CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF WATER POLLUTION CONTROL

REPORT ON AUDIT OF FINANCIAL STATEMENTS
For the year ended December 31, 2016

CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF WATER POLLUTION CONTROL

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CLARK SCHAEFER HACKETT
CPAS & ADVISORS

One East Fourth Street, Suite 1200, Cincinnati, Ohio 45202
P. 513.241.3111 | F. 513.241.1212 | cshco.com

INDEPENDENT AUDITORS' REPORT

To the Honorable Frank G. Jackson, Mayor, Members of Council and the Audit Committee
Division of Water Pollution Control
Department of Public Utilities
City of Cleveland, Ohio:

Report on the Financial Statements

We have audited the accompanying financial statements of the Division of Water Pollution Control, Department of Public Utilities, City of Cleveland, Ohio (the "Division") as of and for the year ended December 31, 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 Division of Water Pollution Control, Department of Public Utilities, City of Cleveland, Ohio as of December 31, 2016, and the changes 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.

Emphasis of Matter

As described in Note A to the basic financial statements, the financial statements present only the Division and do not purport to, and do not present fairly the financial position of the City of Cleveland as of December 31, 2016, and the respective changes in its financial position and cash flows for the year 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 27, 2017

CITY OF CLEVELAND, OHIO
DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF WATER POLLUTION CONTROL

MANAGEMENT'S DISCUSSION AND ANALYSIS

GENERAL

As management of the City of Cleveland's (the City) Department of Public Utilities, Division of Water Pollution Control (the Division), we offer readers of the Division's financial statements this narrative overview and analysis of the financial activities of the Division for the year ended December 31, 2016. Please read this information in conjunction with the Division's basic financial statements and footnotes that begin on page 14.

The Division was created for the purpose of supplying sewer services to customers within the Cleveland metropolitan area. Embarking with a rudimentary system in the late 1800's, the Cleveland Sewer System developed as the City itself expanded. Until the early 1970's, the City operated the entire system and managed all aspects of sewage treatment and disposal.

In 1972, a court order created the Northeast Ohio Regional Sewer District (NEORSD) and transferred the operation of all wastewater treatment plants and interceptors to the NEORSD in December 1973.

The City retained responsibility for the sewer collector system in Cleveland. The Division serves a significant portion of the entire metropolitan area by managing the sanitary sewage and storm water drainage collection system. The sewer collection system transfers sanitary and storm sewage from its point of origin to an interceptor sewer or treatment plant for processing. The system is comprised of over 1,400 miles of sewer lines with attendant catch basins and includes 12 pump/lift stations. The Division is also responsible for the cleaning of 44,000 catch basins and for maintaining two storm detention basins.

The Division currently has 122,814 customer accounts in the City, of which 94.4% are residential and 5.6% commercial. Also, in 2016, the Division's sewers transported 1,788,294 Mcf's (thousand cubic feet) of water.

The Division acts as a custodian of billings and receipts for 17 other agencies including the NEORSD, other municipalities and Dominion East Ohio's residential service line protection plan. Accounts are billed quarterly and payments collected each month are remitted to the appropriate agency by the 15th of the subsequent month.

COMPARISON OF CURRENT YEAR'S AND PRIOR YEARS' DATA

FINANCIAL HIGHLIGHTS

- The assets and deferred outflows of resources of the Division exceeded its liabilities and deferred inflows of resources (net position) by $99,409,000 and $95,321,000 at December 31, 2016 and 2015, respectively. Of these amounts, $26,011,000 and $21,803,000 are unrestricted net position at December 31, 2016 and 2015, respectively, and may be used to meet the Division's ongoing obligations to customers and creditors.

- The Division's net position increased by $4,088,000 in 2016. The rise is primarily attributed to an increase in operating revenues of $1,930,000.

FINANCIAL HIGHLIGHTS (Continued)

- The Division's total debt increased in 2016 by $31,908,000 due to the issuance of the Division's first series of revenue bonds.

- The Division benefited from having a full year of revenue related to its fixed rate charge in 2016, which varied between $12.00 and $550.00 per quarter based on meter size. This revenue amounted to $6,371,000 in 2016.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Division's basic financial statements. The accompanying financial statements present financial information for the City's Division of Water Pollution Control Fund, in which the City accounts for the operations of the Department of Public Utilities, Division of Water Pollution Control. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The Division is considered an enterprise fund because the operations of the Division are similar to a private sector business enterprise. Accordingly, in accounting for the activities of the Division, the economic resources measurement focus and the accrual basis of accounting is used.

The basic financial statements of the Division can be found on pages 14 - 19 of this report.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the basic financial statements. The notes to the basic financial statements can be found on pages 21 - 43 of this report. Required supplementary information can be found on pages 44 - 45 of this report.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

CONDENSED STATEMENT OF NET POSITION INFORMATION

Provided below are the statements of net position information for the Division as of December 31, 2016 and December 31, 2015:

	2016	2015
	(Amounts in Thousands)	
Assets:		
Capital assets, net	$ 78,498	$ 74,271
Restricted assets	31,895	617
Current assets	160,050	137,933
Total Assets	270,443	212,821
Deferred outflows of resources	3,244	1,080
Net position:		
Net investment in capital assets	70,873	73,518
Restricted for debt services	2,525	
Unrestricted	26,011	21,803
Total net position	99,409	95,321
Liabilities:		
Long-term obligations	46,246	6,917
Current liabilities	127,823	111,544
Total liabilities	174,069	118,461
Deferred inflows of resources	209	119

Current Assets: During 2016, the Division's current assets increased by $22,117,000. Unrestricted cash and cash equivalents increased by $11,889,000, while net accounts receivable rose by $8,419,000. The increase in both is primarily attributed to escalating sewer rates.

CONDENSED STATEMENT OF NET POSITION INFORMATION (Continued)

Capital Assets: At December 31, 2016, net capital assets amounted to $78,498,000. This is an increase of $4,227,000 from the prior year, mainly attributed to an increase of $4,903,000 in construction in progress and $3,430,000 in utility plant, offset by a net increase in accumulated depreciation of $4,940,000. A summary of the activity in the Division's capital assets during the year ended December 31, 2016, is as follows:

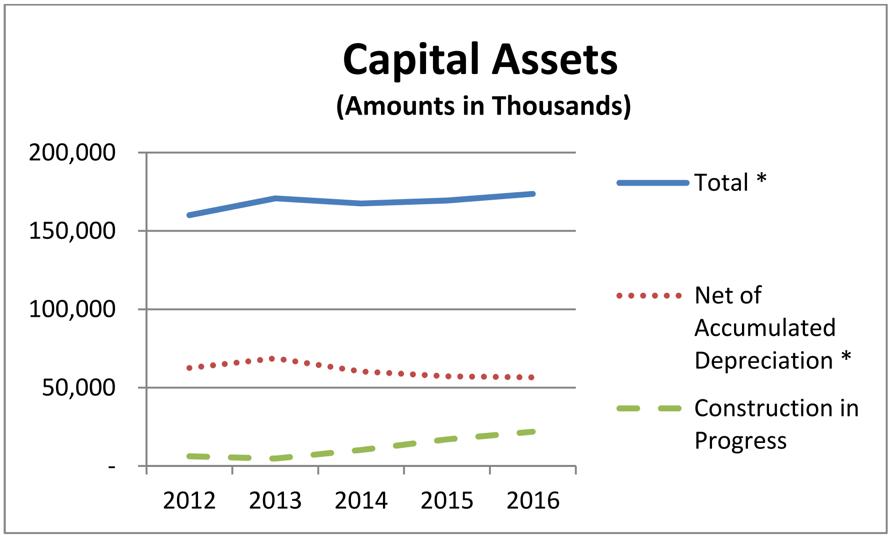
	Balance January 1, 2016	Additions	Reductions	Balance December 31, 2016
	(Amounts in Thousands)			
Land	$ 297	$	$	$ 297
Utility plant	144,630	4,227	(797)	148,060
Buildings, structures and improvements	9,019			9,019
Furniture, fixture, equipment and vehicles	15,412	1,146	(312)	16,246
Construction in progress	17,045	9,787	(4,884)	21,948
Total	186,403	15,160	(5,993)	195,570
Less: Accumulated depreciation	(112,132)	(5,925)	985	(117,072)
Capital assets, net	$ 74,271	$ 9,235	$ (5,008)	$ 78,498

In 2016, the largest capital additions were the Ontario Street Project, Lee Road Betterment, and a Work Order Management System.

The major capital projects/expenses for the year included:

- Bryant Avenue
- Rehabilitating and Relining Sewers
- Manholes & Catch Basins
- Rockwell Avenue Sewer

CONDENSED STATEMENT OF NET POSITION INFORMATION (Continued)



* Construction in Progress not included

Additional information on the Division's capital assets, including commitments made for future capital expenditures, can be found in Note D.

Current Liabilities: Current liabilities increased by $16,279,000 in 2016, mainly due to an increase in amounts due for billings on behalf of others of $15,575,000, partially offset by a decrease in due to other City of Cleveland departments, divisions or funds of $380,000. The rise in amounts due for billings on behalf of others is primarily attributed to an increase in cash and cash equivalents and net accounts receivable.

***Pension Liability*:** During 2015, the Division adopted Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions — an Amendment of GASB Statement No. 27* and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68* 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 Division's actual financial condition by adding deferred inflows of resources related to pension and the net pension liability to the reported net position and subtracting deferred outflows of resources 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.

CONDENSED STATEMENT OF NET POSITION INFORMATION (Continued)

Under the new standards required by GASB Statement No. 68, the net pension liability equals the Division'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 Division part of a bargained-for benefit to the employee and should accordingly be reported by the Division as a liability since they received the benefit of the exchange. However, the Division 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 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 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 Division. In the event that contributions, investment returns and other changes are insufficient to keep up with 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 Division 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 of resources.

As a result of implementing GASB Statement No. 68, the Division is reporting a net pension liability and deferred inflows/outflows of resources related to pension on the accrual basis of accounting.

CONDENSED STATEMENT OF NET POSITION INFORMATION (Continued)

Long-Term Debt: At the end of 2016, the Division had total debt outstanding of $32,661,000 associated with its new issuance of revenue bonds, with one OWDA construction loan and two OPWC construction loans. The revenue bonds are backed by the net revenues of the Division. The loans are payable from revenues generated by the Division but do not have a lien on the revenues.

The activity in the Division's debt obligations outstanding during the year ended December 31, 2016 is summarized below:

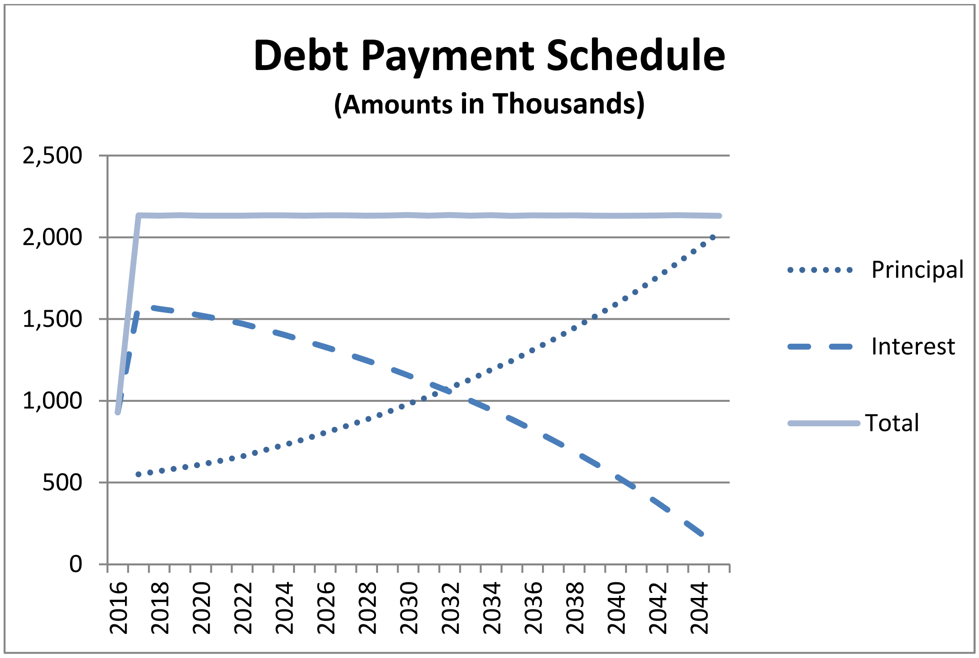
	Balance January 1, 2016	Debt Issued	Debt Retired	Balance December 31, 2016
	(Amounts in thousands)			
Water Pollution Control Revenue Bonds, Series 2016	$	$ 32,390	$	$ 32,390
Ohio Water Development Authority Loans (OWDA)	610		(458)	152
Ohio Public Works Commission Loans (OPWC)	143		(24)	119
Total	$ 753	$ 32,390	$ (482)	$ 32,661

The bonds ratings for the Division's outstanding revenue bonds as of December 31, 2016, as of follows:

	Moody's Investors Service	Standard & Poor's
Water Pollution Control Revenue Bonds	Aa3	A+

The ratio of net revenue available for debt service to debt service requirements (revenue bond coverage) is a useful indicator of the Division's debt position to management, customers, and creditors and investors. The Division's revenue bond coverage for 2016 was 1,061% because no bond principal was due in 2016 and the Division made only one interest payment.

CONDENSED STATEMENT OF NET POSITION INFORMATION (Continued)



Additional information on the Division's long-term debt can be found in Note B on pages 26 - 30.

Net Position: Net position serves as a useful indicator of a government's financial position. In the case of the Division, assets and deferred outflows of resources exceeded liabilities and deferred inflows of resources by $99,409,000 and $95,321,000 at December 31, 2016 and 2015, respectively.

The largest portion of the Division's net position, $70,873,000 at December 31, 2016, reflects its investment in capital assets (e.g., land, buildings, utility plant, machinery and equipment), net of accumulated depreciation, less any related outstanding debt used to acquire those assets. The Division uses these capital assets to provide services to its customers. Consequently, these assets are not available for future spending. Although the Division's investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the Division's net position, $2,525,000 at December 31, 2016, represents resources that are subject to external restrictions. These funds are set aside for the payment of revenue bonds.

The remaining balance of net position, $26,011,000 at December 31, 2016, is unrestricted and may be used to meet the Division's ongoing obligations to customers and creditors.

CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION INFORMATION

During 2016, the Division's operations increased its net position by $4,088,000. Provided below are the key elements of the Division's results of operations for the years ended December 31, 2016 and 2015:

	2016	2015
	(Amounts in Thousands)	
Operating revenues	$ 28,730	$ 26,800
Operating expenses	24,935	23,142
Operating income (loss)	3,795	3,658
Non-operating revenue (expense):		
Investment income	197	52
Interest expense	(15)	(35)
Amorization of bond premiums and discounts	200	
Gain (loss) on the disposal of assets	(123)	(4)
Other	34	9
Total non-operating revenue (expense), net	293	22
Increase (decrease) in net position	$ 4,088	$ 3,680

Operating revenues: Operating revenues amounted to $28,730,000 in 2016, which was an increase of $1,930,000 from the previous year. The increase is primarily the result of having a full year of revenue related to the April 1, 2015, introduction of the fixed rate charge.

Operating expenses: During 2016, total operating expenses increased by $1,793,000. Charges related to professional services increased by $792,000, primarily due the issuance of the Series 2016 Revenue Bonds.

Non-operating revenues and expenses: In 2016, non-operating revenue (expense) increased by $271,000. The increase was primarily attributed to amortization of bond premiums and discounts of $200,000, as well as an increase in investment income of $145,000, offset by a $123,000 loss on disposal of assets.

ADDITIONAL INFORMATION

This financial report is designed to provide a general overview of the Division's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Office of the Finance Director, City Hall, Room 104, 601 Lakeside Avenue, Cleveland, Ohio 44114.

BASIC FINANCIAL STATEMENTS

CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF WATER POLLUTION CONTROL
STATEMENT OF NET POSITION
December 31, 2016
(Amounts in Thousands)

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	
CAPITAL ASSETS	
Land	$ 297
Utility plant	148,060
Buildings, structures and improvements	9,019
Furniture, fixtures, equipment and vehicles	16,246
	173,622
Less: Accumulated depreciation	(117,072)
	56,550
Construction in progress	21,948
CAPITAL ASSETS, NET	78,498
RESTRICTED ASSETS	
Cash and cash equivalents	31,885
Accrued interest receivable	10
TOTAL RESTRICTED ASSETS	31,895
CURRENT ASSETS	
Cash and cash equivalents	62,082
Restricted cash and cash equivalents	1,603
Receivables:	
Accounts receivable - net of allowance for doubtful accounts of $2,534,000 in 2016	91,849
Unbilled revenue	3,783
Accrued interest receivable	6
Due from other City of Cleveland departments, divisions or funds	357
Materials and supplies	370
TOTAL CURRENT ASSETS	160,050
DEFERRED OUTFLOWS OF RESOURCES	
Pension	3,244

CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF WATER POLLUTION CONTROL
STATEMENT OF NET POSITION
December 31, 2016
(Amounts in Thousands)

NET POSITION, LIABILITIES AND DEFERRED INFLOWS OF RESOURCES	
NET POSITION	
Net investment in capital assets	$ 70,873
Restricted for debt service	2,525
Unrestricted	26,011
TOTAL NET POSITION	99,409
LIABILITIES	
LONG-TERM OBLIGATIONS-excluding amounts due within one year:	
OPWC loans	94
Accrued wages and benefits	148
Revenue Bonds	37,025
Net pension liability	8,979
TOTAL LONG-TERM OBLIGATIONS	46,246
CURRENT LIABILITIES	
Accounts payable	319
Customer deposits and other liabilities	194
Payable from restricted assets	1,603
Accrued wages and benefits	1,076
Due to other City of Cleveland departments, divisions or funds	4,019
Amounts due for billing on behalf of others	119,687
Accrued interest payable	198
Current portion of long-term debt, due within one year	727
TOTAL CURRENT LIABILITIES	127,823
TOTAL LIABILITIES	174,069
DEFERRED INFLOWS OF RESOURCES	
Pension	209

See notes to financial statements.

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CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF WATER POLLUTION CONTROL
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
For the year ended December 31, 2016
(Amounts in Thousands)

OPERATING REVENUES	
Charges for services	$ 28,730
TOTAL OPERATING REVENUES	28,730
OPERATING EXPENSES	
Operations	10,756
Maintenance	8,254
Depreciation	5,925
TOTAL OPERATING EXPENSES	24,935
OPERATING INCOME (LOSS)	3,795
NON-OPERATING REVENUE (EXPENSE)	
Investment income	197
Interest expense	(15)
Amortization of bond premiums and discounts	200
Gain (loss) on disposal of assets	(123)
Other	34
TOTAL NON-OPERATING REVENUE (EXPENSE), NET	293
INCREASE (DECREASE) IN NET POSITION	4,088
NET POSITION, BEGINNING OF YEAR	95,321
NET POSITION, END OF YEAR	$ 99,409

See notes to financial statements.

CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF WATER POLLUTION CONTROL
STATEMENT OF CASH FLOWS
For the year ended December 31, 2016
(Amounts in Thousands)

CASH FLOWS FROM OPERATING ACTIVITIES	
Cash received from customers	$ 26,334
Cash payments to suppliers for goods or services	(8,972)
Cash payments to employees for services	(9,080)
Agency activity on behalf of other sewer authorities	8,396
Other	(35)
NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	16,643
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Proceeds from sale of revenue bonds, loans and notes	37,775
Acquisition and construction of capital assets	(8,480)
Principal paid on long-term debt	(482)
Interest paid on long-term debt	(943)
NET CASH PROVIDED BY (USED FOR) CAPITAL AND RELATED FINANCING ACTIVITIES	27,870
CASH FLOWS FROM INVESTING ACTIVITIES	
Interest received on investments	247
NET CASH PROVIDED BY (USED FOR) INVESTING ACTIVITIES	247
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	44,760
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	50,810
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 95,570

CITY OF CLEVELAND, OHIO

DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF WATER POLLUTION CONTROL
STATEMENT OF CASH FLOWS
For the year ended December 31, 2016
(Amounts in Thousands)

RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES

OPERATING INCOME (LOSS)	$	3,795
Adjustments		
Depreciation		5,925
(Increase) decrease in assets:		
Accounts receivable, net		(8,419)
Unbilled revenue		(40)
Due from other City of Cleveland departments, divisions or funds		(214)
Materials and supplies, net		48
Prepaid expenses		5
(Increase) decrease in deferred outflows of resources - pension		(2,164)
Increase (decrease) in liabilities:		
Accounts payable		143
Customer deposits and other liabilities		(22)
Accrued wages and benefits		(167)
Due to other City of Cleveland departments, divisions or funds		(380)
Amounts due for billings on behalf of others		15,575
Net pension liability		2,468
Increase (decrease) in deferred inflows of resources - pension		90
TOTAL ADJUSTMENTS		12,848
NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	$	16,643

SCHEDULE OF NONCASH CAPITAL AND RELATED FINANCING ACTIVITIES:

Contributions and accounts payable related to capital assets	$	1,603

See notes to financial statements.

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NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Division of Water Pollution Control (the Division) is reported as an Enterprise Fund of the City of Cleveland's Department of Public Utilities and is a part of the City of Cleveland's (the City) primary government. The Division was created for the purpose of supplying sewer services to customers within the metropolitan area. The following is a summary of the more significant accounting policies.

Reporting Model and Basis of Accounting: The accounting policies and financial reporting practices of the Division comply with accounting principles generally accepted in the United States of America applicable to governmental units.

In February of 2015, Governmental Accounting Standards Board (GASB) Statement No. 72, *Fair Value Measurement and Application* was issued. This Statement is effective for reporting periods beginning after June 15, 2015. This Statement addresses accounting and financial reporting issues related to fair value measurements. The definition of fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. As required, the Division has implemented GASB Statement No. 72 as of December 31, 2016.

In June of 2015, GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68* were issued. This Statement is effective for fiscal periods beginning after June 15, 2015 — except those provisions that address employers and governmental nonemployer contributing entities for pensions that are not within the scope of GASB Statement No. 68, which are effective for fiscal years beginning after June 15, 2015. The objective of this Statement is to improve the usefulness of information about pensions included in the general purpose external financial reports of state and local governments for making decisions and assessing accountability. This Statement establishes requirements for defined benefit pensions that are not within the scope of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, as well as for the assets accumulated for purposes of providing those pensions. In addition, it establishes requirements for defined contribution pensions that are not within the scope of GASB Statement No. 68. It also amends certain provisions of GASB Statement No. 67, *Financial Reporting for Pension Plans*, and GASB Statement No. 68 for pension plans and pensions that are within their respective scopes. The Division has determined that GASB Statement No. 73 has no impact on its financial statements as of December 31, 2016.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

In June of 2015, GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments* was issued. This Statement is effective for reporting periods beginning after June 15, 2015. This Statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The objective of this Statement is to identify—in the context of the current governmental financial reporting environment—the hierarchy of generally accepted accounting principles (GAAP). The “GAAP hierarchy” consists of the sources of accounting principles used to prepare financial statements of state and local governmental entities in conformity with GAAP and the framework for selecting those principles. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and no authoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. As required, the Division has implemented GASB Statement No. 76 as of December 31, 2016.

In August of 2015, GASB Statement No. 77, *Tax Abatement Disclosures* was issued. This Statement is effective for reporting periods beginning after December 15, 2015. This Statement requires governments that enter into tax abatement agreements to disclose information about the agreements such as: brief descriptive information, gross dollar amount of taxes abated during the period, and commitments made by a government, other than to abate taxes, as part of a tax abatement agreement. Governments should organize those disclosures by major tax abatement program and may disclose information for individual tax abatement agreements within those programs. The Division has determined that GASB Statement No. 77 has no impact on its financial statements as of December 31, 2016.

In December of 2015, GASB Statement No. 78, *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans* was issued. This Statement is effective for reporting periods beginning after December 15, 2015. The objective of this Statement is to address a practice issue regarding the scope and applicability of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. This issue is associated with pensions provided through certain multiple-employer defined benefit pension plans and to state or local governmental employers whose employees are provided with such pensions. This Statement amends the scope and applicability of GASB Statement No. 68 to exclude pensions provided to employees of state or local governmental employers through a cost-sharing multiple-employer defined benefit pension plan that (1) is not a state or local governmental pension plan, (2) is used to provide defined benefit pensions both to employees of state or local governmental employers and to employees of employers that are not state or local governmental employers, and (3) has no predominant state or local governmental employer (either individually or collectively with other state or local governmental employers that provide pensions through the pension plan). This Statement establishes requirements for recognition and measurement of pension expense, expenditures, and liabilities; note disclosures; and required supplementary information for pensions that have the characteristics described above. The Division has determined that GASB Statement No. 78 has no impact on its financial statements as of December 31, 2016.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

In December of 2015, GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*, was issued. This Statement is effective for reporting periods beginning after June 15, 2015, except for the provisions in paragraphs 18, 19, 23–26, and 40, which are effective for reporting periods beginning after December 15, 2015. This Statement establishes additional note disclosure requirements for qualifying external investment pools that measure all of their investments at amortized cost for financial reporting purposes and for governments that participate in those pools. Those disclosures for both the qualifying external investment pools and their participants include information about any limitations or restrictions on participant withdrawals. As required, the Division has implemented GASB Statement No. 79 as of December 31, 2016.

The Division's net position is accounted for in the accompanying statements of net position and is divided into the following categories:

- Net investment in capital assets
- Amount restricted for debt service
- Remaining unrestricted amount

In addition, certain additional financial information regarding the Division is included in these footnotes.

Basis of Accounting: The Division's financial statements are prepared under the accrual basis of accounting. Under this method, revenues are recognized when earned and measurable and expenses are recognized as incurred.

Revenues: Revenues are derived primarily from sales of sewer services to residential, commercial and industrial customers based upon actual water consumption. Sewer rates are authorized by City Council and billings are made on a cyclical basis. Estimates for services between the end of the various cycles and the end of the year are recorded as unbilled revenue.

Accounts Receivables: The Division's share of the accounts receivable balance is $13,217,000, net of allowance for doubtful accounts of $2,534,000. The remaining accounts receivable balance of $78,632,000 belongs to the Northeast Ohio Regional Sewer District and other municipalities in the Greater Cleveland Region and is offset by corresponding amounts in due for billings on behalf of others.

Statement of Cash Flows: The Division utilizes the direct method of reporting for the statement of cash flows as defined by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Non-Expendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*. In a statement of cash flows, cash receipts and cash payments are classified according to operating, noncapital financing, capital and related financing and investment activities.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Cash and Cash Equivalents: Cash and cash equivalents represent cash on hand and cash deposits maintained by the City Treasurer on behalf of the Division. Cash equivalents are defined as highly liquid investments with maturity of three months or less when purchased.

Investments: The Division follows the provisions of GASB Statement No. 72 *Fair Value Measurement and Application* which requires governmental entities to record their investments at fair value within the fair value hierarchy. The hierarchy is based on the valuation inputs used to measure fair value of the assets. Level 1 inputs are quoted prices in an active market for identical assets. Level 2 inputs are significant other observable inputs. Level 3 inputs are significant unobservable inputs. The Division's investments in money market mutual funds and the State Treasury Asset Reserve of Ohio (STAR Ohio) funds are excluded from fair value measurement requirements under GASB Statement No. 72, and instead are reported at amortized cost.

The Division has invested funds in STAR Ohio during 2016. 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 has adopted GASB Statement No. 79 for the purpose of measuring the value of shares in STAR Ohio. The Division measures their investment in STAR Ohio 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 share that approximates fair value.

Capital Assets and Depreciation: Capital assets are stated on the basis of historical cost or, if contributed, at fair market value as of the date received. Depreciation is computed by allocating the cost of capital assets over the estimated useful lives of the assets using the straight-line method. A capital asset is defined as an item with a useful life in excess of one year and an individual cost of more than $5,000 for furniture, fixtures, equipment and vehicles and $10,000 for all other assets. When capital assets are disposed of, the cost and related accumulated depreciation are removed from the accounts with gains or losses on disposition being reflected in operations. The estimated useful lives are as follows:

Utility plant	5 to 100 years
Building, structures and improvements	5 to 60 years
Furniture, fixtures, equipment and vehicles	3 to 60 years

The Division's policy is to capitalize interest on construction projects up to the point in time that the project is substantially completed. Capitalized interest is included in the cost of the assets and is depreciated on the straight-line basis over the estimated useful lives of such assets. The Division applies GASB guidance pertaining to capitalization of interest costs for its revenue bonds. This statement requires capitalization of interest cost of eligible borrowings, less interest earned on investment of the related bond proceeds from the date of borrowing until the assets constructed from the bond proceeds are ready for their intended use.

For 2016, total interest costs incurred amounted to $1,142,000, of which $1,061,000 was capitalized, net of interest income of $66,000.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Bond Issuance Costs, Discounts, Premiums and Unamortized Losses on Debt Refundings: Bond issuance costs are expensed when incurred. Deferred bond discounts/premiums are netted against long-term debt. The discounts/premiums are amortized over the lives of the applicable bonds. Unamortized loss on debt refundings are categorized as a deferred outflow of resources and is amortized over the shorter of the defeased bond or the newly issued bond.

Deferred Outflows/Inflows 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 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. In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time.

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

Compensated Absences: The Division accrues for compensated absences such as vacation, sick leave and compensatory time using the termination payment method specified under GASB Statement No. 16, *Accounting for Compensated Absences*. These amounts are recorded as accrued wages and benefits in the accompanying statement of net position. The portion of the compensated absence liability that is not expected to be paid or utilized within one year is reported as a long-term liability.

Normally, all vacation time is to be taken in the year available. The Division allows employees to carryover vacation time from one year to the next. Sick days not taken may be accumulated until retirement. An employee is paid one-third of accumulated sick leave upon retirement, calculated at the three year average base salary rate, with the balance being forfeited.

NOTE B - LONG-TERM OBLIGATIONS

Long-term obligations outstanding at December 31, 2016 as follows:

	Interest Rate	Original Issuance	2016
		(Amounts in Thousands)	
Water Pollution Control Revenue Bonds, Series 2016 due through 2045	3.00% - 5.00%	$ 32,390	$ 32,390
Ohio Water Development Authority (OWDA) Loans payable annually through 2017	0.00% - 3.00%	6,485	152
Ohio Public Works Commission (OPWC) Loans payable annually through 2022	0.00%	481	119
		$ 39,356	32,661
Less:			
Unamortized discount and premium			5,185
Current portion			(727)
Total Long-Term Debt			$ 37,119

NOTE B - LONG-TERM OBLIGATIONS (Continued)

Summary: Changes in long-term obligations for the year ended December 31, 2016, are as follows:

	Balance January 1, 2016	Increase	Decrease	Balance December 31, 2016	Due Within One Year
	(Amounts in Thousands)				
Water Pollution Control Revenue Bonds, Series 2016 due through 2045	$	$ 32,390	$	$ 32,390	$ 550
Ohio Water Development Authority (OWDA) Loans payable annually through 2017	610		(458)	152	152
Ohio Public Works Commission (OPWC) Loans payable annually through 2022	143		(24)	119	25
Total bonds and loans	753	32,390	(482)	32,661	727
Accrued wages and benefits	1,391	1,089	(1,256)	1,224	1,076
Net pension liability	6,511	2,468		8,979	
Total	$ 8,655	$ 35,947	$ (1,738)	$ 42,864	$ 1,803

NOTE B - LONG-TERM OBLIGATIONS (Continued)

Minimum principal and interest payments on long-term debt are as follows:

	Principal	Interest	Total
	(Amounts in Thousands)		
2017	$ 727	$ 1,586	$ 2,313
2018	594	1,562	2,156
2019	614	1,545	2,159
2020	634	1,522	2,156
2021	646	1,497	2,143
2022-2026	3,666	7,011	10,677
2027-2031	4,665	6,001	10,666
2032-2036	5,955	4,712	10,667
2037-2041	7,595	3,068	10,663
2042-2045	7,565	969	8,534
Total	$ 32,661	$ 29,473	$ 62,134

In 2015, OWDA completed an interest rate buy-down which resulted in interest rate savings on current loans. Market rate loans with interest rates higher than 4.0% saw a reduction in rates to 4.0% while rates over 3.0% on OWDA loans were reduced to 3.0%. The buy-down commenced retroactively to the January 1, 2016 payment.

The Ohio Water Development Authority and Ohio Public Works Commission Loans are being paid from the revenues derived from operations of the Division.

On April 14, 2016, the City issued $32,390,000 Water Pollution Control Revenue Bonds, Series 2016 (Green Bonds). This was the first series of revenue bonds issued by the Division, with the bonds being issued under and secured by a newly created Master Trust Agreement. The proceeds of these bonds will be used to pay capital costs relating to the acquisition, construction and improvement of the system along with funding the debt service reserve requirement and paying the costs of issuing the bonds.

In conjunction with the issuance of the Water Pollution Control Revenue Bonds, Series 2016 the City entered into a Master Trust Agreement for the Series 2016 Bonds and any future series of revenue bonds. Under the terms of the Trust Agreement, the Bonds are special obligations payable solely from and secured by a pledge of and lien on the net revenues of the Division and the Special Funds. The Special Funds include the construction fund, the debt service fund, the debt service reserve fund, the rate stabilization fund, the contingency fund and the balance subfund.

NOTE B - LONG-TERM OBLIGATIONS (Continued)

The indenture requires that the City will at all times prescribe, charge and collect such rates, rental and other charges for the use of the services of the system, and will restrict the operating expenses of the system in such a way that the net revenues available for debt service in each fiscal year shall be not less than the greater of i) 120% of debt service on all bonds then outstanding and payable during the fiscal year or ii) 100% of the sum of (a) debt service on all bonds then outstanding payable during that fiscal year, (b) all required deposits to the debt service reserve fund during that fiscal year, (c) all required deposits to the subordinated debt service fund and to any reserve fund securing subordinated indebtedness during the fiscal year, (d) all required deposits to the contingency fund during the fiscal year and (e) debt service payable on any other obligations payable from the balance subfund and deposits to any reserve funds securing such other obligations. As of December 31, 2016, the Division was in compliance with the terms and requirements of the indenture.

The indenture establishes the following fund accounts for the application of revenues:

***Revenue Fund*:** All revenues of the system are required to be deposited first into the revenue fund. Every month, amounts in the fund are first applied to the payment of operating expenses. A reasonable amount is also maintained in this fund as a working capital reserve.

***Debt Service Fund*:** Deposits are made from the revenue fund on a monthly basis to cover succeeding principal and interest payments as they become due on the revenue bonds.

***Debt Service Reserve Fund*:** Deposits will be made to this fund if the amount in the fund at any given time is less than the debt service reserve requirement. Amounts in the fund were deposited from the proceeds of the revenue bonds secured by the reserve fund and represent the maximum annual debt service requirement of these bonds. The City may elect not to secure any series of bonds with the reserve fund.

***Contingency Fund*:** The balance in this fund must be maintained at a minimum of $1,000,000. Amounts in this fund may be used for the payment of capital costs or for redeeming bonds.

***Balance Subfund*:** Amounts in this fund may be used for any lawful purpose of the water pollution control system.

***Construction Fund*:** Proceeds of the various series of revenue bonds are deposited into this fund to be used, along with earnings from investments of amounts held therein, for the payment of capital costs and issuance costs.

Amounts held in any fund may be invested by the City Treasurer or the trustee in permitted investments. However, the use of funds is limited by the bond indenture and accordingly, the funds are classified as restricted assets in the accompanying financial statements.

The City has pledged future water pollution control revenues to repay $32,390,000 in Water Pollution Control Revenue Bonds issued in 2016. Proceeds from the bonds will be used to pay capital costs relating to the acquisition, construction and improvement of the system. The bonds are payable from water pollution control net revenues and are payable through 2045. Annual principal and interest payments on the bonds are expected to require less than 22% of net revenues.

NOTE B - LONG-TERM OBLIGATIONS (Continued)

The total principal and interest remaining to be paid on the various Water Pollution Control Revenue Bonds is $61,861,000. Principal and interest funded in the current year and total net revenues (including other available funds) were $929,000 and $9,851,000 respectively.

Water Pollution Control Loans: Under Title VI of the Clean Water Act, Congress created the State Revolving Fund (SRF). The SRF program provides federal capitalization grants to states, in addition to the 20% state matching funds, in order to capitalize state level revolving loan funds. Besides the traditional types of municipal wastewater treatment projects, Congress expanded the potential use of SRF funds to include correction of combined sewer overflows, major sewer rehabilitation and new collector sewers.

In Ohio, this SRF program is known as the Water Pollution Control Loan Fund and is jointly administered by the Ohio EPA and the Ohio Water Development Authority. Principal balances on loans increase as project costs are incurred. Interest accrues on principal amounts outstanding during the construction period and is combined with the principal balance upon completion of the project. The repayment period for each loan commences no later than the 1st of January or July following the expected completion dates of the project to which it relates utilizing an estimate of total eligible project costs as the preliminary loan amount. Construction loans and design loans are to be repaid in semi-annual payments of principal and interest over a period of twenty years and five years, respectively. The Division had one SRF loan award related to projects remaining as of December 31, 2016. Three loans were paid off during 2016.

In addition, the Division had two OPWC loan awards as of December 31, 2016. The loan related projects are for sewer repair and replacement at the Hamlet and Adolpha Streets intersection and a storm water detention basin project at Kerruish Park. Both loans are interest-free and principal repayment will be made from the Division's operating revenues.

NOTE C - DEPOSITS AND INVESTMENTS

Deposits: The Division's carrying amount of deposits at December 31, 2016, totaled $6,862,000 and the Division's bank balances were approximately $7,061,000. The differences represent positions in pooled bank accounts and normal reconciling items. Based on the criteria described in GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements) and Reverse Repurchase Agreements* and GASB Statement No. 40, *Deposit and Investment Risk Disclosures – an Amendment of GASB Statement No. 3,* $7,061,000 of the bank balances at December 31, 2016, was insured or collateralized with securities held by the City or by its agent in the City's name.

Custodial credit risk for deposits is the risk that in the event of bank failure, the Division will not be able to recover deposits or collateral for securities that are in possession of an outside party. At year end, the Division's deposits were fully insured or collateralized. All deposits are collateralized with eligible securities pledged and deposited either with the City or with a qualified trustee by the financial institution as security for repayment of all public monies deposited in the financial institution whose market value at all times is equal to at least 110% of the carrying value of the deposits being secured.

NOTE C – DEPOSIT AND INVESTMENTS (Continued)

Investments: In accordance with GASB Statement No. 72, *Fair Value Measurement and Application*, the City reports its investments at fair value based on quoted market values, where applicable and recognized the corresponding change in the fair value of the investments recorded in investment earnings in the year in which the change occurs. The City's investment policies are governed by State statutes and City ordinances which authorize the City to invest in obligations of the U.S. Treasury, agencies and instrumentalities; State Treasurer Asset Reserve Fund (STAR Ohio); commercial paper; US Government Money Market Mutual Funds; guaranteed investment contracts; manuscript debt; bonds and other State of Ohio obligations; certificates of deposit; and repurchase transactions. Such repurchase transactions must be purchased from financial institutions or registered broker/dealers. Repurchase transactions are not to exceed a period of one year and confirmation of securities pledged must be obtained.

Generally, investments are recorded and are kept at the Federal Reserve Bank in the depository institutions' separate custodial account for the City, apart from the assets of the depository institution. Ohio statute prohibits the use of reverse repurchase agreements.

Investment securities are exposed to various risks such as interest rate, market and credit. Market values of securities fluctuate based on the magnitude of changing market conditions; significant changes in market conditions could materially affect portfolio value.

***Interest rate risk*:** As a means of limiting its exposure to fair value losses caused by rising interest rates, the Division invests primarily in both short and long-term investments maturing within five years from the date of purchase. The intent is to avoid the need to sell securities prior to maturity. Investment maturities are disclosed in the Concentration of Credit Risk section.

***Custodial Credit Risk*:** For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Division will not be able to recover the value of the investments or collateral securities that are in the possession of an outside party. The Division does not have an investment policy dealing with investment custodial credit risk beyond the requirement in the State statute.

NOTE C – DEPOSIT AND INVESTMENTS (Continued)

***Credit Risk*:** The Division's investments as of December 31, 2016 include STAR Ohio and money market mutual funds. The Division maintains the highest ratings for their investments. Investments in STAR Ohio and the PNC Treasury Money Market Fund carry a rating of AAAm, which is the highest money market fund rating given by Standard & Poor's. Ohio law requires that STAR Ohio maintain the highest rating provided by at least one nationally recognized standard rating service.

***Concentration of Credit Risk*:** The Division places a limitation on the amount it may invest in any one issuer to minimize the concentration of credit risk. The Division had the following investments at December 31, 2016, which include those classified as cash and cash equivalents in the Statement of Net Position in accordance with the provisions of GASB Statement No. 9 since they have a maturity of three months or less:

Type of Investment	2016 Value	2016 Cost	Investment Maturities Less than One Year
	(Amounts in Thousands)		
STAR Ohio	$ 28,254	$ 28,254	$ 28,254
Money Market Mutual Funds	60,454	60,454	60,454
Total Investments	88,708	88,708	88,708
Total Deposits	6,862	6,862	6,862
Total Deposits and Investments	$ 95,570	$ 95,570	$ 95,570

These amounts are monies invested by the City Treasurer on behalf of the Division and are used in daily operations with excess monies invested daily in STAR Ohio and money market mutual funds. These investments are carried at cost which approximates fair value.

As of December 31, 2016, the investments in STAR Ohio and money market mutual funds are 32% and 68%, respectively, of the Division's total investments.

NOTE D - CAPITAL ASSETS

Capital Asset Activity: Capital asset activity for the year ended December 31, 2016 was as follows:

	Balance January 1, 2016	Additions	Reductions	Balance December 31, 2016
	(Amounts in Thousands)			
Capital assets, not being depreciated:				
Land	$ 297	$	$	$ 297
Construction in progress	17,045	9,787	(4,884)	21,948
Total capital assets, not being depreciated	17,342	9,787	(4,884)	22,245
Capital assets, being depreciated:				
Utility plant	144,630	4,227	(797)	148,060
Buildings, structures and improvements	9,019			9,019
Furniture, fixtures, equipment and vehicles	15,412	1,146	(312)	16,246
Total capital assets, being depreciated	169,061	5,373	(1,109)	173,325
Less: Accumulated depreciation	(112,132)	(5,925)	985	(117,072)
Total capital assets being depreciated, net	56,929	(552)	(124)	56,253
Capital assets, net	$ 74,271	$ 9,235	$ (5,008)	$ 78,498

Commitments: The Division had outstanding commitments of approximately $25,864,000 for future capital expenses at December 31, 2016. It is anticipated that these commitments will be financed from the Division's cash balances. However, at the discretion of the Division, additional long-term debt may be issued in the future to finance a portion of the costs.

NOTE E – DEFINED BENEFIT PENSION PLAN

Net Pension Liability: The net pension liability reported on the statement of net position represents a liability to employees for pensions. Pensions are 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 Division'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 Division's obligation for this liability to annually required payments. The Division's cannot control benefit terms or the manner in which pensions are financed; however, the Division does receive the benefit of employees' services in exchange for compensation including pension.

GASB Statement No. 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.

Ohio Public Employees Retirement System (OPERS): Division's employees, other than full-time police and firefighters, 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. Division's 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.

NOTE E – DEFINED BENEFIT PENSION PLAN (Continued)

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 years of service for the first 30 years and 2.5% for service years in excess of 30	**Formula:** 2.2% of FAS multiplied by years of service for the first 30 years and 2.5% for service years in excess of 30	**Formula:** 2.2% of FAS multiplied by years of service for the first 35 years and 2.5% for service years in excess of 35

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% 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%.

NOTE E – DEFINED BENEFIT PENSION PLAN (Continued)

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

	State and Local	
2016 Statutory Maximum Contribution Rates		
Employer	14.0	%
Employee	10.0	%
2016 Actual Contribution Rates		
Employer:		
Pension	12.0	%
Post-employment Health Care Benefits	2.0	%
Total Employer	14.0	%
Employee	10.0	%

Employer contribution rates are actuarially determined and are expressed as a percentage of covered payrolls. The Division’s contractually required contribution was $764,000 for 2016. All required payments have been made.

NOTE E – DEFINED BENEFIT PENSION PLAN (Continued)

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions: The net pension liability for OPERS was measured as of December 31, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Division's proportion of the net pension liability was based on the Division's share of contributions to the pension plan relative to the contributions of all participating entities. Following is information related to the proportionate share and pension expense:

	OPERS (Amounts in Thousands)	
Proportionate Share of the Net Pension Liability	$	8,979
Proportion of the Net Pension Liability		0.047798%
Pension Expense	$	1,303

At December 31, 2016, the Division's reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	OPERS (Amounts in Thousands)	
Deferred Outflows of Resources		
Net difference between projected and actual earnings on pension plan investments	$	2,480
Division's contributions subsequent to the measurement date		764
Total Deferred Outflows of Resources	$	3,244
Deferred Inflows of Resources		
Differences between expected and actual experience		181
Change in Division's proportionate share		28
Total Deferred Inflows of Resources	$	209

NOTE E – DEFINED BENEFIT PENSION PLAN (Continued)

The $764,000 reported as deferred outflows of resources related to pension resulting from the Division's contributions subsequent to the measurement date which will be recognized as a reduction of the net pension liability in the year ending December 31, 2017. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pension will be recognized in pension expense as follows:

	OPERS (Amounts in Thousands)	
Year Ending December 31:		
2017	$	524
2018		568
2019		628
2020		551
Total	$	2,271

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. The total pension liability in the December 31, 2015, actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Wage Inflation	3.75%
Future Salary Increases, including inflation	4.25% to 10.05% including wage inflation
COLA or Ad Hoc COLA	3%, simple Pre 1/7/2013 retirees: 3%, simple Post 1/7/2013 retires: 3%, simple through 2018, then 2.8%, simple
Investment rate of return	8%
Actuarial Cost Method	Individual Entry Age

NOTE E – DEFINED BENEFIT PENSION PLAN (Continued)

Mortality rates were based on the RP-2000 Mortality Table projected 20 years using Projection Scale AA. For males, 105% of the combined healthy male mortality rates were used. For females, 100% of the combined healthy female mortality rates were used. The mortality rates used in evaluating disability allowances were based on the RP-2000 mortality table with no projections. For males 120% of the disabled female mortality rates were used set forward two years. For females, 100% of the disabled female mortality rates were used.

The most recent experience study was completed for the five year period ended December 31, 2010.

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.

In 2015, OPERS managed investments in four investment portfolios: the Defined Benefits portfolio, the Health Care portfolio, the 115 Health Care Trust portfolios and the Defined Contribution portfolio. During 2016, OPERS consolidated the health care portfolios. The Defined Benefit portfolio includes the investment assets of the Traditional Pension Plan, the defined benefit component of the Combined Plan, the annuitized accounts of the Member-Directed Plan and the VEBA Trust. 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 0.4% for 2015.

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 2015 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 %	2.31 %
Domestic Equities	20.70	5.84
Real Estate	10.00	4.25
Private Equity	10.00	9.25
International Equities	18.30	7.40
Other investments	18.00	4.59
Total	100.00 %	5.27 %

NOTE E – DEFINED BENEFIT PENSION PLAN (Continued)

Discount Rate: The discount rate used to measure the total pension liability was 8%. 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 Division's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate: The following table presents the Division's proportionate share of the net pension liability calculated using the current period discount rate assumption of 8%, as well as what the Division's proportionate share of the net pension liability would be if it were calculated using a discount rate that is one-percentage-point lower (7%) or one-percentage-point higher (9%) than the current rate:

	1% Decrease 7.00%	Current Discount Rate 8.00%	1% Increase 9.00%
	(Amounts in Thousands)		
Division's proportionate share of the net pension liability	$ 14,518	$ 8,979	$ 4,310

NOTE F – OTHER POSTEMPLOYMENT BENEFITS

Plan Description - Ohio Public Employees Retirement System**:** All full-time employees, other than non-administrative full-time police officers and firefighters, participate in the Ohio Public Employees Retirement System (OPERS). 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 – a cost-sharing, multiple-employer defined benefit pension plan that has elements of both a defined benefit and defined contribution plan.

In March 2016, OPERS received two favorable rulings from the Internal Revenue Service (IRS) allowing OPERS to consolidate all health care assets into the OPERS 115 Health Care Trust. Transition to the new health care trust structure was completed July 1, 2016. As of December 31, 2016, 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. Members of the Member-Directed Plan do not qualify for ancillary benefits, including OPERS sponsored health care coverage. OPERS funds a Retiree Medical Account (RMA) for participants in the Member-Directed Plan. At retirement or refund, participants can be reimbursed for qualified medical expenses from their vested RMA balance.

NOTE F – OTHER POSTEMPLOYMENT BENEFITS (Continued)

In order to qualify for 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 meets the definition of an Other Post Employment Benefit (OPEB) as described in GASB Statement No. 45. Please see the Plan Statement in the OPERS 2015 CAFR for details.

The Ohio Revised Code permits, but does not require, OPERS to provide health care to its eligible benefit recipients. Authority to establish and amend health care coverage is provided to the OPERS Board of Trustees (OPERS Board) in Chapter 145 of the Ohio Revised Code.

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

***Funding Policy - Ohio Public Employees Retirement System*:** The Ohio Revised Code provides the statutory authority requiring public employers to fund post-retirement health care through their contributions to OPERS. A portion of each employer’s contribution to OPERS is set aside to fund OPERS health care plans.

Employer contribution rates are expressed as a percentage of the earnable salary of active members. In 2016, State and Local employers contributed at a rate of 14.0% of earnable salary. These are the maximum employer contribution rates permitted by the Ohio Revised Code. Active member contributions do not fund health care.

Each year, the OPERS Board 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 Plan and Combined Plan was 2.0% during calendar year 2016. As recommended by OPERS’ actuary, the portion of employer contributions allocated to health care beginning January 1, 2017 decreased to 1.0% for both plans. The OPERS 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 into the RMA for participants in the Member-Directed Plan for 2016 was 4.0%.

The Division’s actual contributions to OPERS to fund postemployment benefits were $130,000 in 2016, $126,000 in 2015 and $138,000 in 2014. The required payments due in 2016, 2015 and 2014 have been made.

NOTE G - CONTINGENT LIABILITIES AND RISK MANAGEMENT

Contingent Liabilities: Various claims are pending against the City involving the Division for personal injuries, property damage and other matters. The City is responsible for the suits. The City’s management is of the opinion that ultimate settlement of such claims will not result in a material adverse effect on the Division’s financial position, results of operations or cash flows.

NOTE G - CONTINGENT LIABILITIES AND RISK MANAGEMENT (Continued)

Risk Management: The Division is exposed to various risks of loss related to torts; thefts of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Division is generally self-insured. No material losses, including incurred but not reported losses, occurred in 2016.

The City provided the choice of three separate health insurance plans to its employees until March 31, 2016. As of April 1, 2016, the City provided the choice of two separate health self-insurance plans to its employees. The Division is charged a monthly rate per employee by type of coverage. The City participates in the State of Ohio workers' compensation retrospective rating program.

In accordance with GASB Statement No. 10, claims liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. The result of the process to estimate the claims liability is not an exact amount as it depends on many complex factors, such as inflation, changes in legal doctrines and damage awards. Accordingly, claims are re-evaluated periodically to consider the effects of inflation, recent claim settlement trends (including frequency and amount of pay-outs) and other economic and social factors.

The estimate of the claims liability also includes amounts for incremental claim adjustment expenses related to specific claims and other claim adjustment expenses, regardless of whether allocated to specific claims. Estimated recoveries, for example from salvage or subrogation, are another component of the claims liability estimate. Claims liability for the Division is immaterial.

NOTE H - RELATED PARTY TRANSACTIONS

Revenues and Accounts Receivable: The Division provides sewer services to the City, including its various departments and divisions. Standard consumption rates are charged, except for the Division of Fire, public buildings and certain other facilities owned by the City, which by ordinance are provided free sewer services. Billing, collection and various other services for the Division are performed by the Division of Water for a fee. This fee is primarily based on the number of billings made on behalf of the Division during the year at the same rates as charged to other users of the billing system. These fees were approximately $2,368,000 in 2016.

Operating Expenses*:* The Division is provided various intra-city services. Charges are based on actual use or on a reasonable pro-rata basis. The more significant costs for the year ended December 31, 2016, was as follows:

	(Amounts in Thousands)
Electricity purchases	$ 201
Street construction and maintenance	41
City Administration	918
Motor Vehicle Maintenance	243
Utilities Administration and Utilities Fiscal Control	1,139

NOTE I - CUYAHOGA COUNTY REAL PROPERTY TAXES

The Division is required by ordinance to keep records of the estimated property taxes which would be payable to Cuyahoga County were it subject to such taxes. The estimated property taxes for the Division, based on book value of real estate at the current tax rates, would have been approximately $22,000 for the year ended December 31, 2016.

CITY OF CLEVELAND
DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF WATER POLLUTION CONTROL
Required Supplementary Information
Schedule of the Division's Proportionate Share of the Net Pension Liability
Ohio Public Employees Retirement System
Last Three Measurement Years (1), (2)

	2015	2014	2013
		(Amounts in Thousands)	
Division's Proportion of the Net Pension Liability	0.047798%	0.054153%	0.054153%
Division's Proportionate Share of the Net Pension Liability (Asset)	$ 8,979	$ 6,511	$ 6,375
Division's Covered-Employee Payroll	$ 6,092	$ 6,783	$ 6,138
Division's Proportionate Share of the Net Pension Liability (Asset) as a Percentage of its Covered-Employee Payroll	147.39%	95.99%	103.86%
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	81.08%	86.45%	86.36%

(1) Information presented based on measurement periods ended December 31.
(2) Information prior to 2013 was not available. The Division will continue to present information for years available until a full ten-year trend is compiled.

CITY OF CLEVELAND
DEPARTMENT OF PUBLIC UTILITIES
DIVISION OF WATER POLLUTION CONTROL
Required Supplementary Information (Continued)
Schedule of Contributions
Ohio Public Employees Retirement System
Last Four Years (1)

	2016	2015	2014	2013
	(Amounts in Thousands)			
Contractually Required Contributions	$ 764	$ 731	$ 814	$ 798
Contributions in Relation to the Contractually Required Contributions	(764)	(731)	(814)	(798)
Contribution Deficiency (Excess)	$ -	$ -	$ -	$ -
Division's Covered-Employee Payroll	$ 6,367	$ 6,092	$ 6,783	$ 6,138
Contributions as a Percentage of Covered - Employee Payroll	12.00%	12.00%	12.00%	13.00%

(1) Represents employer's calendar year. Information prior to 2013 was not available. The Division will continue to present information for years available until a full ten-year trend is compiled.