Office of the Washington State Auditor
Pat McCarthy

Financial Statements Audit Report

# Lakehaven Water & Sewer District

**For the period January 1, 2019 through December 31, 2019**

**Published January 4, 2021**

**Report No. 1027636**

**Office of the Washington State Auditor**
**Pat McCarthy**

January 4, 2021

Board of Commissioners
Lakehaven Water & Sewer District
Federal Way, Washington

## Report on Financial Statements

Please find attached our report on the Lakehaven Water & Sewer District's financial statements.

We are issuing this report in order to provide information on the District's financial condition.

Sincerely,

Pat McCarthy

Pat McCarthy

State Auditor

Olympia, WA

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**Lakehaven Water & Sewer District**
**January 1, 2019 through December 31, 2019**

Board of Commissioners
Lakehaven Water & Sewer District
Federal Way, Washington

We have audited, 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, the financial statements of the Lakehaven Water & Sewer District, as of and for the year ended December 31, 2019, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated December 29, 2020.

As discussed in Note 15 to the financial statements, in February 2020, a state of emergency was declared, which could have a negative financial effect on the District.

## INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements, we considered the District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the District's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of the District's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## PURPOSE OF THIS REPORT

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the District's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

Pat McCarthy

State Auditor

Olympia, WA

December 29, 2020

# INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

**Lakehaven Water & Sewer District**
**January 1, 2019 through December 31, 2019**

Board of Commissioners
Lakehaven Water & Sewer District
Federal Way, Washington

## REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of the Lakehaven Water & Sewer District, as of and for the year ended December 31, 2019, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed on page 10.

### Management's Responsibilaity for the Financial Statements

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

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our 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 auditor’s judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the District’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 District’s internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

## Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Lakehaven Water & Sewer District, as of December 31, 2019, 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.

## Matters of Emphasis

As discussed in Note 15 to the financial statements, in February 2020, a state of emergency was declared, which could have negative financial effect in the District. Our opinion is not modified with respect to the 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 required supplementary information listed on page 10 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

## OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated December 29, 2020 on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

Pat McCarthy

Pat McCarthy

State Auditor

Olympia, WA

December 29, 2020

# FINANCIAL SECTION

**Lakehaven Water & Sewer District**
**January 1, 2019 through December 31, 2019**

## REQUIRED SUPPLEMENTARY INFORMATION

Management's Discussion and Analysis – 2019

## BASIC FINANCIAL STATEMENTS

Statement of Net Position – 2019
Statement of Revenues, Expenses and Changes in Fund Net Position – 2019
Statement of Cash Flows – 2019
Notes to Financial Statements – 2019

## REQUIRED SUPPLEMENTARY INFORMATION

Schedule of Proportionate Share of Net Pension Liability – PERS 1 and PERS 2/3 – 2019
Schedule of Employer Contributions – PERS 1, PERS 2/3 – 2019
Schedule of Changes in Total OPEB Liability and Related Ratios – 2019

Management's Discussion and Analysis (MD&A) presents a narrative overview and analysis of the financial activities of Lakehaven Water & Sewer District (the District) for the year ended December 31, 2019. Readers are encouraged to read this section in conjunction with the accompanying financial statements and notes to the financial statements, which follow.

## FINANCIAL HIGHLIGHTS

- As of December 31, 2019, the assets and deferred outflows of resources of the District exceeded its liabilities and deferred inflows of resources by $272.6 million (net position). Net position included net investment in capital assets of $225.2 million, restricted net position of $2.1 million and unrestricted net position of $45.2 million.
- In 2019, the District's total net position increased by $8.6 million.

## OVERVIEW OF THE FINANCIAL STATEMENTS

The District's basic financial statements include: A Statement of Net Position, a Statement of Revenues, Expenses & Changes in Fund Net Position, a Statement of Cash Flows and Notes to the Financial Statements. The financial statements are prepared based on the economic resources measurement focus and the full accrual basis of accounting and conform to generally accepted accounting principles as applicable to proprietary funds of governments.

The statement of net position presents total assets and deferred outflows of resources, and total liabilities and deferred inflows of resources with the difference between the two totals reported as net position. It provides information about the nature and amounts of investments in resources (assets), consumption of resources that are applicable to future periods (deferred outflows), obligations to District creditors (liabilities), and the acquisition of resources that are applicable to a future reporting period (deferred inflows). It provides the basis for evaluating the capital structure of the District and assessing the liquidity and financial flexibility of the District. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial condition of the District is improving or deteriorating.

The statement of revenues, expenses, and changes in fund net position presents the results of the business activities over the course of the year. All transactions that affect net position are included. Revenues are reported by major source. Expenses are reported by function. Revenue and expenses distinguish between operating and nonoperating. This statement can be used to determine whether the District has successfully recovered all its costs through its user fees and other charges, profitability and credit worthiness.

The statement of cash flows reports cash receipts, cash payments and net changes in cash resulting from operating, noncapital financing, capital and related financing, and investing activities over the course of the year. It presents information regarding where cash came from and what it was used for.

The notes to the financial statements provide additional information essential to a full understanding of the data provided in the financial statements. The notes disclose the District's significant accounting policies, significant account balances and activities, certain material risks, estimates, obligations, commitments, contingencies, and subsequent events, if any. The notes to the financial statements can be found immediately following the basic financial statements.

In addition to the basic financial statements and accompanying notes, required supplementary information is also presented. The required supplementary information immediately follows the notes to the financial statements.

The combining statements are presented in separate sections immediately after the required supplementary information for the purposes of additional analysis.

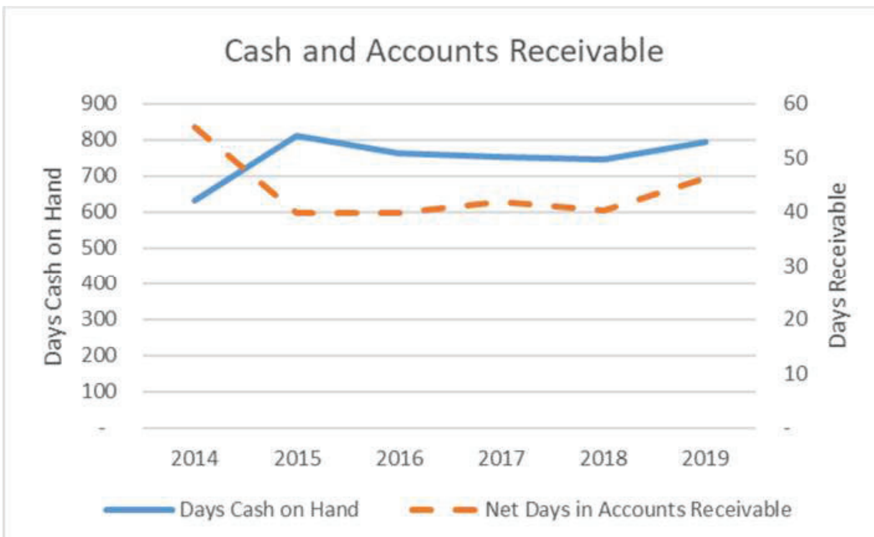
## ANALYSIS OF THE CONDENSED COMPARATIVE STATEMENT OF NET POSITION

The following condensed statement of net position presents the assets and deferred outflows of resources of the District as of December 31, 2019 and 2018 and shows the mix of liabilities and deferred inflows of resources and net position used to acquire these assets and deferred outflows of resources:

| | As of December 31, 2019 | | | As of December 31, 2018 | | |
|---|---|---|---|---|---|---|
| Assets | Water | Waste Water | Total | Water | Waste Water | Total |
| Current Assets | $ 38,932,738 | $ 25,653,804 | $ 64,586,542 | $ 33,848,279 | $ 24,294,062 | $ 58,142,341 |
| Noncurrent Assets | | | | | | |
| Capital Assets - Net | 124,271,671 | 121,161,257 | 245,432,928 | 124,834,663 | 118,193,496 | 243,028,159 |
| Total Assets | 163,204,409 | 146,815,061 | 310,019,470 | 158,682,942 | 142,487,558 | 301,170,500 |
| Deferred Outflow of Resources | | | | | | |
| Total Deferred Outflows | 166,149,090 | 147,545,540 | 313,694,630 | 455,478 | 455,478 | 910,956 |
| Liabilities | | | | | | |
| Current Liabilities | 4,578,069 | 5,632,603 | 10,210,672 | 3,710,417 | 3,186,126 | 6,896,543 |
| Noncurrent Liabilities: | 22,732,152 | 5,896,672 | 28,628,824 | 22,631,591 | 6,625,634 | 29,257,225 |
| Total Liabilities | 27,310,221 | 11,529,275 | 38,839,496 | 26,342,008 | 9,811,760 | 36,153,768 |
| Deferred Inflow of Resources | | | | | | |
| Total Deferred Inflows | 1,139,046 | 1,125,478 | 2,264,524 | 962,664 | 962,664 | 1,925,328 |
| Net Position | | | | | | |
| Net Investment in Capital Assets | 106,568,691 | 118,653,227 | 225,221,918 | 105,210,553 | 116,237,212 | 221,447,765 |
| Restricted | 1,046,469 | 1,083,126 | 2,129,595 | 5,143 | 5,227 | 10,370 |
| Unrestricted | 30,084,663 | 15,154,434 | 45,239,097 | 26,618,052 | 15,926,173 | 42,544,225 |
| Total Net Position | $137,699,823 | $134,890,787 | $272,590,610 | $131,833,748 | $132,168,612 | $264,002,360 |

Current assets consist of cash and cash equivalents held in the maintenance, construction and revenue accounts as well as accounts receivable, prepaid expenses, inventory, and accrued interest. Current assets increased by $6.4 million. The increase is due in part to the excess of revenues over expenses before capital contributions, which was $3.0 million. See the condensed comparative statement of revenues, expenses, and change in fund net position below.

Cash balances vary from year to year based on income from operations, expenses paid for operations and construction costs, borrowings and debt service payments. Customer accounts receivable increased slightly in 2019 primarily due to the timing of payments. Restricted cash increased as funds were reserved for utility taxes as described in Note 12. The District has experienced stable cash and accounts receivable over the last six years. See the days of cash on hand and accounts receivable chart below.

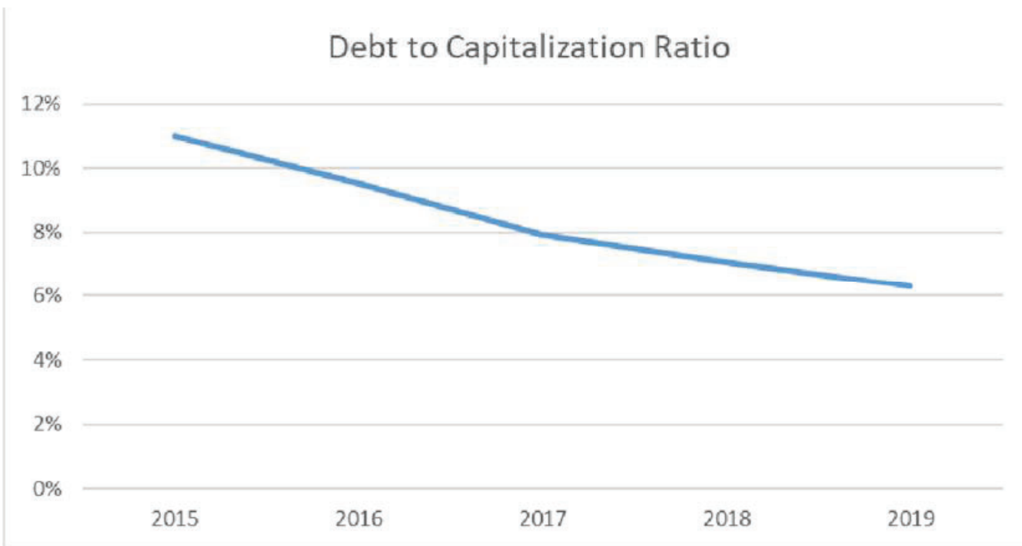



Capital assets consist of net capital assets, which include land, construction in progress, equipment, buildings, infrastructure and intangibles. Capital assets increased by $2.4 million in 2019. The increase was primarily due to increases in capital project spending, which was partially offset by depreciation expense.

Deferred Outflows of Resources consists of pension and OPEB deferred outflows, and deferral related to asset retirement obligations. Pension deferred outflows totaled $1,084,627 in 2019, an increase from $868,798 in 2018. The increase was primarily due to the net effect of differences between expected and actual experience and contributions subsequent to the measurement date. OPEB deferred outflows totaled $354,283 in 2019 an increase from $42,158 in 2018. The District implemented GASB 83 *Asset Retirement Obligations* in 2019 which resulted in a deferred outflow of $2,236,250 in 2019. See Note 15 for more information.

Current liabilities include accounts payable, deposits, interest payable on debt, retainage and the current portion of noncurrent debts. Current liabilities increased by $3.3 million in 2019. The increase was primarily due to the net effect of an increase in current accounts payable. The District had accounts payable of $6.2 million as of December 31, 2019 compared to $3.0 million as of December 31, 2018. The increase in accounts payable was due to the amount of excise tax being held (see Note 12 for more details) and the timing of payments made to vendors.

Noncurrent liabilities include the noncurrent portion of Public Works Trust Fund and State Revolving Fund loans. Noncurrent liabilities also include compensated absences, co-op certificates, pension liability, net other postemployment benefits and excise tax payable. Noncurrent liabilities decreased by $0.6 million in 2019. The decrease is primarily due a reduction in pension liability, a reduction in OPEB liability and is offset in part by the recognition of asset retirement obligations (see Note15 for more details). The District is continuing to pay down its debts, and the debt to capitalization ratio has decreased in the last five years. See the debt to capitalization ratio chart below.




Deferred Inflows of Resources consists of pension and OPEB. Pension deferred inflows increased by $0.3 million. The increase is due to net effect of differences in projected and actual earnings on pension plan investments, differences between expected and actual experience, and changes of assumptions.

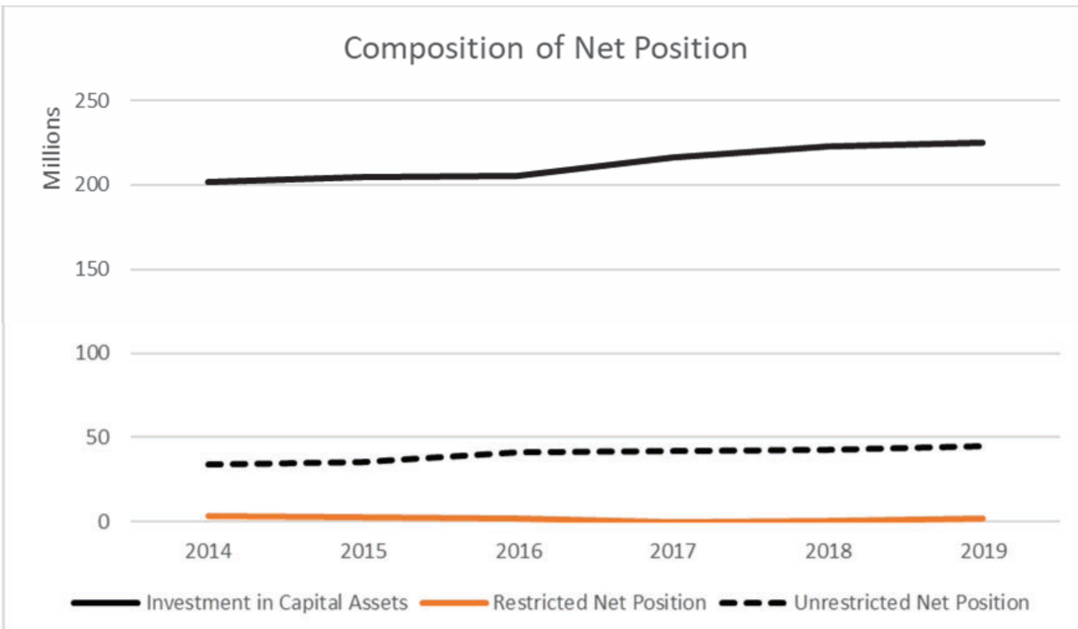
Net Position measures the amount by which assets and deferred outflows exceed the corresponding liabilities and deferred inflows. Over time this may serve as useful measure of the District's financial position. The total net position of $272.6 million is in three categories.

- Investment in Capital Assets represents the book value amount invested in capital assets net of depreciation and the related debt. The primary changes that affected this category were the continued lowering of the District's overall debt through the normal repayment and reduction of the principal partially offset by the net increase in the District's capital assets.

- The Restricted Net Position consists primarily of utility taxes collected as imposed by the City of Federal Way and held with the King County Investment Pool (see Note 12 for more details).

- The Unrestricted Net Position represents the District's unrestricted cash and investments, which is essentially anything that does not fall into the first two categories. The increase in this category is primarily the result of positive change in fund net position. The District is accumulating cash reserves in order to fund future capital and renovation projects.

The District's net position increased by $8.6 million in 2019. See the six years net position chart below. The increase in net position in 2019 reflects the District's ability to meet current and future obligations in the course of its activities.



## Analysis of the Condensed Comparative Statement of Revenues, Expenses, & Changes in Fund Net Position

The following statement of revenues, expenses, and changes in fund net position for the years ended December 31, 2019 and 2018 presents the annual surplus or deficiency of revenues over expenses (the change in net position):

| | As of December 31, 2019 | | | As of December 31, 2018 | | |
|---|---|---|---|---|---|---|
| Revenues | Water | Waste Water | Total | Water | Waste Water | Total |
| Operating Revenues | $ 17,258,527 | $ 19,276,497 | $ 36,535,024 | $ 17,042,091 | $ 18,330,303 | $ 35,372,394 |
| Investment Income | 998,035 | 682,840 | 1,680,875 | 505,523 | 403,200 | 908,723 |
| Gain on Sale of Capital Assets | - | - | - | 308 | 1,874 | 2,182 |
| Other Income | 946,274 | 68,017 | 1,014,291 | 918,037 | 78,696 | 996,733 |
| Total Revenues | 19,202,836 | 20,027,354 | 39,230,190 | 18,465,959 | 18,814,073 | 37,280,032 |
| Expenses | | | | | | |
| Maintenance & Operations | 7,694,870 | 10,874,814 | 18,569,684 | 7,027,042 | 12,021,755 | 19,048,797 |
| Administrative & General | 2,501,176 | 2,474,616 | 4,975,792 | 2,291,982 | 2,306,644 | 4,598,626 |
| Depreciation & Amortization | 4,432,356 | 4,675,108 | 9,107,464 | 4,238,471 | 4,385,381 | 8,623,852 |
| Taxes | 1,804,004 | 1,585,689 | 3,389,693 | 1,514,983 | 1,181,224 | 2,696,207 |
| Public Works & SRF Interest | 182,219 | 6,968 | 189,187 | 141,351 | (103,619) | 37,732 |
| Total Expenses | 16,614,625 | 19,617,195 | 36,231,820 | 15,213,829 | 19,791,385 | 35,005,214 |
| Change in Net Position before Capital Contributions | 2,588,211 | 410,159 | 2,998,370 | 3,252,130 | (977,312) | 2,274,818 |
| Capital Contributions | 3,277,863 | 2,312,017 | 5,589,880 | 2,433,622 | 5,506,163 | 7,939,785 |
| Change in Net Position | 5,866,074 | 2,722,176 | 8,588,250 | 5,685,752 | 4,528,851 | 10,214,603 |
| Total Net Position, January 1 | 131,833,749 | 132,168,611 | 264,002,360 | 126,147,996 | 127,639,761 | 253,787,757 |
| Total Net Position, December 31 | $137,699,823 | $134,890,787 | $272,590,610 | $131,833,748 | $132,168,612 | $264,002,360 |

### Revenues

Water operating revenues increased by $0.2 million in 2019 due to a general rate increase of 4.3% enacted in December 2018. Wastewater operating revenues increased by $0.9 million in 2019 due to a rate increase of 11.2% enacted in December 2018.

Investment income increased by $0.8 million in 2019. The increase was due to a higher average balance invested in the King County Investment Pool. The average balance being invested varies from year to year and can result in differences in the interest collected by the District.

Total operating revenues increased by $2.0 million in 2019.

### Expenses

Water maintenance and operations costs increased in 2019 by $0.7 million and Wastewater maintenance and operations costs decreased by $1.1 million in 2019. Total maintenance and operations costs decreased by $0.5 million in 2019.

The District had a slight increase in administrative and general expenses, approximately $0.4 million in 2019. Administrative and general expenses can vary over time.

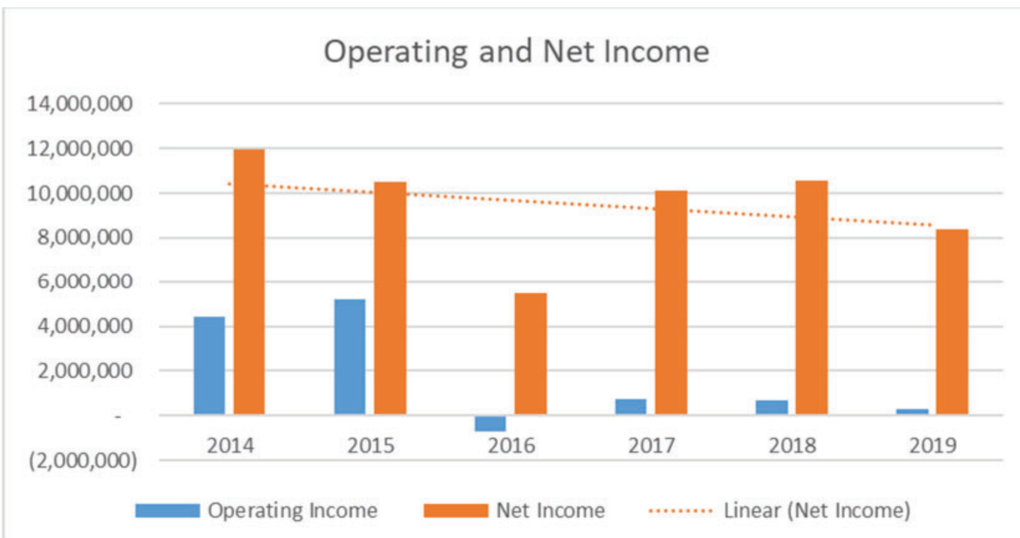
The increase in depreciation and amortization of $0.5 million was primarily due to the increase in depreciable capital assets in 2019.

Taxes are state and local assessments, not income taxes. The increases in taxes of $0.7 million were primarily due to the increase in the utility tax rate charged by the cities of Federal Way and Edgewood in 2019 (see Note 12 for more details).

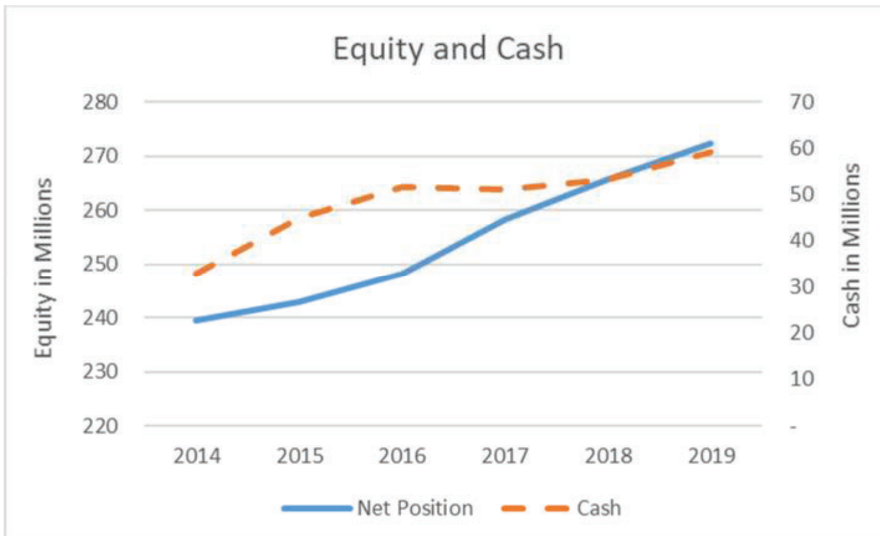
Interest expense increased because construction period interest was not capitalized under the new requirements of GASB 89, which was implemented by the District in 2019.

Capital Contributions

The District had $5.6 million capital contributions in 2019. It decreased from $7.9 million in 2018. This decrease is primarily due to completion of private development activity in the District during 2019.



Net Position
The District's operating revenues exceeded operating expenses for the last three years. For 2019 total revenues exceeded expenses before capital contributions by $3.0 million. This is an increase of $0.7 million over 2018. Capital contributions further added $5.6 million to the final increase in net position of $8.6 million. The Change in Net Position for 2019 was $1.6 million less than 2018. The overall financial position of the District has improved in 2019 and indicates its ability to meet its ongoing obligations.




**Capital Assets**

Capital assets consist of land, construction in progress, equipment, buildings, infrastructure, and intangibles. Net capital assets increased by $2.4 million in 2019. The increase was primarily due to spending for capital projects, which was partially offset by depreciation and amortization expense of $9.1 million.

Significant district capital projects included in the 2019 capital assets are: treatment upgrades totaling $3,017,828; I & I study totaling $2,878,373; and pumping improvements of $966,011.

Over the next ten years it is anticipated that capital spending will be in the range of $207 million with approximately 46% of that for water projects and 54% for wastewater projects. The areas of major emphasis in the capital budget include upgrades to water treatment & filtration, existing infrastructure, pump stations and additional water sources. See Note 3 for more information.

Capital assets for the years ended December 31, 2019 and 2018 were as follows:

| | Beginning Balance | Increase | Decrease | Ending Balance |
|---|---|---|---|---|
| Capital assets not being depreciated: | | | | |
| Land | $ 6,363,341 | $ - | $ - | $ 6,363,341 |
| Construction in progress | 18,192,928 | 2,506,770 | (8,378,047) | 12,321,651 |
| Total capital assets not being depreciated | 24,556,269 | 2,506,770 | (8,378,047) | 18,684,992 |
| Capital assets being depreciated: | | | | |
| Equipment | 35,243,895 | 6,901,841 | - | 42,145,736 |
| Buildings | 2,624,985 | - | - | 2,624,985 |
| Infrastructure | 283,551,636 | 6,391,376 | - | 289,943,012 |
| Intangibles | 70,575,480 | 4,090,292 | - | 74,665,772 |
| Total capital assets being depreciated | 391,995,996 | 17,383,509 | - | 409,379,505 |
| Less accumulated depreciation | | | | |
| Equipment | 16,518,343 | 1,674,479 | - | 18,192,822 |
| Buildings | 1,289,374 | 52,500 | - | 1,341,874 |
| Infrastructure | 138,187,982 | 5,686,819 | - | 143,874,801 |
| Intangibles | 17,528,406 | 1,693,666 | - | 19,222,072 |
| Total accumulated depreciation | 173,524,105 | 9,107,464 | - | 182,631,569 |
| Total capital assets being depreciated, net | 218,471,891 | 8,276,045 | - | 226,747,936 |
| **TOTAL CAPITAL ASSETS, NET** | **$ 243,028,160** | **$ 10,782,815** | **$ (8,378,047)** | **$ 245,432,928** |

## Additional Comments

In addition to the rate increases in 2019 the District has planned Water rate increases of approximately 1.75%/year for 2020 through 2022. The District has planned Wastewater rate increases of approximately 2.8%/year for 2020 through 2022. On March 27, 2019, the City of Federal Way imposed a 7.75% utility tax on all District water and sewer revenue within the city limits. Effective June 1, 2019, the City of Edgewood imposed a 6% utility tax on all District water and sewer revenue within the city limits. These taxes are included in the planned rates.

## Request for Information

This financial report is designed to provide a general overview of the District's finances to all those with an interest in the District's finances. Questions concerning any information provided in this report should be addressed to: Lakehaven Water and Sewer District, 31627 1st Avenue South, Federal Way, WA 98063.

Lakehaven Water & Sewer District
Statement of Net Position
December 31, 2019

| ASSETS | 2019 |
|---|---|
| **Current Assets** | |
| Cash and Cash Equivalents | $ 56,955,116 |
| Accrued Interest Receivable | 111,378 |
| Accounts Receivable - Customers | 4,329,860 |
| Accounts Receivable - Other | 58,607 |
| Inventory | 426,681 |
| Prepaid Expenses | 575,305 |
| Restricted Assets – Cash and Cash Equivalents | 2,129,595 |
| Total Current Assets | 64,586,542 |
| **Noncurrent Assets** | |
| Capital Assets Not Being Depreciated: | |
| - Land | 6,363,341 |
| - Construction in Progress | 12,321,651 |
| Capital Assets Being Depreciated: | |
| - Equipment | 42,145,736 |
| - Buildings | 2,624,985 |
| - Infrastructure | 289,943,012 |
| - Intangibles | 74,665,772 |
| - Less Accumulated Depreciation & Amortization | (182,631,569) |
| Total Capital Assets Being Depreciated | 226,747,936 |
| Total Capital Assets | 245,432,928 |
| Total Noncurrent Assets | 245,432,928 |
| Total Assets | 310,019,470 |
| **DEFERRED OUTFLOWS OF RESOURCES** | |
| Deferred Outflows - Pension | 1,084,627 |
| Deferred Outflows – OPEB | 354,283 |
| Deferred Outflows – Asset Retirement Obligation | 2,236,250 |
| Total Deferred Outflows of Resources | 3,675,160 |
| Total Assets and Deferred Outflows of Resources | $ 313,694,630 |

The notes to the financial statements are an integral part of this statement.

Lakehaven Water & Sewer District
Statement of Net Position
December 31, 2019

| | | 2019 |
|---|---|---|
| **LIABILITIES** | | |
| Current Liabilities | | |
| Accounts Payable | $ | 6,202,559 |
| Deposits, Customers & Developers | | 1,853,084 |
| Retainage Due Contractors | | 137,278 |
| Public Works Trust Fund & State Revolving Fund Loans (Current Portion) | | 1,958,080 |
| Interest Payable | | 59,671 |
| Total Current Liabilities | | 10,210,672 |
| Noncurrent Liabilities | | |
| Public Works Trust Fund & State Revolving Fund Loans (Less Current Portion) | | 16,396,632 |
| Compensated Absences | | 887,540 |
| Net Pension Liability | | 3,701,815 |
| Accrued Other Postemployment | | 5,381,587 |
| Asset Retirement Obligation | | 2,236,250 |
| Other Noncurrent Liabilities | | 25,000 |
| Total Noncurrent Liabilities | | 28,628,824 |
| Total Liabilities | | 38,839,496 |
| **DEFERRED INFLOWS OF RESOURCES** | | |
| Deferred Inflows - Pension | | 2,008,398 |
| Deferred Inflows – OPEB | | 256,126 |
| Total Deferred Inflows of Resources | | 2,264,524 |
| Total Liabilities and Deferred Inflows of Resources | | 41,104,020 |
| **NET POSITION** | | |
| Net Investment in Capital Assets | | 225,221,918 |
| Restricted | | 2,129,595 |
| Unrestricted | | 45,239,097 |
| Total Net Position | $ | 272,590,610 |

The notes to the financial statements are an integral part of this statement.

Lakehaven Water & Sewer District
Statement of Revenues, Expenses and Changes in Fund Net Position
Year Ended December 31, 2019

| | 2019 |
|---|---|
| Operating Revenues | |
| Customer Sales & Service Fees | $ 34,571,463 |
| Permits, Inspection & Delinquency Fees | 435,604 |
| Developer Revenues & Administrative Charges | 1,438,169 |
| Street Lighting Revenues | 89,788 |
| Total Operating Revenues | 36,535,024 |
| Operating Expenses | |
| Maintenance & Operations | 18,569,684 |
| Administrative & General | 4,975,792 |
| Depreciation & Amortization | 9,107,464 |
| Taxes, Other Than Income Tax | 3,389,693 |
| Total Operating Expenses | 36,042,633 |
| Net Operating Income | 492,391 |
| Nonoperating Revenues (Expenses) | |
| Interest Expense | (189,187) |
| Investment Income | 1,680,875 |
| Other Income | 1,014,291 |
| Total Nonoperating Revenues (Expenses) | 2,505,979 |
| Income Before Capital Contributions | 2,998,370 |
| Capital Contributions | 5,589,880 |
| Change in Net Position | 8,588,250 |
| Total Net Position, January 1 | 264,002,360 |
| Total Net Position, December 31 | $ 272,590,610 |

The notes to the financial statements are an integral part of this statement.

Lakehaven Water & Sewer District
Statement of Cash Flows
Year Ended December 31, 2019

| | 2019 |
|---|---|
| **Cash Flows from Operating Activities** | |
| Cash Received from Customers | $ 37,092,632 |
| Cash Paid to Suppliers | (13,963,902) |
| Cash Paid to Employees | (14,168,265) |
| Net Cash Provided by Operating Activities | 8,960,465 |
| **Cash Flows from Capital & Related Financing Activities** | |
| Acquisition & Construction of Capital Assets | (9,784,991) |
| Asset Retirement Obligation | 2,236,250 |
| Payments of Bond Principal & Other Financing | (2,211,370) |
| Interest Paid | (261,210) |
| Cash Contributions in Aid of Construction | 5,173,592 |
| Net Cash Used in Capital & Related Financing Activities | (4,847,729) |
| **Cash Flows from Investing Activities** | |
| Interest Received on Investments | 1,666,043 |
| Net Cash Provided by Investing Activities | 1,666,043 |
| **Net Increase in Cash & Cash Equivalents** | 5,778,779 |
| Cash & Cash Equivalents - January 1 | 53,305,932 |
| Cash & Cash Equivalents - December 31 | $ 59,084,711 |
| **Noncash Investing, Capital and Financing Activities** | |
| Contributions of Capital Assets from Developers | $ 396,980 |

The notes to the financial statements are an integral part of this statement.

Lakehaven Water & Sewer District
Statement of Cash Flows
Year Ended December 31, 2019

| | | 2019 |
|---|---|---|
| Reconciliation of Net Operating Income to Net Cash Provided by Operating Activities | | |
| Net Operating Income | $ | 492,391 |
| Adjustments to Reconcile Net Operating Income to Net Cash Provided by Operating Activities | | |
| Depreciation & Amortization | | 9,107,464 |
| Other Income | | 1,014,291 |
| Changes in Assets, Deferred Outflows of Resources Liabilities & Deferred Inflows of Resources | | |
| Increase in Accounts Receivable | | (456,684) |
| Increase in Inventory | | (150,893) |
| Decrease in Prepaid Expenses | | 648,185 |
| Increase in Accounts Payable | | 985,354 |
| Increase in Compensated Absences | | 23,995 |
| Increase in Deferred Outflows of Resources | | (2,764,204) |
| Increase in Deferred Inflows of Resources | | 339,196 |
| Decrease in Net Pension Liability | | (938,575) |
| Increase in OPEB Liability | | 659,945 |
| Total Changes | | (1,653,681) |
| Net Cash Provided by Operating Activities | $ | 8,960,465 |

The notes to the financial statements are an integral part of this statement.

## NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of Lakehaven Water & Sewer District (the District) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applicable to proprietary funds of governments. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The following is a summary of the most significant accounting policies of the District:

### Reporting Entity

The District is a municipal corporation governed by a five-member elected board. The District's primary activity is to provide water and wastewater services to residential and commercial customers within the District's boundaries. As required by generally accepted accounting principles, management has considered all potential component units in defining the reporting entity. The District has no component units.

### Basis of Accounting and Presentation

The District uses a single enterprise fund and its financial statements are presented based on the flow of economic resources measurement focus and the full accrual basis of accounting. The proprietary fund is comprised of two divisions: water and wastewater. Revenues are recognized when earned and expenses are recognized when incurred, regardless of the timing of related cash flows. Unbilled utility service receivables are accrued at year-end.

The District distinguishes between operating revenues and expenses, and nonoperating revenues and expenses. Operating revenues and expenses result from providing services, and from producing and delivering goods in connection with the District's principal ongoing operations. The principal operating revenues of the District are charges to customers for water and wastewater sales and other related services. Operating expenses pertain to the furnishing of those services which include the costs of sales and services, administration expenses and depreciation expense. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

### Cash and Cash Equivalents

Cash and cash equivalents consist of bank accounts maintained at U.S. Bank, pooled investments in the King County Investment Pool (the KCIP) and restricted cash maintained in the KCIP and by the Pierce County Clerk of Court. For purposes of the statement of cash flows, the District considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

The District voluntarily participates in the KCIP maintained by the King County Treasury Operation Section. The King County Treasurer acts as custodian for the District's cash. The KCIP functions essentially as a demand deposit account where the District receives an allocation of its proportionate share of pooled earnings. Interest earnings distributed are used for the District's operations. The District's equity share of the KCIP's net position is reported on the statement of net position as cash and cash equivalents and reflects the change in fair value of the corresponding investment securities. See Note 2, Deposits and Investments.

Receivables

Receivables consist primarily of amounts due from water and sewer customers. All receivables are recorded when earned. No allowance for uncollectible accounts is provided since the District has the authority to record liens for its receivables and does not experience significant uncollectible amounts.

Inventories

Inventories are valued at average cost.

Prepaids

Payments made in advance to vendors for certain goods or services, such as insurance, that will benefit future periods are recorded as prepaid items. The expenditures are recognized in the period of consumption.

Capital Assets

Capital assets include land, construction in progress, buildings, equipment, infrastructure, and intangible assets. Construction in progress reports all costs associated with projects being developed. Costs relating to projects which are ultimately put into service are transferred to capitalized utility plant. Costs relating to abandoned projects are charged to expense when it is determined that they will not be put into service. Assets acquired through contributions are recorded as additions to the appropriate property, plant and equipment accounts.

Capital assets are defined by the District as assets with an initial individual cost of more than $5,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost when purchased or constructed. Donated capital assets are recorded at acquisition value at the date of donation. Costs for additions or improvements to capital assets are capitalized when they increase the life, effectiveness or efficiency of the asset. Expenditures for maintenance and repairs are charged to expenses as incurred. It is the District's policy to capitalize interest on construction of governmental capital assets.

Provision for depreciation is computed on the straight-line method with the following estimated useful lives:

Equipment, 3 - 25 years;
Buildings, 50 years;
Infrastructure, 10 - 50 years;
Intangibles, 10 - 50 years.

Upon retirement of an asset, the cost of the asset and the related accumulated depreciation are removed from the property accounts and the gain or loss is reflected in the statement of revenues, expenses and changes in fund net position. See Note 3.

Compensated Absences

Compensated absences are absences for which employees will be paid, such as vacation and sick leave. Employees may accumulate and be paid upon retirement or other separation from employment a maximum of 320 hours of vacation/sick leave time. The District accrues accumulated vacation/sick leave benefits.

Unemployment Insurance

The District is on the reimbursable method with the State of Washington for unemployment compensation. The District does not have a reserve account for this liability, should it occur.

Medical Insurance

The District's medical, dental and life insurance program is purchased through Health Care Authority of the State of Washington (see Note 9).

Costs Arising Out of Developer Extensions

The Board of Commissioners adopted resolutions establishing a procedure which reimburses the District for costs associated with the preparation and execution of the Developer Extension Agreements.

Capital Contributions

Grants, ULID assessments, and contributions in aid of construction from property owners are recorded as capital contributions in the statement of revenues, expenses and changes in fund net position.

Noncurrent Debt

Noncurrent debt is recorded net of premiums and discounts. Premiums and discounts on noncurrent debt are amortized by the interest method over the period the related debt is outstanding. Amortization of discounts/premiums is included in interest expense.

Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of recourses related to pensions, and pension expense, information about the fiduciary net position of all state sponsored pension plans and additions to/deductions from those plans' fiduciary net position have been determined on the same basis as they are reported by the Washington State Department of Retirement Systems. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Deferred Outflows/Inflows of Resources

Deferred outflows of resources represent a consumption of net position that applies to future periods and will not be recognized as an outflow of resources (expense) until that time. Deferred outflows of resources relating to pension plans consist of contributions subsequent to the measurement date and the District's proportionate share of deferred outflows related to those plans. Pension plan contributions subsequent to the measurement date are recognized as a reduction of the net pension liability in the following year. Deferred outflows of resources for the net difference between projected and actual earnings on plan investments are amortized over a closed five-year period. The remaining deferred outflows of resources related to pensions are amortized over the average expected service lives of all employees provided with pensions through each plan. Deferred outflows relating to other post-employment benefits (OPEB) are similar to pension described above.

Deferred inflows of resources represent an acquisition of net position that applies to future periods and will not be recognized as an inflow of resources (revenue) until that time. Deferred inflows of resources consist of the District's proportionate share of deferred inflows related to pension plans. Deferred inflows of resources for the net difference between projected and actual earnings on plan investments are amortized over a closed five-year period. The remaining deferred inflows of resources related to pensions are amortized over the average expected service lives of all employees provided with pensions through each plan.

In 2019, the District implemented GASB Statement 83 and recognized the deferred outflows of resources for its asset retirement obligations. The recognition of deferred outflows is to offset the liability recognized.

Net Position
Net position is classified in the following three components:

*Net Investment in Capital Assets* - This component of net position consists of capital assets, net of accumulated depreciation, and capital-related deferred outflows of resources reduced by the outstanding balances of any capital-related borrowings and deferred inflows of resources. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net position component as the unspent proceeds.

*Restricted* - This component of net position consists of assets restricted by external creditors (such as through debt covenants), grantors, contributors or others reduced by related liabilities and deferred inflows of resources, that restrict the use of net assets.

*Unrestricted Net Position* - This component of net position consists of all net position that does not meet the definition of "restricted" or "net investment in capital assets."

Use of Estimates
The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Accounting Pronouncements
GASB Statement No. 83, *Certain Asset Retirement Obligation*. This new GASB statement establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for asset retirement obligations. It requires that recognition occur when the liability is both incurred and reasonably estimable. It is effective for reporting periods beginning after

June 15, 2018. The District implemented this new GASB statement in 2019. See Note 15 Asset Retirement Obligations for more details.

GASB Statement No. 84, *Fiduciary Activities*. This new GASB statement establishes criteria for identifying fiduciary activities of all state and local governments. An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements. It is effective for reporting periods beginning after December 15, 2018. Management has determined that this new GASB statement is not applicable to the District.

GASB Statement No. 87, *Leases*. This new GASB statement establishes a single model for lease accounting based on the foundational principle that leases are financing of the right to use an underlying asset. Under this statement, a lessee is required to recognize a lease liability and an intangible right-to- use lease asset. It is effective for reporting periods beginning after December 15, 2019. The District is currently evaluating the impact of this new GASB statement.

GASB Statement No. 88, *Certain Disclosures Related to Debt*, including Direct Borrowings and Direct Placements. This statement defines debt for purposes of disclosure in notes to financial statements as a liability that arises from a contractual obligation to pay cash in one or more payments to settle an amount that is fixed at the date the contractual obligation is established. It is effective for reporting periods beginning after June 15, 2018. The District implemented this new GASB statement in 2019.

GASB Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*. This new GASB statement establishes accounting requirements for interest cost incurred before the end of a construction period. It is effective for reporting periods beginning after December 15, 2019. The District implemented this new GASB statement in 2019.

GASB Statement No. 90, *Majority Equity Interests* – an amendment of GASB Statements No. 14 and No.61. This new GASB statement defines a majority equity interest and specifies that a majority equity interest in a legally separate organization should be reported as an investment if a government's holding of the equity interest meets the definition of an investment. A majority equity interest that meets the definition of an investment should be measured using the equity method at fair value. It is effective for reporting period beginning after December 15, 2018. Management has determined that this new GASB statement is not applicable to the District.

GASB Statement No. 91, *Conduit Debt Obligations*. This new GASB statement defines conduit debt obligation and requires issuers to disclose information about the conduit debt obligations organized by type of commitment and improve comparability by removing the diversity in current practice. This statement also includes note disclosures that help inform users of the potential impact of commitments on financial resources. It is effective for reporting beginning after December 15, 2020. Earlier application is encouraged. The District is currently evaluating the impact of this new GASB statement.

GASB Statement No. 92, *Omnibus 2020*. This new GASB statement addresses a variety of topics including issues related to reinsurance recoveries and terminology used to refer to derivative instruments, intra-entity transfers, postemployment benefit arrangements, and the measurement of liabilities (and assets, if any) associated with asset retirement obligations in a government acquisition. It is effective for periods beginning after June 15, 2020. Earlier application is encouraged and is permitted by topic. The District is currently evaluating the impact of this new GASB statement.

GASB Statement No. 93, *Replacement of Interbank Offered Rates*. This statement removes interbank offered rate (IBOR) as an appropriate benchmark interest rate and identifies a Security Overnight Financing Rate and the Effective Federal Funds Rate as appropriate benchmark interest rates for the qualitative evaluation of the effectiveness of an interest rate swap. The removal of LIBOR is effective for reporting periods ending after December 31, 2020. All other requirements are effective for reporting periods beginning after June 15, 2020. Earlier application is encouraged. The District is currently evaluating the impact of this new GASB statement.

**NOTE 2 DEPOSITS AND INVESTMENTS**

The District's cash and investment balances at December 31, 2019 are listed below:

| | |
|---|---|
| Bank Deposits | $ 26,250 |
| Restricted cash in Pierce County | 58,619 |
| Restricted cash deposit Tacoma Public Utilities | 151,683 |
| Investment in King County Investment Pool | 58,848,159 |
| Total Cash & Investments | $ 59,084,711 |

The District's deposits in bank accounts are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC).

Unimpaired Investments in King County Investment Pool

In accordance with state investment laws, the District's governing body has entered into a formal Interlocal agreement with the District's *ex officio* treasurer, King County, to have all its funds not required for immediate expenditure to be invested in the King County Investment Pool (KCIP).

The KCIP is not registered with the Securities and Exchange Commission as an investment company. Oversight is provided by the King County Executive Finance Committee (EFC), which serves the role of the County Finance Committee as defined in RCW 36.48.070. All investments are subject to written policies and procedures adopted by the EFC.

The District receives an allocation of its proportionate share of pooled earnings. Unrealized gains and losses due to changes in the fair values are not distributed to the District. However, the District has adopted GASB 72 and reports its investments in the KCIP at fair value. The unrealized gains or losses are recognized in the statement of revenues, expenses, and changes in fund net position.

As of December 31, 2019, the District had the following unimpaired investments in the KCIP:

| Investment Type | Fair Value | Effective Duration |
|---|---|---|
| King County Investment Pool | $ 58,848,159 | .92 Years |

The District categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation of inputs used to measure the fair value of assets. Level 1 inputs are quoted prices in an active market from identical assets, Level 2 inputs are significant other observable inputs, and Level 3 inputs are significant unobservable inputs. The following is a summary of inputs in valuing the District's unimpaired investment in the KCIP as of December 31, 2019:

| | | **Fair Value Measurements Using** | | |
|---|---|---|---|---|
| **Investments at Fair Value Level** | **Fair Value 12/31/19** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Unobserv-able Inputs (Level 3)** |
| Governmental Agencies | $ 18,076,370 | $ - | $ 18,076,370 | $ - |
| Commercial Paper | 4,121,648 | - | 4,121,648 | - |
| Corporate Notes | 7,124,563 | - | 7,124,563 | - |
| U.S. Agency Mortgage-backed Securities | 58,880 | - | 58,880 | - |
| Treasury Securities | 22,786,825 | 22,786,825 | - | - |
| Subtotals | $ 52,168,287 | $ 22,786,825 | $ 29,381,461 | **$ -** |
| **Investments measured at amortized cost (not subject to Fair Value Hierarchy)** | | | | |
| Repurchase Agreements | $ 996,121 | | | |
| State government Investment Pool | 5,683,751 | | | |
| Subtotal investments measured at cost | 6,679,872 | | | |
| **Total investments in Investment Pool** | **$ 58,848,159** | | | |

U.S. Treasury Securities are valued using quoted prices in active markets and classified in Level 1 of the fair value hierarchy.

U.S. Agency Securities, Commercial Paper, Bank Corporate Notes and U.S. Agency Mortgage-backed Securities are valued using standard inputs including benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data including market research publications.

Repurchase Agreements and State Government Investment Pool are overnight securities and are not subject to GASB Statement No. 72 and reported at amortized costs.

Impaired Investment Pool

The King County Executive Finance Committee approved the bifurcation of the investment pool as of September 1, 2008. This separated the impaired investments into their own pool distinct from the main pool of performing investments. The reasons for bifurcating the pool were to: (1) ensure the yield on the performing assets is not negatively impacted by the impaired investments; (2) enhance transparency about the value of the performing pool and the impaired pool; and (3) ease the implementation of the restructuring processes for the impaired investments.

For the bifurcation, three impaired commercial paper investments were placed into an impaired investment pool (the impaired pool). The impaired pool holds one commercial paper asset (Victoria), in which the County accepted an exchange offer in 2009 and is receiving cash flows from the investment's underlying securities. For the other two commercial paper investments (Cheyne and Rhinebridge), the County accepted a cash-out option in 2008, based on the results of the separate restructuring auctions conducted by the designated "receiver" of each commercial paper asset.

As of December 31, 2019, the impaired pool held one commercial paper asset where the impaired pool accepted an exchange offer and is receiving the cash flows from the investment's underlying securities. The impaired pool also held the residual investments in two commercial paper assets that were part of completed enforcement event, where the impaired pool accepted the cash out option. all impaired commercial paper investments have completed enforcement events. The District's share of the impaired pool principal was $28,977 and the total fair value of these investments was $19,500. As a result of the bifurcation in 2008, the District wrote off its impaired investments. The District reported the impaired investments when receiving the distributions from the impaired pool as interest income on the statement of revenues, expenses and changes in fund net position.

*Interest Rate Risk*. As of December 31, 2019, the Pool's average duration was 0.92 years. As a means of limiting its exposure to rising interest rates, securities purchased in the KCIP must have a final maturity, or weighted average life, no longer than five years. While the KCIP's market value is calculated on a monthly basis, unrealized gains and losses are not distributed to participants. The KCIP distributes earnings monthly using an amortized cost methodology.

*Credit Risk*. As of December 31, 2019, the District's investment in the KCIP was not rated by a nationally recognized statistical rating organization (NRSRO). In compliance with state statutes, KCIP's policies authorize investments in U.S. Treasury securities, U.S. agency securities and mortgage-backed securities, corporate notes (rated at least "A" by two NRSROs), municipal securities (rated at least "A" by two NRSROs), commercial paper (rated at least the equivalent of "A-1" by two NRSROs), certificates of deposits issued by qualified public depositaries, repurchase agreements, and the Local Government Investment Pool managed by the Washington State Treasurer's office.

## NOTE 3 CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2019 were as follows:

| | Beginning Balance | Increase | Decrease | Ending Balance |
|---|---|---|---|---|
| Capital assets not being depreciated: | | | | |
| Land | $ 6,363,341 | $ - | $ - | $ 6,363,341 |
| Construction in progress | 18,192,928 | 2,506,770 | (8,378,047) | 12,321,651 |
| Total capital assets not being depreciated | 24,556,269 | 2,506,770 | (8,378,047) | 18,684,992 |
| Capital assets being depreciated: | | | | |
| Equipment | 35,243,895 | 6,901,841 | - | 42,145,736 |
| Buildings | 2,624,985 | - | - | 2,624,985 |
| Infrastructure | 283,551,636 | 6,391,376 | - | 289,943,012 |
| Intangibles | 70,575,480 | 4,090,292 | - | 74,665,772 |
| Total capital assets being depreciated | 391,995,996 | 17,383,509 | - | 409,379,505 |
| Less accumulated depreciation | | | | |
| Equipment | (16,518,343) | (1,674,479) | - | (18,192,822) |
| Buildings | (1,289,374) | (52,500) | - | (1,341,874) |
| Infrastructure | (138,187,982) | (5,686,819) | - | (143,874,801) |
| Intangibles | (17,528,406) | (1,693,666) | - | (19,222,072) |
| Total accumulated depreciation | (173,524,105) | (9,107,464) | - | (182,631,569) |
| Total capital assets being depreciated, net | 218,471,891 | 8,276,045 | - | 226,747,936 |
| **TOTAL CAPITAL ASSETS, NET** | **$ 243,028,160** | **$ 10,782,815** | **$ (8,378,047)** | **$ 245,432,928** |

The District capitalizes employee wages and benefit costs in connection with the construction of utility plant assets. In 2019, total wage and benefit costs of $1,838,505 was capitalized.

The District implemented GASB 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*, and interest costs incurred for the construction of capital assets during the reporting period are no longer capitalized.

Total depreciation expense of $9,107,464 was reported on the accompanying statement of revenues, expenses and changes in fund net position.

## NOTE 4 RESTRICTED ASSETS

In accordance with the bond resolutions and other agreements, separate restricted accounts are required to be established. The assets held in these accounts are restricted for specific uses. As of the end of 2019, the cash and cash equivalents held in the Revenue Bond Fund were no longer restricted as all the outstanding bonds were paid off in 2017. The restricted cash account had not been closed yet. The remaining balance was $251 at December 31, 2019.

Restricted cash and cash equivalents also included utility tax payable to City of Federal Way and City of Edgewood as required by the contractual terms. See Note 12 Franchise Fees.

Restricted cash and cash equivalents are invested into the King County Investment Pool and reported at fair value. See Note 2 Deposits and Investments.

## NOTE 5 DEFERRED COMPENSATION PLAN

Pursuant to RCW 41.50.770, Washington State offers its employees and employees of those political subdivisions that elect to participate, a deferred compensation program, in accordance with Internal Revenue Code Section 457. The deferred compensation is not available to employees until termination, retirement, disability, death or unforeseeable financial emergency. This deferred compensation plan is administered by the Washington State Department of Retirement Systems (DRS). Employee deferrals totaled $358,741 in 2019. These assets have been excluded from the accompanying financial statements.

## NOTE 6 OPERATING LEASES

In April 2014, the District entered into a noncancellable operating lease agreement with Ricoh USA, Inc. for two copy machines. The lease payments began in 2014 and the terms are for 60 months with payments of $2,123 made quarterly.

In June 2014, the District entered into a noncancellable operating lease agreement with Ricoh USA, Inc. for one copy machine. The lease payments began in 2014 and the terms are for 60 months with payments of $1,740 made quarterly. The contract also calls for a one-time payment of $10,000 for a service contract on the machine.

In January 2015, the District entered into a noncancellable operating lease agreement with Ricoh USA, Inc. for four copy machines. The lease payments began in 2015 and the terms are for 60 months with payments of $2,046 made quarterly. The contract also calls for a one-time payment totaling $12,050 for service contracts on the machines.

In December 2015, the District entered into a noncancellable operating lease agreement with Ricoh USA, Inc. for three copy machines. The lease payments began in 2016 and the terms are for 60 months with payments of $2,184 made quarterly. The contract also calls for a one-time payment totaling $7,456 for service contracts on the machines.

In April 2016, the District entered into a noncancellable operating lease agreement with Ricoh USA, Inc. for one copy machine. The lease payments began in 2018 and the terms are for 60 months with payments of $1,008 made quarterly. The contract also calls for additional quarterly payments of $315 for a service contract on the machine.

In November 2019, the District entered into a lease agreement with Pacific Office Automation for one color printer. The lease payments began in 2019 and the terms are for 60 months with payments of $164 made quarterly.

In 2019, the District entered into three operating leases, including one stamp machine and two copy machines. The lease payments for all new leases in 2019 have terms for 60 months. The quarterly lease payments range from $1,028 to $1,144

At December 31, 2019 the future minimum lease payments under these leases are as follows:

| Year Ended December 31, | Amount |
|---|---|
| 2020 | $ 31,082 |
| 2021 | 16,221 |
| 2022 | 15,482 |
| 2023 | 15,361 |
| 2024 | 7,350 |
| Total future minimum lease payments | $ 85,496 |

## NOTE 7 NONCURRENT DEBTS AND LIABILITIES

The District implemented GASB 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*. All of the District's loans below are direct borrowings.

**Direct Borrowings**

The District has entered into agreements with the Department of Community, Trade and Economic Development of the State of Washington to receive the following Public Works Trust Fund and State Revolving Fund long term loans as direct borrowings as follows:

| Type | Contract | Project | Origination Date | Maurity Date | Interest Rate | Original Debt | Current Balance |
|---|---|---|---|---|---|---|---|
| Loan | PW-00-691-34 | Wastewater treatment plant upgrades | 3/30/2000 | 7/1/2020 | 1.000% | $ 1,575,700 | $ 83,392 |
| Loan | PW-02-691-031 | Second supply project | 3/28/2002 | 7/1/2022 | 0.500% | 10,000,000 | 1,588,235 |
| Loan | PW-04-691-039 | Water filtration at various well sites | 4/8/2004 | 7/1/2024 | 0.228% | 1,700,000 | 472,533 |
| Loan | PW-04-691-PRE-130 | Redondo outfall replacement | 6/30/2004 | 7/1/2024 | 0.500% | 570,705 | 151,950 |
| Loan | PW-06-962-021 | Redondo outfall replacement | 6/5/2006 | 7/1/2026 | 0.500% | 2,400,000 | 911,228 |
| Loan | PC-12-951-018 | Green River Water Treatment Plant Filtration Facility | 4/8/2004 | 6/1/2031 | 0.500% | 10,000,000 | 6,430,810 |
| Loan | DM 12-952-108 | Green River Filtration Facility | 6/3/2012 | 10/1/2035 | 1.500% | 5,982,486 | 4,816,222 |
| Loan | DM 10-952-030 | Green River Treatment Plant/Filtration Facility | 8/26/2010 | 10/1/2034 | 1.500% | 3,030,000 | 2,284,342 |
| Loan | DM 11-952-021 | Green River Treatment Plant/Filtration Facility | 6/30/2011 | 10/1/2035 | 1.500% | 2,020,000 | 1,616,000 |
| | | | | | | Total Outstanding | 18,354,712 |
| | | | | | | Less: Current portion | (1,958,080) |
| | | | | | | Long Term Debt | $ 16,396,632 |

The District has pledged future water and wastewater net revenue to repay $18,354,712 in loans issued between 2000 and 2011. The loans are payable through 2035. The loans are revenue obligations of the District payable solely from the net revenue of the district. Net revenue means gross revenue minus expenses of maintenance and operations. The District retains the right to issue future bonds and notes that constitute a lien and change on net revenue superior to the liens and charges of the existing loan contracts. The District has the right to repay the unpaid balance of the loan in full at any time or make accelerated payments without penalty.

Loans payments 30 days or more delinquent will be assessed a daily penalty of 12% per annum on the entire due balance. If the lender terminates the loan agreement for cause or convenience there is no effect on the District's obligations to repay the unpaid balance of the loan.

The annual debt service requirements to maturity for debt from direct borrowings and direct placements are as follows:

| Year | Principal | Interest |
|---|---|---|
| 2020 | $ 1,958,080 | $ 179,356 |
| 2021 | 1,874,688 | 163,606 |
| 2022 | 1,874,688 | 148,689 |
| 2023 | 1,345,276 | 133,773 |
| 2024 | 1,345,276 | 121,503 |
| 2025-2029 | 5,711,371 | 431,673 |
| 2030-2034 | 3,843,318 | 162,908 |
| 2035-2039 | 402,015 | 6,030 |
| | $ 18,354,712 | $ 1,347,538 |

Changes in Noncurrent Liabilities

| Description | Beginning Balance | Additions | Reductions | Ending Balance | Due Within One Year |
|---|---|---|---|---|---|
| Loans | $ 20,566,082 | $ - | $ (2,211,370) | $ 18,354,712 | $ 1,958,080 |
| Pension Liability | 4,640,392 | - | (938,577) | 3,701,815 | - |
| OPEB | 4,721,642 | 659,945 | - | 5,381,587 | - |
| Compensated Absences | 863,544 | 23,996 | - | 887,540 | - |
| Other Long-term Liabilities | 707,168 | 1,094,761 | - | 1,801,929 | 1,776,929 |
| | $ 31,498,828 | $ 1,778,702 | $ (3,149,947) | $ 30,127,583 | $ 3,735,009 |

## NOTE 8 PENSIONS

The following table represents the aggregate pension amounts for all plans for the year 2019:

| Aggregate Pension Amounts – All Plans | |
|---|---|
| Pension liabilities | $3,701,815 |
| Pension assets | $ - |
| Deferred outflows of resources | $1,084,627 |
| Deferred inflows of resources | $2,008,398 |
| Pension expense/expenditures | $452,055 |

**State Sponsored Pension Plans**
Substantially all of the District's full-time and qualifying part-time employees participate in one of the following statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing, multiple-employer public employee defined benefit and defined contribution retirement plans. The state Legislature establishes, and amends, laws pertaining to the creation and administration of all public retirement systems.

The Department of Retirement Systems (DRS), a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan. The DRS CAFR may be obtained by writing to:

Department of Retirement Systems Communications
Unit
P.O. Box 48380
Olympia, WA 98540-8380

Or the DRS CAFR may be downloaded from the DRS website at www.drs.wa.gov.

**Public Employees' Retirement System (PERS)**
PERS members include elected officials; state employees; employees of the Supreme, Appeals and Superior Courts; employees of the legislature; employees of district and municipal courts; employees of local governments; and higher education employees not participating in higher education retirement programs. PERS is comprised of three separate pension plans for membership purposes. PERS plans 1 and 2 are defined benefit plans, and PERS plan 3 is a defined benefit plan with a defined contribution component.

**PERS Plan 1** provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service.

The AFC is the average of the member's 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service. Members retiring from active status prior to the age of 65 may receive actuarially reduced benefits. Retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and non-duty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Department of Labor and Industries. PERS 1 members were vested after the completion of five years of eligible service. The plan was closed to new entrants on September 30, 1977.

*Contributions* - The **PERS Plan 1** member contribution rate is established by State statute at 6 percent. The employer contribution rate is developed by the Office of the State Actuary and includes an administrative expense component that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates. The PERS Plan 1 required contribution rates (expressed as a percentage of covered payroll) for 2019 were as follows:

| **PERS Plan 1** | | |
|---|---|---|
| **Actual Contribution Rates** | **Employer** | **Employee*** |
| January – June 2019 | | |
| PERS Plan 1 | 7.52% | 6.00% |
| PERS Plan 1 UAAL | 5.13% | |
| Administrative Fee | 0.18% | |
| **Total** | **12.83%** | **6.00%** |
| July – December 2019 | | |
| PERS Plan 1 | 7.52% | 6.00% |
| PERS Plan 1 UAAL | 5.13% | |
| Administrative Fee | 0.18% | |
| **Total** | **12.83%** | **6.00%** |

**PERS Plan 2/3** provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service for Plan 2 and 1 percent of AFC for Plan 3. The AFC is the average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 members who have at least 20 years of service credit and are 55 years of age or older, are eligible for early retirement with a benefit that is reduced by a factor that varies according to age for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions:

- With a benefit that is reduced by three percent for each year before age 65; or
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules

PERS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service credit. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit. Other PERS Plan 2/3 benefits include duty and non-duty disability payments, a cost-of-living allowance (based on the CPI), capped at three percent annually and a one-time duty related death benefit, if found eligible by the Department of Labor and Industries. PERS 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service if 12 months of that service are earned after age 44.

**PERS Plan 3** defined contribution benefits are totally dependent on employee contributions and investment earnings on those contributions. PERS Plan 3 members choose their contribution rate upon joining membership and have a chance to change rates upon changing employers. As established by statute, Plan 3 required defined contribution rates are set at a minimum of 5 percent and escalate to 15 percent with a choice of six options. Employers do not contribute to the defined contribution benefits. PERS Plan 3 members are immediately vested in the defined contribution portion of their plan.

| PERS Plan 2/3 | | |
|---|---|---|
| **Actual Contribution Rates** | **Employer 2/3** | **Employee Plan 2*** |
| January – June 2019 | | |
| PERS Plan 2/3 | 7.52% | 7.41% |
| PERS Plan 1 UAAL | 5.13% | |
| Administrative Fee | 0.18% | |
| Employee PERS Plan 3 | | Varies |
| **Total** | **12.83%** | **7.41%** |
| July – December 2019 | | |
| PERS Plan 2/3 | 7.52% | 7.90% |
| PERS Plan 1 UAAL | 5.13% | |
| Administrative Fee | 0.18% | |
| Employee PERS Plan 3 | | Varies |
| **Total** | **12.83%** | **7.90%** |

*Contributions* - The **PERS Plan 2/3** employer and employee contribution rates are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. The Plan 2/3 employer rates include a component to address the PERS Plan 1 UAAL and an administrative expense that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 2 employer and employee contribution rates and Plan 3 contribution rates. The PERS Plan 2/3 required contribution rates (expressed as a percentage of covered payroll) for 2019 were as follows:

The District's actual PERS plan contributions were $525,839 to PERS Plan 1 and $772,773 to PERS Plan 2/3 for the year ended December 31, 2019.

**Actuarial Assumptions**

The total pension liability (TPL) for each of the DRS plans was determined using the most recent actuarial valuation completed in 2019 with a valuation date of June 30, 2018. The actuarial assumptions used in the valuation were based on the results of the Office of the State Actuary's (OSA) *2007-2012 Experience Study* and the *2017 Economic Experience Study*.

Additional assumptions for subsequent events and law changes are current as of the 2018 actuarial valuation report. The TPL was calculated as of the valuation date and rolled forward to the measurement date of June 30, 2019. Plan liabilities were rolled forward from June 30, 2018, to June 30, 2019, reflecting each plan's normal cost (using the entry-age cost method), assumed interest and actual benefit payments.

- **Inflation:** 2.75% total economic inflation; 3.50% salary inflation
- **Salary increases**: In addition to the base 3.50% salary inflation assumption, salaries are also expected to grow by promotions and longevity
- **Investment rate of return:** 7.4%

Mortality rates were based on the RP-2000 report's Combined Healthy Table and Combined Disabled Table, published by the Society of Actuaries. The OSA applied offsets to the base table and recognized future improvements in mortality by projecting the mortality rates using 100 percent Scale BB. Mortality rates are applied on a generational basis; meaning, each member is assumed to receive additional mortality improvements in each future year throughout his or her lifetime.

There were changes in methods and assumptions since the last valuation.
- Updated modeling to reflect providing benefit payments to the date of initial retirement eligibility for terminated vested members who delay application for retirement benefits.
- Updated Cost-of-Living Adjustment (COLA) programming to reflect legislation signed during the 2018 Legislative Session (C151 L18). This law provides PERS and TRS Plan 1 annuitants who are not receiving a basic minimum, alternative minimum, or temporary disability benefit with a one-time permanent 1.5 percent increase to their monthly retirement, not to exceed $62.50 per month.

**Discount Rate**
The discount rate used to measure the total pension liability for all DRS plans was 7.4 percent.

To determine that rate, an asset sufficiency test included an assumed 7.5 percent long-term discount rate to determine funding liabilities for calculating future contribution rate requirements. Consistent with the long-term expected rate of return, a 7.4 percent future investment rate of return on invested assets was assumed for the test. Contributions from plan members and employers are assumed to continue being made at contractually required rates (including PERS 2/3). Based on these assumptions, the pension plans' fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.4 percent was used to determine the total liability.

**Long-Term Expected Rate of Return**
The long-term expected rate of return on the DRS pension plan investments of 7.4 percent was determined using a building-block-method. In selecting this assumption, the Office of the State Actuary (OSA) reviewed the historical experience data, considered the historical conditions that produced past annual investment returns, and considered capital market assumptions and simulated expected investment returns

provided by the Washington State Investment Board (WSIB). The WSIB uses the capital market assumptions and their target asset allocation to simulate future investment returns at various future times.

**Estimated Rates of Return by Asset Class**

Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2019, are summarized in the table below. The inflation component used to create the table is 2.2 percent and represents the WSIB's most recent long-term estimate of broad economic inflation.

| Asset Class | Target Allocation | % Long-Term Expected Real Rate of Return Arithmetic |
|---|---|---|
| Fixed Income | 20% | 2.20% |
| Tangible Assets | 7% | 5.10% |
| Real Estate | 18% | 5.80% |
| Global Equity | 32% | 6.30% |
| Private Equity | 23% | 9.30% |
| | **100%** | |

**Sensitivity of the Net Pension Liability/(Asset)**

The table below presents the District's proportionate share of the net pension liability calculated using the discount rate of 7.4 percent, as well as what the District's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage point lower (6.4 percent) or 1-percentage point higher (8.4 percent) than the current rate.

| | 1% Decrease (6.4%) | Current Disc Rate (7.4%) | 1% Increase (8.4%) |
|---|---|---|---|
| PERS 1 | $3,546,359 | $2,831,835 | $2,211,891 |
| PERS 2/3 | $6,672,406 | $869,981 | $(3,891,293) |

**Pension Plan Fiduciary Net Position**

Detailed information about the State's pension plans' fiduciary net position is available in the separately issued DRS financial report.

**Pension Liabilities (Assets), Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions**

At June 30, 2019, the District reported a total pension liability of $3,701,815 for its proportionate share of the net pension liabilities as follows:

| | Liability |
|---|---|

| | |
|---|---|
| PERS 1 | $2,831,835 |
| PERS 2/3 | $869,980 |

The District's proportionate share of the collective net pension liabilities was as follows:

| | Proportionate Share 6/30/18 | Proportionate Share 6/30/19 | Change in Proportion |
|---|---|---|---|
| PERS 1 | .071163% | .073643% | .002480% |
| PERS 2/3 | .085640% | .089565% | .003925% |

Employer contribution transmittals received and processed by the DRS for its fiscal year ended June 30 are used as the basis for determining each employer's proportionate share of the collective pension amounts reported by the DRS in the Schedules of Employer and Nonemployer Allocations for all plans in which the District participates.

The collective net pension liability (asset) was measured as of June 30, 2019, and the actuarial valuation date on which the total pension liability (asset) is based was as of June 30, 2018, with update procedures used to roll forward the total pension liability to the measurement date.

**Pension Expense**

For the year ended December 31, 2019, the District recognized pension expense as follows:

| | Pension Expense |
|---|---|
| PERS 1 | $245,507 |
| PERS 2/3 | 206,548 |
| TOTAL | $452,055 |

**Deferred Outflows of Resources and Deferred Inflows of Resources**

At December 31, 2019, the District reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

| PERS 1 | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|---|---|
| Differences between expected and actual experience | - | - |
| Net difference between projected and actual investment earnings on pension plan investments | - | $189,190 |
| Changes of assumptions | - | - |
| Changes in proportion and differences between contributions and proportionate share of contributions | - | - |
| Contributions subsequent to the measurement date | $257,873 | - |
| TOTAL | $257,873 | $189,190 |

| PERS 2/3 | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|---|---|
| Differences between expected and actual experience | $249,252 | $187,041 |
| Net difference between projected and actual investment earnings on pension plan investments | - | 1,266,338 |
| Changes of assumptions | 22,277 | 365,015 |
| Changes in proportion and differences between contributions and proportionate share of contributions | 153,147 | 814 |
| Contributions subsequent to the measurement date | 402,078 | - |
| TOTAL | $826,754 | $1,819,207 |

| All Plans | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|---|---|
| Differences between expected and actual experience | $249,252 | $187,041 |
| Net difference between projected and actual investment earnings on pension plan investments | - | 1,455,528 |
| Changes of assumptions | 22,277 | 365,015 |

| All Plans | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|---|---|
| Changes in proportion and differences between contributions and proportionate share of contributions | 153,147 | 814 |
| Contributions subsequent to the measurement date | 659,951 | - |
| TOTAL | $1,084,627 | $2,008,398 |

Deferred outflows of resources related to pensions resulting from the District's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2019. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

| Year ended December 31: | PERS 1 |
|---|---|
| 2020 | $(41,765) |
| 2021 | (98,929) |
| 2022 | (35,304) |
| 2023 | (13,193) |
| Thereafter | - |

| Year ended December 31: | PERS 2/3 |
|---|---|
| 2020 | $(362,592) |
| 2021 | (623,314) |
| 2022 | (261,352) |
| 2023 | (127,647) |
| 2024 | (46,784) |
| Thereafter | 27,157 |

## NOTE 9 OTHER POSTEMPLOYMENT BENEFITS (OPEB) PLAN

The following table represents the aggregate OPEB amounts for all plans subject to the requirements of GASB State 75 for the year 2019:

| ***Aggregate OPEB Amounts – All Plans*** | |
|---|---|
| *OPEB liabilities* | *$5,381,587* |
| *OPEB assets* | *$ -* |
| *Deferred outflows of resources* | *$354,283* |
| *Deferred inflows of resources* | *$256,126* |
| *OPEB expenses/expenditures* | *$406,459* |

<u>OPEB Plan Description</u>
The District provides to its retirees employer subsidies for postemployment medical and dental insurance benefits (OPEB) provided through the Public Employees Benefits Board (PEBB). It is a single-employer defined benefit plan and administered by the Washington State Health Care Authority (HCA) per RCW 41.05.065.

The PEBB plan is not a trust and there are no assets available. The plan is financed on a pay-as-you-go basis, meaning that PEBB employers pay these costs as they occur. The actual medical and dental costs are paid through annual fees and premiums to the PEBB. Legally, the District does not have a contractual obligation or a policy to maintain and provide its employees with continued medical and dental insurance coverage after termination or retirement. The OPEB relationship between PEBB employers and their employees and retirees is not formalized in a contract or plan document. Rather, the benefits are provided in accordance with a substantive plan. A substantive plan is one in which the plan terms are understood by the employers and plan members. This understanding is based on communications between the employers and plan members and the historical pattern of practice with regard to the sharing of benefit costs.

GASB Statement 75, *Accounting and Financial Reporting by Employers for Post-Employment Benefits Other Than Pensions*, requires governments to account for other post-employment benefits (OPEB) on an accrual basis, rather than on a pay as you go basis. The effect is the recognition of an actuarially determined expense on the statement of Activities when a future retiree earns their post-employment benefits, rather than when they use their post-employment benefit. The post-employment benefit liability is recognized on the Statement of Net Position over time.

The PEBB created within the HCA, is authorized to design benefits and determine the terms and conditions of employee and retired employee participation and coverage, including the establishment of eligibility criteria for both active and retired employees. The PEBB program that the District enrolled in covers medical and dental benefits; no other employee benefits are included in the program.  The District employees who end public employment are eligible to continue PEBB insurance coverage as a retiree if they retire under the public employees' retirement system and are vested in that system.

The Office of the State Actuary, a department within the primary government of the State of

Washington, issues a publicly available Other Postemployment Benefits Actuarial Valuation Report. The Other Postemployment Benefits Actuarial Valuation Report may be obtained by writing to: Office of the State Actuary, PO Box 40914, Olympia, Washington 98504 or it may be downloaded from the Office of the State Actuary website at http://osa.leg.wa.gov.

The Public Employees Benefits Board (PEBB) plan offers a subsidized retirement coverage to its plan participants and the District can terminate medical insurance with no future obligation or liability to PEBB or its retirees.

The subsidies provided by PEBB to the District include the following:

• Explicit Medical Subsidy for Post 65 retirees and spouses
• Implicit Medical and Dental Subsidy

The explicit subsidies are monthly amounts per retiree and spouse. As of the valuation date, the explicit subsidy for post-65 retirees and spouses is the lesser of $150 or 50% of the monthly premium.
The implicit medical subsidy is the difference between the total cost of medical benefits and the premiums. For pre-65 retirees and spouses, the retirees pay the full premium amount, but that amount is based on a pool that includes active employees. Active employees will tend to be younger and healthier than retirees on average, and therefore can be expected to have lower average health costs. For post-65 retirees and spouses, the retiree does not pay the full premium due to the subsidy discussed above.

***Employees covered by benefit terms:*** At December 31, 2019, the following employees were covered by the benefit terms:

| | |
|---|---|
| Inactive employees or beneficiaries currently receiving benefits | 25 |
| Inactive employees entitled to but not yet receiving benefits | – |
| Active employees | 106 |
| Total | 131 |

It is not possible to estimate the number of employees entitled to, but not yet receiving benefits because neither the District nor HCA has an accurate way to measure this.

The plan is funded on a pay as you go basis and there are no assets accumulated in a qualifying trust.

Assumptions and Other Inputs

The total OPEB liability in the June 30, 2019 actuarial valuation was determined using the following actuarial assumptions and other inputs, applied to all periods included in the measurement, unless otherwise specified:

- Discount rate is based on Bond Buyer General Obligation 20-Bond Municipal Index. This resulted in a 3.87% discount rate for the beginning total OPEB liability, measured as of June 30, 2018, and 3.50% for the ending total OPEB liability, measured as of June 30, 2019.

- Projected salary changes at 3.50%. In addition to the base 3.50% salary inflation assumption, salaries are also expected to grow by merits and longevity.

- Health cost trend rate initially at 6.80% for pre-65 claims and contributions and decreases to 6.30%, 6.10%, 5.30% for the years ending June 30, 2020, 2021, and 2022, respectively. The rate for the each year between June 30, 2023 through 2025 is 5.50%, 6.30% for each year of next 10 years ending June 30, 2035, 6.00% for each year of next 10 years ending June 30, 2045, 5.60% for each year of next 10 years ending June 30, 2055, 5.40% for each year of next 10 years ending June 30, 2065, 4.60% for each year of next 10 years ending June 30, 2075, and 4.50% per year thereafter.

- Health cost trend rate initially at 3.60% for post-65 claims and increases to 7.60% for each year of June 30, 2020 and 2021. The rate decreases to 5.20% for the year ending June 30, 2022. The rate for the each year between June 30, 2023 through 2025 is 5.30%, 5.40% for each year of next 10 years ending June 30, 2035, 5.60% for each year of next 10 years ending June 30, 2045, 5.80% for each year of next 10 years ending June 30, 2055, 5.50% for each year of next 10 years ending June 30, 2065, 4.70% for each year of next 10 years ending June 30, 2075, 4.60% for each year of next 10 years ending June 30, 2085, and 4.70% per year thereafter.

- Health cost trend rate initially at 1.10% for post-65 contributions and increases to 9.30% and 12.40% for the year ending June 30, 2020 and 2021 respectively. The rate decreases to 6.80% for the year ending June 30, 2022. The rate for the each year between June 30, 2023 through 2025 is 5.50%, 5.50% for each year of next 10 years ending June 30, 2035, 5.70% for each year of next 10 years ending June 30, 2045, 5.90% for each year of next 10 years ending June 30, 2055, 5.50% for each year of next 10 years ending June 30, 2065, 4.70% for each year of next 10 years ending June 30, 2075, 4.60% for each year of next 10 years ending June 30, 2085, and 4.70% per year thereafter.

- Dental costs trend at 1.10% for the year ending June 30, 2019, 2.00% for the year ending June 30, 2020, 2.00% for the year ending June 30, 2021, 2.50% or the year ending June 30, 2022, 3.50% for the year ending June 30, 2023, and 4.0% per year thereafter.

- Mortality rates were based on the RP-2000 report's Combined Healthy Table and Combined Disabled Table, published by the Society of Actuaries, adjusted by -1 year for both males and females, with generational mortality adjustments using projection scale BB.

- Inflation rate at 2.75% total economic inflation.

- Post-retirement participation percentage of 65% for medical benefits and 50% for dental benefits.

- Percentage with spouse coverage of 45%.

<u>Sensitivity of OPEB Liability</u>

The following presents the total OPEB liability of the District calculated using the current healthcare cost trend rates as well as what the OPEB liability would be if it were calculated using trend rates that are 1-percentage point lower or 1-percentage point higher than the current trend rates.

| | 1% Decrease | Current Healthcare Cost Trend Rate | 1% Increase |
|---|---|---|---|
| Total OPEB Liability | $4,380,281 | $5,381,587 | $6,707,435 |

The following presents the total OPEB liability of the District calculated using the discount rate of 3.5 percent, as well as what the OPEB liability would be if it were calculated using a discount rate that is 1- percentage point lower (2.5%) or 1-percentage point higher (4.5%) that the current rate.

| | 1% Decrease (2.5%) | Current Discount Rate (3.5% | 1% Increase (4.5%) |
|---|---|---|---|
| Total OPEB Liability | $6,503,243 | $5,381,587 | $4,504,954 |

Changes in the Total OPEB Liability

| ***Plan Name*** | |
|---|---|
| ***Total OPEB Liability Beginning Balance (Restated)*** | $4,721,642 |
| *Service cost* | 205,875 |
| *Interest* | 189,079 |
| *Changes of benefit terms* | - |
| **Differences between expected and actual experience* | - |
| **Changes of assumptions* | 349,309 |
| *Benefit payments* | (84,318) |
| *Other changes* | - |
| ***Total OPEB Liability Ending Balance*** | $5,381,587 |

The net OPEB liability of $5,381,587 was determined by the actuarial valuation as of July 1, 2019, with the results rolled forward to December 31, 2019. The actuarial valuation and actuarial measurement dates were July 1, 2018 and June 30, 2019, respectively. Discount rates decreased from 3.87% to 3.50% based on the Bond Buyer General Obligation 20-bond municipal bond index for

bonds that mature in 20 years. Service costs, which are the amounts of benefits earned by active employees over the current year, and interest costs on the OPEB liability (or future value subsidy) increased the OPEB liability were $205,875 and $189,079 respectively. The net effect of assumptions changes increased the OPEB liability by $349,309. Benefit payments of $189,079 were subsidies expected to be paid throughout the year.

The District recognized OPEB expense of $406,459 in 2019.

At December 31, 2019, the District reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

| | *Deferred Outflows of Resources* | *Deferred Inflows of Resources* |
|---|---|---|
| *Differences between expected and actual experience* | *$ -* | *$ -* |
| *Changes of assumptions* | *306,184* | *(192,886)* |
| *Payments subsequent to the measurement date* | *48,099* | *-* |
| *TOTAL** | *$ 354,283* | *$ (192,886)* |

Deferred outflows of resources of $48,099 resulting from payments subsequent to the measurement date will be recognized as a reduction of the total OPEB liability in the year ended December 31, 2019. Other amounts reported as deferred outflows and deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows:

| *Year ended December 31:* | |
|---|---|
| *2020* | *$11,505* |
| *2021* | *11,505* |
| *2022* | *11,505* |
| *2023* | *11,505* |
| *2024* | *11,505* |
| *Thereafter* | *55,773* |

## NOTE 10 RISK MANAGEMENT

The District is a member of Cities Insurance Association of Washington (CIAW). Chapter 48.62 RCW authorizes the governing body of any one or more governmental entities to form together into or join a program or organization for the joint purchasing of insurance, and/or joint self-insuring, and/or joint hiring or contracting for risk management services to the same extent that they may individually purchase insurance, self-insure, or hire or contract for risk management services. An agreement to form a pooling arrangement was made pursuant to the provisions of Chapter 39.34 RCW, the Interlocal Cooperation Act. The program was formed on September 1, 1988, when 32 cities in the state of Washington joined together by signing an Interlocal Governmental Agreement to pool their self-insured losses and jointly purchase insurance and administrative services. As of December 1, 2019, there are over 200 members in the program.

The program provides the following forms of joint self-insurance and reinsurance coverage for its members: Property, including Automobile Comprehensive and Collision; Equipment Breakdown; and Crime Protection; and Liability, including General, Automobile, and Wrongful Acts, which are included to fit members' various needs. The District carries commercial general liability, automobile and fidelity coverage with CIAW.

The program acquires liability insurance through their Administrator, Brown & Brown Insurance of Washington, which is subject to a per-occurrence self-insured retention of $100,000 except for Wrongful Acts and Law Enforcement Liability which have a self-insured retention of $25,000. The standard member deductible is $1,000 (deductible may vary per member), while the program is responsible for the $100,000 self-insured retention. The Crime Coverage deductible is $1,000 with a self-insured retention of $25,000. Insurance carriers cover insured losses in excess of the sum of the deductible and the self-insured retention to the limits of each policy. Since the program is a cooperative program, there is a joint liability among the participating members towards the sharing of the $100,000 of the self-insured retention. The program also purchases a Stop Loss Policy as another layer of protection to its membership.

Members contract to remain in the program for a minimum of one year, and must give notice before December 1, to terminate participation the following December 1. The Interlocal Agreement is renewed automatically each year. In the event of termination, a member is still responsible for contributions to the program for any unresolved, unreported, and in-process claims for the period they were a signatory to the Interlocal Agreement.

A board of ten members is selected by the membership from three geographic areas of the state on a staggered term basis and is responsible for conducting the business affairs of the program.
The program has no employees. Claims are filed by the members/brokers with Brown & Brown Insurance of Washington, who has been contracted to perform program administration, claims adjustment, administration and loss prevention for the program.

In the past three years (2019, 2018, and 2017), there have been no claim settlements, per occurrence or in aggregate, that have exceeded the coverage provided by excess/reinsurance contracts.

**Unemployment Compensation Self-insurance**
The District is self-insured for unemployment compensation exposure. Claims against the District are administered by the Washington State Department of Employment Security and are subsequently reimbursed by the District. Actual costs are paid by the District as incurred. No claims or reimbursements were paid in 2019.

**Property Risks**
The District carries commercial insurance for all other risks of loss, including property, earth

movement, flood, electronic data processing equipment and boiler & machinery insurance. Settled claims resulting from these risks have not exceeded commercial insurance coverage in 2018 or 2019. In 2016 the District incurred a casualty loss of $1,232,639 in excess of insurance coverage.

## NOTE 11 SECOND SUPPLY PROJECT PARTNERSHIP AGREEMENT

In 2002, the District entered into an agreement with the City of Tacoma, Department of Public Utilities, Water Division, the City of Kent, and the Covington Water District to permit, design, finance, construct, operate, and maintain a second supply project and to receive deliveries of project water. The project has been designed to permit all participants to receive at their point(s) of delivery their respective participant shares of second diversion water simultaneously. The participants understand and acknowledge that the capability of project facilities at any point in time is dependent upon the use being made of the project by the participants, and external factors as well. Tacoma shall own the project, and all facilities related thereto, up to points of diversion. Each participant has a contractual obligation to pay its participant share of project costs, initially as a capital contribution in exchange for, and to qualify each participant to enjoy, the rights and interest as described in section 5 of the agreement, and upon operation as a share of operating and maintenance costs of a project providing water that is furnished by each of the participants to its customers.

It is anticipated that the agreement will have a life of no less than 100 years. There shall be a project committee composed of one representative of each participant. The representatives of the participants shall have the following votes at the project committee meetings: Tacoma (15) votes, Covington Water District (7) votes, Kent (7) votes, Lakehaven Water & Sewer District (7) votes.

The District has spent $73,760,007 towards this project as of December 31, 2019. Further

information can be obtained from the District office.

## NOTE 12 FRANCHISE AGREEMENT WITH THE CITY OF FEDERAL WAY

In March of 2018 the District entered into a franchise agreement with the City of Federal Way (the City) in order to specify the rights and duties of the District to install, operate and maintain a water and sewer system located in certain rights of way located in the City.

In July of 2018, the District began collecting and distributing to the City a monthly franchise fee equal to 3.6 percent of revenue generated within the City (as defined by the agreement). The franchise fee increases to 3.8 percent in 2020-2023, and to 4.0 percent for 2024-2026.

On March 27, 2019, the City of Federal Way imposed a 7.75% utility tax on all District water and sewer revenue within the city limits. The District is contesting the legality of this tax, but it is unlikely that a final decision will be issued by the court before 2020 at the earliest. The District is paying the amount of the tax in excess of the 3.6% franchise fee into a separate fund maintained by the King County Treasurer until the legality of the tax has been resolved, at which time the funds will either by paid to the City of Federal Way or refunded to the District customers.

During 2019, the District reported utility tax to the City of Federal Way of $2,147,552 based on the 7.75% tax rate and the amount paid to the City of Federal Way was $910,866. The excess amount was reported as a payable and set aside in the King County Investment Pool as a restricted cash and cash equivalent.

In July of 2018, the City began paying the District for the cost of maintaining the fire hydrants within City boundaries and agrees to bear the cost of the Puget Sound Energy streetlights located in the right of way within City boundaries previously paid for by the District. Amounts received from the City under the agreement totaled $645,789 in 2019.

The agreement runs through 2026 and as a result of the franchise agreement, the City will not attempt to assume the jurisdiction of the District under the provisions of RCW Chapter 35.13A.

Further information can be obtained from the District office.

**NOTE 13 CONSTRUCTION AND OTHER SIGNFICIANT COMMITMENTS**
As of December 31, 2019, the District is obligated under various construction contracts totaling $8,966,557 of which $5,143,607 has been expended.

**NOTE 14 ASSET RETIREMENT OBLIGATION**
The District implemented GASB 83, Certain Asset Retirement Obligations, in 2019 and recognized an asset retirement obligation (the ARO) of $2,236,250 in consideration of the State regulations regarding well decommissioning. While recognizing the ARO liability for the initial year, the entire amount is also reported as a deferred outflow of resources to offset the recognition of the ARO liability.

Wells have explicit decommissioning requirements that are triggered when they are permanently taken out of service. These requirements are found in RCW 18.104 (the Washington Well Construction Act) and WAC 173-160-381. For resource protection wells or geotechnical soil borings, the decommissioning requirements are found in WAC 173-160-460.

The ARO liability was estimated based on the estimated cost of decommissioning. The decommissioning cost is assumed at $100 per foot of depth, including labor and equipment cost of $75 per foot and cost of grout or other plugging material of $25 per foot. The District currently has a total of 56 wells, ranging from 34 feet to 1,097 feet in depth.

The functional life of a well hole and casing is estimated to be 120 years. The remaining useful life of each well is determined based on the year of the well placed in service.

**NOTE 15 COVID-19 PANDEMIC**
In February 2020, the Governor of the state of Washington declared a state of emergency in response to the spread of the deadly new virus known as COVID-19. In the months following the declaration, precautionary measures to slow the spread of the virus were ordered. These measures included closing schools, cancelling public events, limiting public and private gatherings, and restricting business operations, travel and non-essential activities.

Although the length of time these measures will continue is unknown at the time of this writing, the overall financial impact on the District is deemed to be immaterial.

Lakehaven Water & Sewer District
Schedules of Proportionate Share of the Net Pension Liability
As of June 30 (Measurement Date)
Last 10 Fiscal Years*

**PERS 1**

| Year | Employer's Proportion of Net Pension Liability (Asset) | Employer's Proportionate Share of Net Pension Liability (Asset) | Employer's Covered Payroll | Net Pension Liability (Asset) as a Percentage of Covered Payroll | Plan Fiduciary Net Position as a Percentage of the Total Pension Liability |
|---|---|---|---|---|---|
| 2019 | 0.073643% | $ 3,288,921 | $ 10,099,294 | 32.57% | 67.12% |
| 2018 | 0.071163% | 3,178,165 | 9,131,898 | 34.80% | 63.22% |
| 2017 | 0.070027% | 3,322,836 | 8,536,481 | 38.93% | 61.24% |
| 2016 | 0.069877% | 3,752,724 | 8,080,298 | 46.44% | 57.03% |
| 2015 | 0.069594% | 3,640,414 | 7,830,626 | 46.49% | 59.10% |
| 2014 | 0.071239% | 3,588,698 | 7,647,088 | 46.93% | 61.19% |
| 2013 | 0.046870% | 2,738,733 | 7,455,744 | 36.73% | |

**PERS 2/3**

| Year | Employer's Proportion of Net Pension Liability (Asset) | Employer's Proportionate Share of Net Pension Liability (Asset) | Employer's Covered Payroll | Net Pension Liability (Asset) as a Percentage of Covered Payroll | Plan Fiduciary Net Position as a Percentage of the Total Pension Liability |
|---|---|---|---|---|---|
| 2019 | 0.089565% | $ 1,529,243 | $ 9,857,052 | 15.51% | 97.77% |
| 2018 | 0.085640% | 1,462,227 | 8,891,877 | 16.44% | 95.77% |
| 2017 | 0.084629% | 2,940,454 | 8,304,868 | 35.41% | 90.97% |
| 2016 | 0.084187% | 4,238,750 | 7,863,094 | 53.91% | 85.82% |
| 2015 | 0.084600% | 3,022,806 | 7,614,472 | 39.70% | 89.20% |
| 2014 | 0.086424% | 1,746,942 | 7,445,501 | 23.46% | 93.29% |
| 2013 | 0.060311% | 2,575,289 | 7,253,724 | 35.50% | |

* Information is presented only for those years for which information is available.

Lakehaven Water & Sewer District
Schedule of Employer Contributions
As of December 31 (Employer Reporting Date)
Last 10 Fiscal Years*

**PERS 1**

| Year | Statutorily Required Contribution | Contributions in Relation to the Statutorily Required Contribution | Contribution Deficiency (Excess) | Employer's Covered Payroll | Contributions as a Percent of Covered Payroll |
|---|---|---|---|---|---|
| 2019 | $ 525,839 | $ (525,839) | $ - | $ 10,099,294 | 5.21% |
| 2018 | 506,907 | (506,907) | - | 9,652,251 | 5.25% |
| 2017 | 442,993 | (442,993) | - | 8,709,281 | 5.09% |
| 2016 | 413,916 | (413,916) | - | 8,388,336 | 4.93% |
| 2015 | 353,367 | (353,367) | - | 7,837,215 | 4.51% |
| 2014 | 318,625 | (318,625) | - | 7,455,744 | 4.27% |
| 2013 | 232,460 | (232,460) | - | 7,088,370 | 3.28% |

**PERS 2/3**

| Year | Statutorily Required Contribution | Contributions in Relation to the Statutorily Required Contribution | Contribution Deficiency (Excess) | Employer's Covered Payroll | Contributions as a Percent of Covered Payroll |
|---|---|---|---|---|---|
| 2019 | $ 772,773 | $ (772,773) | $ - | $ 9,857,052 | 7.84% |
| 2018 | 705,267 | (705,267) | - | 9,408,598 | 7.50% |
| 2017 | 582,100 | (582,100) | - | 8,474,842 | 6.87% |
| 2016 | 508,798 | (508,798) | - | 8,166,935 | 6.23% |
| 2015 | 425,476 | (425,476) | - | 7,621,061 | 5.58% |
| 2014 | 371,781 | (371,781) | - | 7,253,724 | 5.13% |
| 2013 | 323,470 | (323,470) | - | 6,904,440 | 4.68% |

*Information is presented only for those years for which information is available.

Lakehaven Water & Sewer District
Schedules of Changes in
Total OPEB Liability and Related Ratios
As of June 30 (Measurement Date)
Last 10 Fiscal Years*

| | 2019 | 2018 |
|---|---|---|
| **Total OPEB liability - Beginning** | $ 4,721,642 | $ 4,662,957 |
| Service Cost | 205,875 | 217,524 |
| Interest | 189,079 | 173,371 |
| Changes of benefit terms | | - |
| Differences between expected and actual experience | 349,309 | (256,126) |
| Changes of assumptions | | - |
| Benefit Payments | (84,318) | (76,084) |
| **Total OPEB liability - Ending** | 5,381,587 | 4,721,642 |
| Covered-Employee Payroll | $ 9,993,945 | $ 9,131,898 |
| Total OPEB liability as a % of covered-employee payroll | 53.85% | 51.70% |

Notes to Schedule:
No assets are accumulated in a trust that meets the criteria in paragraph 4 of GASB 75.

* Until a full 10-year trend is compiled, only information for those years available is presented.

## ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

We work with our audit clients and citizens to achieve our vision of government that works for citizens, by helping governments work better, cost less, deliver higher value, and earn greater public trust.

In fulfilling our mission to hold state and local governments accountable for the use of public resources, we also hold ourselves accountable by continually improving our audit quality and operational efficiency and developing highly engaged and committed employees.

As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

Our audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits of state agencies and local governments as well as fraud, state whistleblower and citizen hotline investigations.

The results of our work are widely distributed through a variety of reports, which are available on our website and through our free, electronic subscription service.

We take our role as partners in accountability seriously, and provide training and technical assistance to governments, and have an extensive quality assurance program.

| Contact information for the State Auditor's Office | |
|---|---|
| **Public Records requests** | PublicRecords@sao.wa.gov |
| **Main telephone** | (564) 999-0950 |
| **Toll-free Citizen Hotline** | (866) 902-3900 |
| **Website** | www.sao.wa.gov |