

CITY OF HAMILTON, OHIO – WASTEWATER SYSTEM

Financial Statements

Years Ended December 31, 2017 and 2016

With Independent Auditors' Report



Dave Yost • Auditor of State

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

We have reviewed the *Independent Auditor's Report* of the City of Hamilton - Wastewater System, Butler County, prepared by Clark, Schaefer, Hackett & Co., for the audit period January 1, 2017 through December 31, 2017. 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 23, 2018

This page intentionally left blank.

TABLE OF CONTENTS

Independent Auditor's Report	1 - 2
Management's Discussion and Analysis.....	3 - 9
Financial Statements:	
Statements of Net Position	10
Statements of Revenues, Expenses and Changes in Net Position	11
Statements of Cash Flows.....	12
Notes to Financial Statements.....	13 – 30
Required Supplementary Information:	
Schedule of the Proportionate Share of the Net Pension Liability	31
Schedule of Contributions.....	31

This page intentionally left blank.

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 years ended December 31, 2017 and 2016 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the 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 previously present fairly, in all material respects, the financial position of the City of Hamilton, Ohio - Wastewater System as of December 31, 2017 and 2016, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

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, 2017 and 2016, 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 and schedules of net pension liability and pension contributions, as listed in the table of contents, 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 25, 2018

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2017 and 2016
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, 2017 and 2016. 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 2017 and 2016 are as follows:

- The assets and deferred outflows of resources of the Hamilton Wastewater System exceed its liabilities and deferred inflows of resources at the close of 2017 by \$28,644,555 and \$29,222,510 at the close of 2016 (net position). Of these amounts, \$11,981,383 and \$12,540,894 (unrestricted net position) can be used to meet the System's ongoing obligations to customers and creditors.
- The System's total net position decreased by \$577,955 between 2017 and 2016, representing a 2% decrease.
- In 2017, the Wastewater System's long-term debt, net of premiums and discounts, decreased by \$2,337,594 due to meeting debt service requirements and bond refunding.

Wastewater System Summary

The City of Hamilton, Ohio owns and operates the Wastewater System, serving approximately 23,600 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 Statements of Net Position, the Statements of Revenues, Expenses and Changes in Net Position, and the Statements 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, 2017 and 2016.

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2017 and 2016
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 2017 and 2016. 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 Statements of Net Position and the Statements 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 2017 and 2016?" 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 outflows of resources exceeded liabilities and deferred inflows of resources by \$28,644,555 and \$29,222,510 as of December 31, 2017 and 2016, respectively. By far, the largest portion of the net position of the Wastewater System during 2017 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 balance increased during 2017 due to revenue bond refunding in 2017. The ratios of net investment in capital assets to total net position are as follows: 44% for 2017, 36% for 2016 and 50% for 2015. 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.

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2017 and 2016
Unaudited

Table 1 provides a summary of the Wastewater System's Statement of Net Position for the Years Ended December 31, 2017, 2016 and 2015.

	2017	2016	2015
Current and other assets	\$ 18,780,345	\$ 21,675,341	\$ 27,712,087
Capital assets	61,722,230	63,470,175	59,929,834
Total assets	<u>80,502,575</u>	<u>85,145,516</u>	<u>87,641,921</u>
Deferred outflows of resources	2,656,833	953,872	540,442
Long-term liabilities:			
Net pension liability	2,435,275	1,853,976	1,594,487
Other long-term amounts	49,799,190	51,596,307	52,467,209
Other liabilities	2,227,642	3,319,787	4,347,552
Total liabilities	<u>54,462,107</u>	<u>56,770,070</u>	<u>58,409,248</u>
Deferred inflows of resources	52,746	106,808	28,181
Net investment in capital assets	12,677,212	10,621,758	14,757,884
Restricted	3,985,960	6,059,858	6,173,856
Unrestricted	11,981,383	12,540,894	8,813,194
Total net position	<u>\$ 28,644,555</u>	<u>\$ 29,222,510</u>	<u>\$ 29,744,934</u>

During 2015, the Wastewater System adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions—an Amendment GASB Statement No. 27*, which significantly revised accounting for pension costs and liabilities. For reasons discussed below, many end users of this financial statement will gain a clearer understanding of the Wastewater System's actual financial condition by adding deferred inflows related to pension and net pension liability to the reported net position and subtracting deferred outflows related to pension.

Governmental Accounting Standards Board standards are national and apply to all government financial reports prepared in accordance with generally accepted accounting principles. When accounting for pension costs, GASB Statement No. 27 focused on a funding approach. This approach limited pension costs to contributions annually required by law, which may or may not be sufficient to fully fund each plan's *net pension liability*. GASB Statement No. 68 takes an earnings approach to pension accounting; however, the nature of Ohio's statewide pension systems and state law governing those systems requires additional explanation in order to properly understand the information presented in these statements.

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2017 and 2016
Unaudited

Under GASB Statement No. 68, the net pension liability equals the City's proportionate share of each plan's collective:

1. Present value of estimated future pension benefits attributable to active and inactive employees' past service
2. Minus plan assets available to pay these benefits

GASB notes that pension obligations, whether funded or unfunded, are part of the "employment exchange" – that is, the employee is trading his or her labor in exchange for wages, benefits, and the promise of a future pension. GASB noted that the unfunded portion of this pension promise is a present obligation of the government, part of a bargained-for benefit to the employee, and should accordingly be reported by the government as a liability since they received the benefit of the exchange. However, the City is not responsible for certain key factors affecting the balance of this liability. In Ohio, the employee shares the obligation of funding pension benefits with the employer. Both the employer and employee contribution rates are capped by State statute. A change in these caps requires action of both Houses of the General Assembly and approval of the Governor. Benefit provisions are also determined by State statute. The employee enters the employment exchange with the knowledge that the employer's promise is limited not by contract, but by law. The employer enters the exchange also knowing that there is a specific, legal limit to its contribution to the pension system. In Ohio, there is no legal means to enforce the unfunded liability of the pension system *as against the public employer*. State law operates to mitigate/lessen the moral obligation of the public employer to the employee, because all parties enter the employment exchange with notice as to the law. The pension system is responsible for the administration of the plan.

Most long-term liabilities have set repayment schedules or, in the case of compensated absences (i.e., sick and vacation leave), are satisfied through paid time-off or termination payments. There is no repayment schedule for the net pension liability. As explained above, changes in pension benefits, contribution rates, and return on investments affect the balance of the net pension liability, but are outside the control of the local government. In the event that contributions, investment returns, and other changes are insufficient to keep up with the required pension payments, State statute does not assign/identify the responsible party for the unfunded portion. Due to the unique nature of how the net pension liability is satisfied, this liability is separately identified within the long-term liability section of the statement of net position.

In accordance with GASB Statement No. 68, the Wastewater System's statements prepared on an accrual basis of accounting include an annual pension expense for their proportionate share of each plan's *change* in net pension liability not accounted for as deferred inflows/outflows.

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2017 and 2016
Unaudited

As of December 31, 2017, 2016 and 2015, the Wastewater System is able to report positive balances in net position. The overall changes in net position were decreases of \$577,955 in 2017, \$522,424 in 2016 and \$105,620 in 2015. Operating revenues decreased slightly by \$16,640, while operating expenses increased by \$932,622 due to increases in the change in net pension liability and increases in wage expense due to new employment agreements.

Net non-operating expenses of \$1.3 million decreased by \$893,731, primarily due to a decrease in interest and fiscal charges, with the refunding of the Series 2011 Revenue bonds and increased use of interest-free OPWC loans.

	2017	2016	2015
Operating revenues	\$ 12,368,579	\$ 12,385,219	\$ 11,821,865
Operating expenses:			
Depreciation	3,563,726	3,529,973	2,652,857
Other operating expenses	8,054,016	7,155,147	6,816,788
Total operating expenses	<u>11,617,742</u>	<u>10,685,120</u>	<u>9,469,645</u>
Operating income	750,837	1,700,099	2,352,220
Non-Operating revenues (expenses)			
Interest and fiscal charges	(1,720,118)	(2,547,784)	(2,421,995)
Loss on disposal of capital assets	(22,137)	-	(173,737)
Other non-operating revenues	413,463	325,261	128,227
Total non-operating revenues (expenses)	<u>(1,328,792)</u>	<u>(2,222,523)</u>	<u>(2,467,505)</u>
Transfers	<u>-</u>	<u>-</u>	<u>9,665</u>
Change in net position	(577,955)	(522,424)	(105,620)
Beginning net position	29,222,510	29,744,934	29,850,554
Ending net position	<u>\$ 28,644,555</u>	<u>\$ 29,222,510</u>	<u>\$ 29,744,934</u>

Capital Assets and Debt Administration

Capital Assets: The City's net investment in capital assets of the Wastewater System as of December 31, 2017, 2016 and 2015 amounted to \$12.7 million, \$10.6 million, and \$14.8 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 2017.

Debt Administration: At the end of 2017, the City had two outstanding long-term revenue bond issues, the 2009 Wastewater System Revenue Bonds totaling \$11,465,000 and the 2016 Wastewater System Revenue Refunding Bonds of \$8,715,000.

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2017 and 2016
Unaudited

In 2017, the Wastewater System refunded \$26,220,000 in Series 2009A revenue bonds with the issuance of \$25,445,000 in notes maturing in March 2018.

Also during 2017, the Wastewater System received a State agency loan for sanitary sewer improvements.

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

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 2016, City Council approved a rate ordinance providing for a series of five rate increases of approximately 3% annually, with the first increase effective August 1, 2016, and each subsequent increase, thereafter, effective July 1, for years 2017 through 2020. The City has a single rate schedule, applicable to all wastewater customers in the City, with the exception of customers that have separate agreements. The rate schedule provides for a basic billing charge; a capacity charge based on the water meter size; 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.

City of Hamilton, Ohio

Wastewater System

Management's Discussion and Analysis
For the Years Ended December 31, 2017 and 2016
Unaudited

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.

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. This was completed in 2015. 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 began in 2014, and is estimated to cost approximately \$6.5 million. All requirements of the SECAP were completed in 2016.

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, 2017 AND 2016**

	<u>2017</u>	<u>2016</u>
ASSETS		
Current assets:		
Cash and investments	\$ 13,039,470	13,873,418
Accounts receivable (less allowance for uncollectible accounts of \$1,141,492 and \$1,193,205)	1,598,213	1,588,261
Interest receivable	39,626	41,927
Inventory of supplies at cost	1,176	649
Prepaid expenses	115,900	111,228
Total current assets	<u>14,794,385</u>	<u>15,615,483</u>
Restricted assets:		
Cash and investments	<u>3,985,960</u>	<u>6,059,858</u>
Noncurrent assets:		
Nondepreciable capital assets	9,060,603	10,343,079
Depreciable capital assets, net	<u>52,661,627</u>	<u>53,127,096</u>
Total noncurrent assets	<u>61,722,230</u>	<u>63,470,175</u>
Total assets	<u>80,502,575</u>	<u>85,145,516</u>
DEFERRED OUTFLOWS OF RESOURCES		
Deferred charge on debt refunding	1,707,078	241,273
Pension	949,755	712,599
Total deferred outflows of resources	<u>2,656,833</u>	<u>953,872</u>
LIABILITIES		
Current liabilities:		
Accounts payable	267,089	434,417
Accrued wages and benefits	46,604	111,436
Intergovernmental payable	5,710	4,901
Accrued interest payable	301,537	650,726
Customer deposits payable	277,652	252,190
Compensated absences payable - current portion	199,470	181,850
OWDA loans payable - current portion	19,580	19,267
Revenue bonds payable - current portion	1,110,000	1,665,000
Total current liabilities	<u>2,227,642</u>	<u>3,319,787</u>
Non-current liabilities:		
Compensated absences payable	169,772	183,982
OWDA loans payable	291,531	301,400
OPWC loans payable	3,518,021	3,242,422
General obligation notes payable	25,445,000	-
Revenue bonds payable	20,374,866	47,868,503
Net pension liability	2,435,275	1,853,976
Total noncurrent liabilities	<u>52,234,465</u>	<u>53,450,283</u>
Total liabilities	<u>54,462,107</u>	<u>56,770,070</u>
DEFERRED INFLOWS OF RESOURCES		
Pension	<u>52,746</u>	<u>106,808</u>
NET POSITION		
Net investment in capital assets	12,677,212	10,621,758
Restricted for debt service	1,985,960	4,059,858
Restricted for rate stabilization	2,000,000	2,000,000
Unrestricted	<u>11,981,383</u>	<u>12,540,894</u>
Total net position	<u>\$ 28,644,555</u>	<u>29,222,510</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, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
Operating revenues:		
Charges for services	\$ 12,346,330	12,384,393
Other operating revenues	<u>22,249</u>	<u>826</u>
Total operating revenues	<u>12,368,579</u>	<u>12,385,219</u>
Operating expenses:		
Personal services	2,557,137	1,973,944
Materials and supplies	302,621	332,908
Contractual services	2,549,669	2,442,263
Depreciation	3,563,726	3,529,973
Other operating expenses	<u>2,644,589</u>	<u>2,406,032</u>
Total operating expenses	<u>11,617,742</u>	<u>10,685,120</u>
Operating income	750,837	1,700,099
Non-operating revenues (expenses):		
Investment earnings	173,322	85,247
Grants	240,141	240,014
Loss on disposal of capital assets	(22,137)	-
Interest and fiscal charges	<u>(1,720,118)</u>	<u>(2,547,784)</u>
Total non-operating revenues (expenses)	<u>(1,328,792)</u>	<u>(2,222,523)</u>
Change in net position	(577,955)	(522,424)
Net position - beginning of year	<u>29,222,510</u>	<u>29,744,934</u>
Net position - end of year	\$ <u><u>28,644,555</u></u>	<u><u>29,222,510</u></u>

See notes to financial statements.

**CITY OF HAMILTON, OHIO - WASTEWATER SYSTEM
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2017 AND 2016**

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities:		
Cash received from customers	\$ 12,358,627	12,219,294
Cash paid for employee services and benefits	(2,325,286)	(2,112,184)
Cash paid to suppliers for goods and services	(5,582,934)	(5,133,548)
Net cash from operating activities	<u>4,450,407</u>	<u>4,973,562</u>
Cash flows from noncapital financing activities:		
Intergovernmental grants	<u>240,141</u>	<u>240,014</u>
Cash flows from capital and related financing activities:		
Payments for capital acquisitions	(1,901,311)	(9,919,409)
Note issuance	25,445,000	-
Revenue bond proceeds	-	9,490,000
Premium on bond issuance	-	1,619,387
Revenue bond principal retirement	(27,885,000)	(13,140,000)
OPWC loan proceeds	275,599	3,242,422
OWDA loan principal retirement	(9,556)	(18,655)
Debt interest payments and fiscal charges	(3,698,749)	(2,781,447)
Net cash from capital and related financing activities	<u>(7,774,017)</u>	<u>(11,507,702)</u>
Cash flows from investing activities:		
Interest from investments and change in fair value of investments	<u>175,623</u>	<u>57,414</u>
Net change in cash and investments	(2,907,846)	(6,236,712)
Cash and investments at beginning of year	19,933,276	26,169,988
Cash and investments at end of year	\$ <u>17,025,430</u>	<u>19,933,276</u>
Reconciliation of operating income to net cash from operating activities:		
Operating income	\$ 750,837	1,700,099
Adjustments to reconcile operating income to net cash from operating activities:		
Depreciation	3,563,726	3,529,973
Change in deferred outflows-pension	(237,156)	(450,783)
Change in deferred inflows-pension	(54,062)	78,627
Changes in assets and liabilities:		
(Increase) decrease in receivables	(9,952)	(165,925)
(Increase) decrease in inventory	(527)	(18)
(Increase) decrease in prepaid items	(4,672)	(1,368)
Increase (decrease) in customer deposits payable	25,462	8,596
Increase (decrease) in payables	(103,935)	39,892
Increase (decrease) in accrued liabilities	(61,422)	(11,113)
Increase (decrease) in intergovernmental payables	809	(13,907)
Increase (decrease) in net pension liability	581,299	259,489
Net cash from operating activities	\$ <u>4,450,407</u>	<u>4,973,562</u>
Schedule of noncash activities:		
Outstanding liabilities for purchase of certain capital assets	\$ <u>180,564</u>	<u>243,957</u>

See notes to financial statements.

CITY OF HAMILTON, OHIO – WASTEWATER SYSTEM

Notes to Financial Statements Years Ended December 31, 2017 and 2016

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. In accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, and GASB Statement No. 72, *Fair Value Measurement and Application*, all investments are recorded at fair value except for nonparticipating investment contracts which are reported at amortized cost, which approximates 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 cost based on a moving-average cost method.

Capital Assets – Expenses 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 5 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 \$271,577 and \$317,822 in 2017 and 2016, respectively. Amortization of bond discounts was \$107,940 and \$57,067 in 2017 and 2016, respectively.

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.

Pension – For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the pension plans and additions to/deductions from their fiduciary net position have been determined on the same basis as they are reported by the pension system. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. The pension system reports investments at fair value.

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. For the Wastewater System, deferred outflows of resources are reported in the statement of net position for deferred charges on refunding and pension. 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. The deferred outflows of resources related to pension are explained in Note 7.

Deferred Inflows of Resources – In addition to liabilities, the statement of financial position will report a separate section for deferred inflows of resources. Deferred inflows of resources represent an acquisition of net position that applies to a future period and will not be recognized until that time. For the Wastewater System, deferred inflows of resources include pension (see Note 7).

Net Position – Net position represents the difference between assets and deferred outflows of resources, reduced by liabilities and deferred inflows 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.

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 \$15,039,470 and \$15,873,418 at December 31, 2017 and 2016, respectively, and consisted of demand deposits, money market funds, U.S. government agency securities and State Treasury Asset Reserve of Ohio (STAR Ohio). Cash and investments held by trustees were \$1,985,960 and \$4,059,858 at December 31, 2017 and 2016, 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 the net asset value (NAV) per share provided by STAR Ohio. The NAV per share is calculated on an amortized cost basis that provides a NAV per share that approximates fair value. For 2017, there were no limitations or restrictions on any participant withdrawals due to redemption notice periods, liquidity fees, or redemption gates. However, notice must be given 24 hours in advance of all deposits and withdrawals exceeding \$25 million. STAR Ohio reserves the right to limit the transaction to \$50 million, requiring the excess amount to be transacted the following business day(s), but only to the \$50 million limit. All accounts of the participant will be combined for these purposes.

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, 2017, approximately 93% 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. Fair value in U.S. Treasury securities are measured using level 1 inputs, using quoted prices in active markets for identical assets. Fair value in U.S. agency securities and commercial paper are measured using level 2 inputs, using significant other observable inputs.

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 1.96 years and STAR Ohio which has a credit rating of AAAm.

3. ACCOUNTS RECEIVABLE

Receivables at December 31, 2017 and 2016 consist of the following:

	<u>2017</u>	<u>2016</u>
Earned and unbilled consumer accounts	\$ 754,266	712,000
Earned and billed consumer accounts	1,984,867	2,069,466
Other	572	0
Less allowance for uncollectible accounts	<u>(1,141,492)</u>	<u>(1,193,205)</u>
Total	<u>\$ 1,598,213</u>	<u>1,588,261</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 \$3,985,960 and \$6,059,858 at December 31, 2017 and 2016, respectively.

5. CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2017 and 2016 was as follows:

	Balance 1/1/17	Increases	Decreases	Balance 12/31/17
<i>Nondepreciable capital assets:</i>				
Land	\$ 2,847,497	-	-	2,847,497
Construction in progress	<u>7,495,582</u>	<u>825,145</u>	<u>(2,107,621)</u>	<u>6,213,106</u>
Subtotal	<u>10,343,079</u>	<u>825,145</u>	<u>(2,107,621)</u>	<u>9,060,603</u>
<i>Capital assets being depreciated:</i>				
Buildings and improvements	80,332,751	-	-	80,332,751
Machinery and equipment	<u>42,062,421</u>	<u>3,120,394</u>	<u>(106,641)</u>	<u>45,076,174</u>
Subtotal	<u>122,395,172</u>	<u>3,120,394</u>	<u>(106,641)</u>	<u>125,408,925</u>
Totals at historical cost	<u>132,738,251</u>	<u>3,945,539</u>	<u>(2,214,262)</u>	<u>134,469,528</u>
Less accumulated depreciation:				
Buildings and improvements	40,674,866	1,088,107	-	41,762,973
Machinery and equipment	<u>28,593,210</u>	<u>2,475,619</u>	<u>(84,504)</u>	<u>30,984,325</u>
Total accumulated depreciation	<u>69,268,076</u>	<u>3,563,726</u>	<u>(84,504)</u>	<u>72,747,298</u>
Capital assets, net	<u>\$ 63,470,175</u>	<u>381,813</u>	<u>(2,129,758)</u>	<u>61,722,230</u>
	Balance 1/1/16	Increases	Decreases	Balance 12/31/16
<i>Nondepreciable capital assets:</i>				
Land	\$ 2,847,497	-	-	2,847,497
Construction in progress	<u>25,565,506</u>	<u>4,821,496</u>	<u>(22,891,420)</u>	<u>7,495,582</u>
Subtotal	<u>28,413,003</u>	<u>4,821,496</u>	<u>(22,891,420)</u>	<u>10,343,079</u>
<i>Capital assets being depreciated:</i>				
Buildings and improvements	58,052,432	22,285,664	(5,345)	80,332,751
Machinery and equipment	<u>40,080,035</u>	<u>2,854,574</u>	<u>(872,188)</u>	<u>42,062,421</u>
Subtotal	<u>98,132,467</u>	<u>25,140,238</u>	<u>(877,533)</u>	<u>122,395,172</u>
Totals at historical cost	<u>126,545,470</u>	<u>29,961,734</u>	<u>(23,768,953)</u>	<u>132,738,251</u>
Less accumulated depreciation:				
Buildings and improvements	39,599,897	1,080,314	(5,345)	40,674,866
Machinery and equipment	<u>27,015,739</u>	<u>2,449,659</u>	<u>(872,188)</u>	<u>28,593,210</u>
Total accumulated depreciation	<u>66,615,636</u>	<u>3,529,973</u>	<u>(877,533)</u>	<u>69,268,076</u>
Capital assets, net	<u>\$ 59,929,834</u>	<u>26,431,761</u>	<u>(22,891,420)</u>	<u>63,470,175</u>

6. LONG TERM DEBT

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 percent 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 percent per annum. The Series 2009B Build America Bonds fully mature in 2039 with interest ranging from 6.11 to 6.62 percent 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 percent per annum.

In October 2016, the Wastewater System refunded \$10,840,000 of Series 2005 Wastewater System Revenue Refunding Bonds. The net proceeds of the Series 2016 bonds have been used to currently refund the Series 2005 Bonds that were originally issued to refund the 1996 and 1998 Wastewater Revenue Bonds. The Wastewater System reduced its aggregate debt service payments over the life of the refunded bonds by \$1,172,361 and obtained an economic gain (difference between the present values of the old and new debt service payments) of \$1,196,228.

In December 2017, the City defeased \$26,220,000 of Wastewater System Revenue Bonds, along with portions of Electric and Water Revenue Bonds, through the issuance of \$45,220,000 of Various Purpose General Obligation Notes. The Wastewater System's portion of the 2017 Notes was \$25,445,000. The net proceeds of the 2017 Notes have been invested in obligations guaranteed as to both principal and interest by the United States and placed in irrevocable escrow accounts which, including interest earned, will be used to pay the principal and interest on the refunded bonds. The refunded bonds, which have an outstanding balance of \$26,220,000 at December 31, 2017 are not included in the Wastewater System's outstanding debt since the Wastewater System has in-substance satisfied its obligations through the advanced refunding. As a result of the issuance of the \$45,220,000 Notes, the City reduced its aggregate debt service payments over the life of the Electric, Water and Wastewater refunded bonds by \$4,118,083 and obtained an economic gain (difference between the present value of the old and new debt service payments) of \$539,762.

The \$45,220,000 in Various Purpose General Obligation Notes were retired in March 2018 with the issuance of \$43,930,000 of Revenue Refunding Bonds. See Note 12.

Debt activity for the year ended December 31, 2017 was as follows:

	Balance 1/1/17	Additions	Reductions	Balance 12/31/17	Due Within One Year
Series 2009A Revenue Bonds	\$ 290,000	-	(290,000)	-	-
Series 2009B Revenue BABs	11,465,000	-	-	11,465,000	295,000
Series 2011 Revenue Bonds	26,820,000	-	(26,820,000)	-	-
Series 2016 Revenue Bonds	9,490,000	-	(775,000)	8,715,000	815,000
Less deferred amount					
for issuance premiums	1,620,098	-	(271,577)	1,348,521	-
for issuance discounts	(151,595)	-	107,940	(43,655)	-
OWDA loan	320,667	-	(9,556)	311,111	19,580
OPWC loan	3,242,422	275,599	-	3,518,021	-
Notes payable	-	25,445,000	-	25,445,000	-
Net pension liability	1,853,976	581,299	-	2,435,275	-
Compensated absences	365,832	185,260	(181,850)	369,242	199,470
Total bonds	\$ <u>55,316,400</u>	<u>26,487,158</u>	<u>(28,240,043)</u>	<u>53,563,515</u>	<u>1,329,050</u>

Debt activity for the year ended December 31, 2016 was as follows:

	Balance 1/1/16	Additions	Reductions	Balance 12/31/16	Due Within One Year
2005 Refunding Bonds	\$ 12,270,000	-	(12,270,000)	-	-
Series 2009A Revenue Bonds	570,000	-	(280,000)	290,000	290,000
Series 2009B Revenue BABs	11,465,000	-	-	11,465,000	-
Series 2011 Revenue Bonds	27,410,000	-	(590,000)	26,820,000	600,000
Series 2016 Revenue Bonds	-	9,490,000	-	9,490,000	775,000
Less deferred amount					
for issuance premiums	318,533	1,619,387	(317,822)	1,620,098	-
for issuance discounts	(208,662)	-	57,067	(151,595)	-
OWDA loan	339,322	-	(18,655)	320,667	19,267
OPWC loan	-	3,242,422	-	3,242,422	-
Net pension liability	1,594,487	259,489	-	1,853,976	-
Claims payable	2,400,000	-	(2,400,000)	-	-
Compensated absences	408,535	144,161	(186,864)	365,832	181,850
Total bonds	\$ <u>56,567,215</u>	<u>14,755,459</u>	<u>(16,006,274)</u>	<u>55,316,400</u>	<u>1,866,117</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, 2017 are as follows:

		<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2018	\$	1,110,000	1,128,149	2,238,149
2019		1,145,000	1,085,675	2,230,675
2020		1,190,000	1,033,439	2,223,439
2021		1,245,000	970,443	2,215,443
2022		1,295,000	904,585	2,199,585
2023-2027		6,170,000	3,511,429	9,681,429
2028-2032		2,640,000	2,315,177	4,955,177
2033-2037		3,630,000	1,335,320	4,965,320
2038-2041		<u>1,755,000</u>	<u>175,430</u>	<u>1,930,430</u>
Total	\$	<u>20,180,000</u>	<u>12,459,647</u>	<u>32,639,647</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 interest rate on the loan is 3.25 percent, per annum. This loan is payable from wastewater utility charges. As of December 31, 2017, the outstanding loan balance was \$311,111.

The future financing requirements on the loan balance at December 31, 2017 was:

		<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2018	\$	19,580	9,954	29,534
2019		20,221	9,311	29,532
2020		20,884	8,649	29,533
2021		21,568	7,965	29,533
2022		22,275	7,258	29,533
2023-2027		122,810	24,855	147,665
2028-2030		<u>83,773</u>	<u>4,827</u>	<u>88,600</u>
Total	\$	<u>311,111</u>	<u>72,819</u>	<u>383,930</u>

In 2016, the Wastewater System obtained financing through the Ohio Public Works Commission (OPWC) for the Gilmore Road Pump Station with a 0 percent interest rate. This loan will be received in increments as the project is completed. As of December 31, 2017, the City had received \$3,518,021 from OPWC. Subsequent amounts will be received in future years. As of December 31, 2017, the loan had not been finalized and there is no amortization schedule yet for the loan.

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.

Net Pension Liability

The net pension liability reported on the statement of net position represents a liability to employees for pensions. Pension is a component of exchange transactions—between an employer and its employees—of salaries and benefits for employee services. Pensions are provided to an employee—on a deferred-payment basis—as part of the total compensation package offered by an employer for employee services each financial period. The obligation to sacrifice resources for pensions is a present obligation because it was created as a result of employment exchanges that already have occurred.

The net pension liability represents the Wastewater System's proportionate share of each pension plan's collective actuarial present value of projected benefit payments attributable to past periods of service, net of each pension plan's fiduciary net position. The net pension liability calculation is dependent on critical long-term variables, including estimated average life expectancies, earnings on investments, cost of living adjustments and others. While these estimates use the best information available, unknowable future events require adjusting this estimate annually.

Ohio Revised Code limits the Wastewater System's obligation for this liability to annually required payments. The Wastewater System cannot control benefit terms or the manner in which pensions are financed; however, the Wastewater System does receive the benefit of employees' services in exchange for compensation including pension.

GASB 68 assumes the liability is solely the obligation of the employer, because (1) they benefit from employee services; and (2) State statute requires all funding to come from these employers. All contributions to date have come solely from these employers (which also includes costs paid in the form of withholdings from employees). State statute requires the pension plans to amortize unfunded liabilities within 30 years. If the amortization period exceeds 30 years, each pension plan's board must propose corrective action to the State legislature. Any resulting legislative change to benefits or funding could significantly affect the net pension liability. Resulting adjustments to the net pension liability would be effective when the changes are legally enforceable.

The proportionate share of each plan's unfunded benefits is presented as a long-term *net pension liability* on the accrual basis of accounting. Any liability for the contractually-required pension contribution outstanding at the end of the year is included in *intergovernmental payable* on both the accrual and modified accrual bases of accounting.

Plan Description – Ohio Public Employees Retirement System (OPERS)

Wastewater System employees participate in the Ohio Public Employees Retirement System (OPERS). OPERS administers three separate pension plans. The traditional pension plan is a cost-sharing, multiple-employer defined benefit pension plan. The member-directed plan is a defined contribution plan and the combined plan is a cost-sharing, multiple-employer defined benefit pension plan with defined contribution features. While members (e.g. Wastewater System employees) may elect the member-directed plan and the combined plan, substantially all employee members are in OPERS' traditional plan; therefore, the following disclosure focuses on the traditional pension plan.

OPERS provides retirement, disability, survivor and death benefits, and annual cost of living adjustments to members of the traditional plan. Authority to establish and amend benefits is provided by Chapter 145 of the Ohio Revised Code. OPERS issues a stand-alone financial report that includes financial statements, required supplementary information and detailed information about OPERS' fiduciary net position that may be obtained by visiting <https://www.opers.org/financial/reports.shtml>, by writing to the Ohio Public Employees Retirement System, 277 East Town Street, Columbus, Ohio 43215-4642, or by calling 800-222-7377.

Senate Bill (SB) 343 was enacted into law with an effective date of January 7, 2013. In the legislation, members were categorized into three groups with varying provisions of the law applicable to each group. The following table provides age and service requirements for retirement and the retirement formula applied to final average salary (FAS) for the three-member groups under the traditional plan as per the reduced benefits adopted by SB 343 (see OPERS CAFR referenced above for additional information):

Group A Eligible to retire prior to January 7, 2013 or five years after January 7, 2013	Group B 20 years of service credit prior to January 7, 2013 or eligible to retire ten years after January 7, 2013	Group C Members not in other Groups and members hired on or after January 7, 2013
State and Local	State and Local	State and Local
Age and Service Requirements: Age 60 with 60 months of service credit or Age 55 with 25 years of service credit	Age and Service Requirements: Age 60 with 60 months of service credit or Age 55 with 25 years of service credit	Age and Service Requirements: Age 57 with 25 years of service credit or Age 62 with 5 years of service credit
Formula: 2.2% of FAS multiplied by year of service for the first 30 years and 2.5% for service years in excess of 30	Formula: 2.2% of FAS multiplied by year of service for the first 30 years and 2.5% for service years in excess of 30	Formula: 2.2% of FAS multiplied by year of service for the first 35 years and 2.5% for service years in excess of 35

Final average salary (FAS) represents the average of the three highest years of earnings over a member's career for Groups A and B. Group C is based on the average of the five highest years of earnings over a member's career.

Members who retire before meeting the age and years of service credit requirement for unreduced benefits receive a percentage reduction in the benefit amount.

When a benefit recipient has received benefits for 12 months, an annual cost of living adjustment (COLA) is provided. This COLA is calculated on the base retirement benefit at the date of retirement and is not compounded. For those retiring prior to January 7, 2013, the COLA will continue to be a 3 percent simple annual COLA. For those retiring subsequent to January 7, 2013, beginning in calendar year 2019, the COLA will be based on the average percentage increase in the Consumer Price Index, capped at 3 percent.

Funding Policy – The Ohio Revised Code (ORC) provides statutory authority for member and employer contributions as follows:

	<u>2017</u>	<u>2016</u>
Statutory Maximum Contribution Rates		
Employer	14.0 %	14.0 %
Employee	10.0 %	10.0 %
Actual Contribution Rates		
Employer:		
Pension	13.0 %	12.0 %
Post-employment Health Care Benefits	1.0 %	2.0 %
Total Employer	<u>14.0 %</u>	<u>14.0 %</u>
Employee	<u>10.0 %</u>	<u>10.0 %</u>

Employer contribution rates are actuarially determined and are expressed as a percentage of covered payroll. The Wastewater System's contractually required contributions were \$197,521 and \$167,646 for 2017 and 2016, respectively. Of these amounts, \$4,847 and \$4,901 were reported as intergovernmental payables in 2017 and 2016, respectively.

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

The net pension liabilities for OPERS were measured as of December 31, 2016 and 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Wastewater System's proportion of the net pension liability was based on the Wastewater System's share of contributions to the pension plan relative to the contributions of all participating entities in those measurement periods.

The following is information related to the proportionate share and pension expense:

	<u>2017</u>	<u>2016</u>
Proportionate Share of the Net Pension Liability	\$2,435,275	\$1,853,976
Proportion of the Net Pension Liability	0.0107242%	0.0107035%
Change in Proportion	0.0000207%	
Pension Expense	\$779,309	\$229,893

At December 31, 2017 and 2016, the Wastewater System reported deferred outflows of resources and deferred inflows of resources related to pension from the following sources:

	<u>2017</u>	<u>2016</u>
Deferred Outflows of Resources		
Net difference between projected and actual earnings on pension plan investments	\$ 362,667	\$ 544,953
Changes in assumptions	386,265	-
Differences between expected and actual experience	3,302	-
Wastewater System contributions subsequent to the measurement date	<u>197,521</u>	<u>167,646</u>
Total Deferred Outflows of Resources	<u>\$ 949,755</u>	<u>\$ 712,599</u>
Deferred Inflows of Resources		
Differences between expected and actual experience	\$ 14,493	\$ 41,325
Wastewater System change in proportionate share	<u>38,253</u>	<u>65,483</u>
Total Deferred Inflows of Resources	<u>\$ 52,746</u>	<u>\$ 106,808</u>

\$197,521 reported as deferred outflows of resources related to pension resulting from the Wastewater System's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending December 31, 2018. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pension will be recognized in pension expense as follows:

Year Ending December 31:		
2018	\$	271,551
2019		309,645
2020		128,911
2021		<u>(10,619)</u>
Total	\$	<u>699,488</u>

Actuarial Assumptions - OPERS

Actuarial valuations of an ongoing plan involve estimates of the values of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and cost trends. Actuarially determined amounts are subject to continual review or modification as actual results are compared with past expectations and new estimates are made about the future.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employers and plan members) and include the types of benefits provided at the time of each valuation.

In 2016, the OPERS' actuarial consultants conducted an experience study for the period 2011 through 2015, comparing assumptions to actual results. The experience study incorporates both a historical review and forward-looking projections to determine the appropriate set of assumptions to keep the plan on a path toward full funding. Information from this study led to changes in both demographic and economic assumptions, with the most notable being a reduction in the actuarially assumed rate of return from 8.0 percent down to 7.5 percent, for the defined benefit investments. The total pension liability in the December 31, 2016, actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Wage Inflation	3.25 percent
Future Salary Increases, including inflation COLA or Ad Hoc COLA	3.25 to 10.75 percent including wage inflation Pre 1/7/2013 Retirees: 3 percent, simple; Post 1/7/2013 Retirees: 3 percent simple through 2018, then 2.15 percent simple
Investment Rate of Return	7.5 percent
Actuarial Cost Method	Individual Entry Age

Mortality rates are based on the RP-2014 Healthy Annuitant mortality table. For males, Healthy Annuitant Mortality tables were used, adjusted for mortality improvement back to the observation period base of 2006 and then established the base year as 2015. For females, Healthy Annuitant Mortality tables were used, adjusted for mortality improvements back to the observation period base year of 2006 and then established the base year as 2010. The mortality rates used in evaluating disability allowances were based on the RP-2014 Disabled mortality tables, adjusted for mortality improvement back to the observation base year of 2006 and then established the base year as 2015 for males and 2010 for females. Mortality rates for a particular calendar year for both healthy and disabled retiree mortality tables are determined by applying the MP-2015 mortality improvement scale to the above described tables.

The most recent experience study was completed for the five-year period ended December 31, 2015.

The long-term rate of return on defined benefit investment assets was determined using a building-block method in which best-estimate ranges of expected future real rates of return are developed for each major asset class. These ranges are combined to produce the long-term expected real rate of return by weighting the expected future real rates of return by the target asset allocation percentage, adjusted for inflation.

During 2016, OPERS managed investments in four investment portfolios: the Defined Benefits portfolio, the 401(h) Health Care portfolio, the 115 Health Care Trust portfolio and the Defined Contribution portfolio. The 401(h) Health Care Trust was closed as of June 30, 2016. The Defined Benefit portfolio contains the investment assets of the Traditional Pension Plan, the defined benefit component of the Combined Plan, the annuitized accounts of the Member-Directed Plan. The Defined Benefit portfolio historically included the assets of the Member-Directed retiree medical accounts funded through the VEBA Trust. However, the VEBA Trust was closed as of June 30, 2016 and the net position transferred to the 115 Health Care Trust portfolio as of July 1, 2016. Within the Defined Benefit portfolio, contributions into the plans are all recorded at the same time, and benefit payments all occur on the first of the month. Accordingly, the money-weighted rate of return is considered to be the same for all plans within the portfolio. The money weighted rate of return, net of investments expense, for the Defined Benefit portfolio is 8.3 percent for 2016.

The allocation of investment assets with the Defined Benefit portfolio is approved by the Board of Trustees as outlined in the annual investment plan. Plan assets are managed on a total return basis with a long-term objective of achieving and maintaining a fully funded status for the benefits provided through the defined benefit pension plans. The table below displays the Board-approved asset allocation policy for 2016 and the long-term expected real rates of return:

Asset Class	Target Allocation	Weighted Average Long-Term Expected Real Rate of Return (Arithmetic)
Fixed Income	23.00 %	2.75 %
Domestic Equities	20.70	6.34
Real Estate	10.00	4.75
Private Equity	10.00	8.97
International Equities	18.30	7.95
Other investments	18.00	4.92
Total	100.00 %	5.66 %

Discount Rate The discount rate used to measure the total pension liability was 7.5 percent. The projection of cash flows used to determine the discount rate assumed that contributions from plan members and those of the contributing employers are made at the statutorily required rates. Based on those assumptions, the pension plan’s fiduciary net position was projected to be available to make all projected future benefits payments of current plan members. 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.

Sensitivity of the Wastewater System’s Proportionate Share of the Net Pension Liability to Changes in the Discount Rate The following table presents the Wastewater System’s proportionate share of the net pension liability calculated using the current period discount rate assumption of 7.5 percent, as well as what the Wastewater System’s proportionate share of the net pension liability would be if it were calculated using a discount rate that is one-percentage-point lower (6.5 percent) or one-percentage-point higher (8.5 percent) than the current rate:

	1% Decrease (6.50%)	Current Discount Rate (7.50%)	1% Increase (8.50%)
	Wastewater System's proportionate share of the net pension liability	\$ 3,720,476	2,435,275

OPERS Other Postemployment Benefits

Plan Description – 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; and the Combined Plan – cost-sharing, multiple-employer defined benefit pension plan that has elements of both a defined benefit and defined contribution plan.

OPERS maintains a cost-sharing, multiple-employer defined benefit post-employment health care trust, which funds multiple health care plans including medical coverage, prescription drug coverage and deposits to a Health Reimbursement Arrangement to qualifying benefit recipients of both the Traditional Pension and the Combined plans. This trust is also used to fund health care for Member-Directed Plan participants, in the form of a Retiree Medical Account (RMA). At retirement or refund, Member-Directed Plan participants may be eligible for reimbursement of qualified medical expenses from their vested RMA balance.

In order to qualify for post-employment health care coverage, age-and-service retirees under the Traditional Pension and Combined Plans must have 20 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 is considered an Other Postemployment Benefit (OPEB) as described in GASB Statement No. 45. Please see the Plan Statement in the OPERS 2016 CAFR for details.

The ORC 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 ORC.

OPERS issues a stand-alone financial report. Interested parties may obtain a copy by visiting <https://www.opers.org/financial/reports.shtml#CAFR>, by making a written request to OPERS, 277 East Town Street, Columbus, Ohio 43215-4642, or by calling (614) 222-5601 or 1-800-222-7377.

Funding Policy – The ORC 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 2017, local government employers contributed at a rate of 14 percent of covered payroll. The ORC currently limits the employer contribution to a rate not to exceed 14 percent of covered payroll for local government employers. Active members do not make contributions to the OPEB plan.

Each year, the OPERS Board of Trustees determines the portion of the employer contribution rate that will be set aside to fund health care plans. The portion of employer contributions allocated to health care for members in the Traditional Pension and Combined Plans was 1 percent during calendar year 2017. As recommended by OPERS’ actuary, the portion of employer contributions allocated to health care beginning January 1, 2018 decreased to 0 percent for both plans. The Board is also authorized to establish rules for the retiree or their surviving beneficiaries to pay a portion of the health care provided. Payment amounts vary depending on the number of covered dependents and the coverage selected. The employer contribution as a percentage of covered payroll deposited to the RMA for participants in the Member-Directed Plan for 2017 was 4 percent.

The Wastewater System's contributions for health care to the OPERS for the years ending December 31, 2017, 2016, and 2015 \$14,000, \$24,000 and \$32,000, respectively, which were equal to the required contributions for each year.

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.

The Metropolitan Pension Plan currently has no assets and the plan is not administered through a trust. GASB Statement No. 73 establishes requirements for defined benefit pensions that are not with the scope of GASB Statement No. 68, as well as for the assets accumulated for purposes of providing those pensions. The total pension liability was deemed not material to the Gas System's financial statements. As such, the Metropolitan Pension Plan liability is not reported in the financial statements.

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.

The Wastewater System's annual OPEB cost and net OPEB for the Retiree Life Insurance Plan for the years ended December 31, 2017, 2016, and 2015 are as follows:

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Annual required contribution (ARC)	\$ 18,980	\$ 19,363	\$ 18,099
Interest on Net OPEB	392	282	183
Adjustments to ARC	<u>(593)</u>	<u>(417)</u>	<u>(274)</u>
Annual OPEB cost	18,779	19,228	18,008
Contributions made	<u>16,460</u>	<u>16,634</u>	<u>15,947</u>
Increase in Net OPEB	2,319	2,594	2,061
Net OPEB, beginning of year	<u>9,230</u>	<u>6,636</u>	<u>4,575</u>
Net OPEB, end of year	<u>\$ 11,549</u>	<u>\$ 9,230</u>	<u>\$ 6,636</u>

The Wastewater System’s annual OPEB cost, percentage of OPEB contributed, net OPEB, and unfunded actuarial accrued liabilities for years ended December 31, 2017, 2016, and 2015 are as follows:

<u>Years Ended</u>	<u>Annual OPEB Cost</u>	<u>Percentage of OPEB Contributed</u>	<u>Net OPEB Obligation</u>	<u>Unfunded Actuarial Accrued Liability</u>
2017	\$ 18,779	87.7%	\$ 11,549	\$ 277,234
2016	19,228	86.5%	9,230	254,226
2015	18,008	88.6%	6,636	266,328

The actuarial valuation date was December 31, 2017 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 the likely outcome will not be material to the Wastewater System’s basic financial statements.

9. RELATED PARTY TRANSACTIONS

The Wastewater System purchases electricity from the City’s Electric System. Purchases of \$526,876 and \$588,601 were made in 2017 and 2016, respectively, 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 \$2,545,000 and \$2,291,000 in 2017 and 2016, 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, 2017, the Wastewater System had contractual commitments in the amounts of approximately \$269,000 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.

12. SUBSEQUENT EVENT

In March and April 2018, the City issued \$43,930,000 of Revenue Refunding Bonds. The 2018 bond proceeds, including issuance premium, were used to retire the 2017 Various Purpose General Obligation Notes reported by the Electric, Water and Wastewater Systems.

The Wastewater System refunding bonds were issued in the amount of \$25,325,000, carry an interest rate of 2 to 5 percent, and mature in 2041.

**CITY OF HAMILTON, OHIO – WASTEWATER SYSTEM
REQUIRED SUPPLEMENTARY INFORMATION
OHIO PUBLIC EMPLOYEES RETIREMENT SYSTEM**

**SCHEDULE OF THE PROPORTIONATE SHARE OF THE NET PENSION LIABILITY
LAST FOUR MEASUREMENT PERIODS**

	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Wastewater System's proportion of the Net Pension Liability	0.0107242%	0.0107035%	0.0132201%	0.0132201%
Wastewater System's proportionate share of the Net Pension Liability	\$ 2,435,275	\$ 1,853,976	\$ 1,594,487	\$ 1,567,858
Wastewater System's Covered Payroll	\$ 1,397,050	\$ 1,468,558	\$ 1,636,133	\$ 1,471,631
Wastewater System's Proportionate Share of the Net Pension Liability as a Percentage of it Covered Payroll	174.32%	126.24%	97.45%	106.54%
Plan Fiduciary Net Position as a Percentage as a Percentage of the Total Pension Liability	77.25%	81.08%	86.45%	86.36%

Note: Information prior to 2014 was not available.

The schedule is reported as of the measurement date of the net pension liability, which is the prior year end.

**SCHEDULE OF CONTRIBUTIONS
LAST FIVE YEARS**

	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>
Contractually Required Contributions	\$ 197,521	\$ 167,646	\$ 176,227	\$ 196,336	\$ 191,312
Contributions in Relation to the Contractually Required Contribution	<u>(197,521)</u>	<u>(167,646)</u>	<u>(176,227)</u>	<u>(196,336)</u>	<u>(191,312)</u>
Contribution Deficiency (Excess)	<u>\$ -</u>				
Wastewater System's Covered Payroll	\$ 1,519,392	\$ 1,397,050	\$ 1,468,558	\$ 1,636,133	\$ 1,471,631
Contributions as a Percentage of Covered Payroll	13.00%	12.00%	12.00%	12.00%	13.00%

Note: Information prior to 2013 was not available.

NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION

There were no recent significant changes of benefit terms, investment policies, the size or composition of the population covered by the benefit terms impacting the actuarial valuation study for the year ended December 31, 2016.

In 2016, a five-year experience study was completed on the period January 1, 2011 through December 31, 2015. The Board adopted changes to both the demographic and economic assumptions as a result of the study. The most notable change in demographic assumptions is an increased life expectancy of the members and the most notable change in economic assumptions is the reduction in the actuarially assumed rate of return from 8.00% down to 7.50% for the defined benefit investments. The new assumptions are included in the 2016 actuarial valuation.

In 2016, OPERS, in conjunction with the Board's investment consultants, also completed an asset liability study. Periodically, the System engages in a more comprehensive study that examines the nature of the pension liabilities the plan will ultimately pay and the characteristics of the asset allocation projections and the associated level of risk. As a result of this study, OPERS modified the asset allocation slightly, but not substantively.

This page intentionally left blank.



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 2, 2018**