2014**