Office of the Washington State Auditor
Pat McCarthy

Financial Statements Audit Report

Northshore Utility District

King County

For the period January 1, 2014 through December 31, 2015

Published January 17, 2017

Report No. 1018428

Office of the Washington State Auditor
Pat McCarthy

January 17, 2017

Board of Commissioners
Northshore Utility District
Kenmore, Washington

Report on Financial Statements

Please find attached our report on the Northshore Utility District's financial statements.

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

Sincerely,

Pat McCarthy

State Auditor

Olympia, WA

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Northshore Utility District
King County
January 1, 2014 through December 31, 2015

Board of Commissioners
Northshore Utility District
Kenmore, 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 Northshore Utility District, King County, Washington, as of and for the years ended December 31, 2015 and 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated January 9, 2017. As discussed in Note 1 to the financial statements, during the year ended December 31, 2015, the District implemented Governmental Accounting Standards Board *Statement No. 68, Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audits 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

January 9, 2017

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

Northshore Utility District
King County
January 1, 2014 through December 31, 2015

Board of Commissioners
Northshore Utility District
Kenmore, Washington

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of basic of the Northshore Utility District, King County, Washington, as of and for the years ended December 31, 2015 and 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed on page 10.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America 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 opinions.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of basic of the Northshore Utility District, as of December 31, 2015 and 2014, and the respective changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Matters of Emphasis

As discussed in Note 1 to the financial statements, in 2015, the District adopted new accounting guidance, Governmental Accounting Standards Board *Statement No. 68, Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 11 through 17 and pension plan information on pages 44 through 45 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 January 9, 2017 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

State Auditor

Olympia, WA

January 9, 2017

FINANCIAL SECTION

Northshore Utility District
King County
January 1, 2014 through December 31, 2015

REQUIRED SUPPLEMENTARY INFORMATION

BASIC FINANCIAL STATEMENTS

REQUIRED SUPPLEMENTARY INFORMATION

MANAGEMENT DISCUSSION AND ANALYSIS

For the Year Ended December 31, 2015

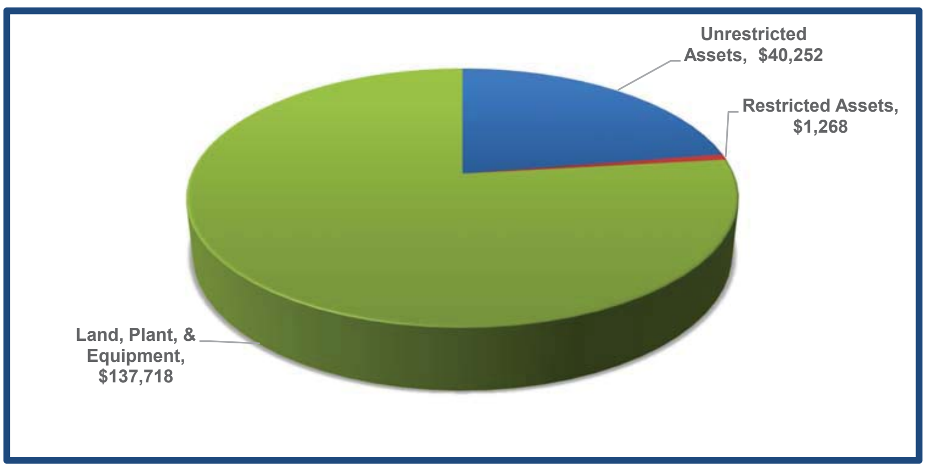
As management of the Northshore Utility District (the District), we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended December 31, 2015. We encourage readers to consider the information presented here in conjunction with the District's financial statements.

The financial position of the District has improved over prior years, which were mildly affected by an economic downturn and slow economic growth.

- The assets of the District exceeded its liabilities, creating a net position at the close of 2015 of $175.5 million representing an increase of $3.7 million over 2014.
- As of the close of 2015, the District cash balance was $40.9 million representing an increase of $4.1 million from December 31, 2014.

The District had total operating revenues of $39.7 million and operating expenses of $36.0 million for the fiscal year ended December 31, 2015.

The vast majority of the District's assets are held in land, plant, and equipment. Other assets are categorized as restricted or unrestricted, as illustrated below, (in $000):



Overview of the Financial Statements

The management discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements are comprised of District-wide financial statements and notes to the financial statements. The District began implementing the Governmental Accounting Standards Board (GASB) Statement No. 34 model of financial reporting in 2003. In 2012, the District implemented GASB Statement No. 63 (Financial Reporting of Deferred Inflows and Outflows of Resources, and Net Position). During 2015, the District implemented GASB Statement No. 68 (Accounting and Financial Reporting for Pensions). These statements establish standards for external financial reporting for all state and local government entities.

DISTRICT FINANCIAL STATEMENTS

The District's financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private sector business.

The ***Statement of Net Position*** presents information on all of the District's assets and deferred outflows vs. liabilities and deferred inflows, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the District is improving or deteriorating. Assets are designated as either "Unrestricted" or "Restricted" based upon their purpose. Restricted assets are those subject to constraints that are externally imposed, such as those imposed by creditors through debt covenants. Funds without a designated purpose are referred to as "Unrestricted." The District had assets restricted for construction and debt service of $1.3 million and $777,185 as of December 31, 2015, and 2014, respectively. In addition, as of the end of 2014, the District considered its Section 125 bank balance as restricted funds, which amounted to $51,980. Please refer to Note 6 of the financial statements.

Total current assets increased significantly during the year, primarily due to a $4.1 million increase in cash. The details of this increase can be seen in the Comparative Statement of Cash Flows on page 18. There was also an increase in prepaid insurance of $188K strictly due to the timing of payments.

Non-current and other assets consist of assessments and contracts receivable. The decrease in these accounts is due to normal payments from customers.

Total net capital assets increased by $2.1 million. Notwithstanding the impact of depreciation and the sale of surplus capital assets ($4.2 million), this net increase was due to:

Capital Improvement Projects (CIP):
In 2015 CIP decreased by almost $5 million. This included $10.3 million being transferred from CIP to water and sewer utility plants (depreciable capital assets), and an additional $5.3 million spent on new and existing CIP.

Depreciable Capital Assets:
These capital assets increased $11.3 million over 2014. The largest increase came in water and sewer utility plants, at $11.1 million. Most of this was transferred over from CIP. The balance of this increase came from the purchase of various vehicles and equipment.

Total current liabilities decreased by $331K during the year. $262K of this decrease was simply a timing difference in payables from restricted assets in the normal course of business. $35K of this decrease was an expected reduction in the current PWTF loans payable.

Total non-current liabilities increased by $2.5 million. This change was due to an increase in the net pension liability of $3.2 million due to the implementation of GASB Statement #68 (please refer to Note 7) and an expected decrease in the non-current portion of PWTF loans in the amount of $370K. The District also recorded deferred inflows related to pensions (per GASB Statement #68) in the amount of $489K.

The ***Statement of Revenues, Expenses, and Changes in Net Position*** presents information showing how the District's position changed during the most recent fiscal year. All changes are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., depreciation as well as earned but unused vacation leave).

Gross utility revenues increased $2.9 million during the year (7.7%). Sewer service revenues increased $1.8 million (8.4%) over 2014. Water service revenues increased $1.1 million (7.6%). For the months March through December of 2015, the District's base rates for sewer service increased 10.9% from the previous year. Water rates during this same time, for a District average 14 CCF consumption with a single family residential unit, increased 8.9%. Street light service revenue actually decreased by $106K. During June of 2015, the city of Kirkland assumed the street light billing for all of the District's customers in their jurisdiction. Non-operating revenues increased only slightly during the year.

Total operating expenses increased $1.2 million during the year. Wholesale costs for water and sewer (Seattle Public Utilities and King County, respectively) increased by $1.1 million.

The ***Statement of Cash Flows*** accounts for the net change in cash and cash equivalents by summarizing cash receipts and cash disbursements resulting from operating activities, capital, and related financing and investment activities. This statement assists the user in determining the source of cash coming into the District, the items for which cash was expended, and the beginning and ending cash balance.

The notes provide additional information that is essential to a full understanding of the data provided in the District's financial statements.

The overall financial condition of the District continues to improve, as indicated by continued increases in net position over 2015, 2014 and 2013. Development in the District continues to show strength. Facilities benefit charges, remained strong at $1.5 million in 2015, with little change from 2014. Investment rates of return moved up slightly from .50% in 2014 to .61% in 2015.

Condensed Statements of Net Position

	2015	2014	2013	2015-2014 Change	Change %
Current, Restricted and Other Assets	$47,679,091	$43,328,192	$39,683,301	$4,350,899	10.0%
Capital Assets (net of depreciation)	137,718,221	135,622,193	132,551,502	2,096,028	1.5%
Total Assets	$185,397,312	$178,950,385	$172,234,803	$6,446,927	3.6%
Total Deferred Outflows	260,655	$0	$0	$260,655	N/A
Current Liabilities	$3,095,149	$3,426,005	$2,482,957	($330,856)	-9.7%
Non-Current Liabilities	6,578,244	3,735,003	4,147,067	2,843,241	76.1%
Total Liabilities	$9,673,393	$7,161,008	$6,630,024	$2,512,385	35.1%
Total Deferred Inflows	$489,219	$0	$0	$489,219	N/A
Net Position					
Net Investment in Capital Assets	$133,975,448	$131,474,743	$127,991,988	$2,500,705	1.9%
Restricted Net Position	1,267,720	829,165	432,327	438,555	52.9%
Unrestricted Net Position	40,252,187	39,485,469	37,180,464	766,718	1.9%
Total Net Position	$175,495,355	$171,789,377	$165,604,779	$3,705,978	2.2%

The net position of the District increased $3.7 million from $171.8 million in 2014 to $175.5 million in 2015. In 2013, the District's net position was $165.6 million.

In 2015, the majority of the District's gross income (92.4%) was derived from water and wastewater service charges received from its ratepayers. The District also derives cash flows from street light service, connection charges (facility benefit charges) and investment earnings.

Additional assets are received from developers in the form of infrastructure donated to the District upon completion of their projects (developer donated plant).

Condensed Statement of Revenues, Expenses and Changes in Net Position

	2015	2014	2013	2015-2014 Change	Change (%)
Operating Revenues:					
Sewer	$23,901,107	$22,056,886	$21,656,724	$1,844,221	8.4%
Water	15,936,172	14,814,964	14,712,078	1,121,208	7.6%
Other	1,523,413	1,615,911	1,622,364	(92,498)	-5.7%
Less discounts	(1,652,309)	(1,536,804)	(1,492,312)	(115,505)	7.5%
Non-Operating Revenues:					
Facility benefit charges	1,505,329	1,531,876	1,625,968	(26,547)	-1.7%
Other	272,720	225,631	369,906	47,089	20.9%
Total Revenues	$41,486,432	$38,708,464	$38,494,728	$2,777,968	7.2%
Operating Expenses	$36,027,113	$34,871,508	$34,103,377	$1,155,605	3.3%
Non-Operating Expenses	21,540	18,170	101,993	3,370	18.5%
Total Expenses	$36,048,653	$34,889,678	$34,205,370	$1,158,975	3.3%
Income Before Plant Donation	$5,437,779	$3,818,786	$4,289,358	$1,618,993	42.4%
Developer donated plant	2,002,411	2,365,810	2,682,400	(363,399)	-15.4%
Change in Net Position	$7,440,190	$6,184,596	$6,971,758	$1,255,594	20.3%
Beginning Net Position	171,789,375	165,604,779	158,633,021	6,184,596	3.7%
Change in Accounting Principle	(3,734,209)	-	-	(3,734,209)	N/A
Ending Net Position	$175,495,356	$171,789,375	$165,604,779	$3,705,981	2.2%

CAPITAL ASSETS AND DEBT ADMINISTRATION

By far the largest portion of the District's total assets (74.3%) is investment in capital assets (e.g. buildings, land, utility plant, equipment, and construction in progress). The District uses these capital assets to provide water and sewer services to residential and commercial ratepayers in the District. The unrestricted net position of the District represents assets that are available for future use to provide utility services.

As of December 31, 2015, the District's investment in capital assets for its activities, shown on the Statement of Net Position as Capital Assets, was $137.7 million net of accumulated depreciation. This is an increase of $2.1 million (1.5%) from December 31, 2014. Capital assets include land, improvements to land and land rights, buildings, building improvements, vehicles, machinery, equipment, utility plant, and all other tangible or intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period. Please refer to Note 3.

LONG-TERM DEBT

The District took advantage of favorable interest rates in 2003 by advance refunding of its outstanding 1995 Revenue Bonds, while at the same time acquiring $4.2 million in new financing. In preparation for this event, the District made a presentation to Standard & Poors, the credit rating agency in May 2003, and obtained an improved credit rating of "AA". An advance refunding transaction occurs when the District retires its outstanding bonds ahead of their scheduled due date with a new series of bonds. In most cases, the advance refunding results in lower debt service costs. Revenue bonds offer a number of distinct advantages. Much like a home mortgage, revenue bonds allow the District to spread out payments over twenty years. Instead of burdening today's ratepayers with the total cost of improvements, all users of the system over the next twenty years will shoulder that cost. In 2008, Standard & Poor's updated the District's bond rating from "AA" to "AAA". Please refer to Note 6 of the financial statements.

The District has historically sought Public Works Trust Fund (PWTF) loans issued by the Washington Public Works Board to finance its water and sewer capital projects. These loans are offered to competing public entities to fund capital projects. In 2010, the District applied for and in 2011 was awarded $3.105 million in state funding to construct a gravity sewer main bypass of the District's lift station 10. This lift station sits on the shores of Lake Washington. It is difficult to access, particularly during inclement weather, and its elimination will greatly reduce the District's environmental exposure should the lift station fail. The current annual interest rate on these loans ranges from 0.25% to 1.0%.

2013 was the last year that the District had revenue bond debt service payments in excess of $1 million. Bond principal payments dropped from $1,360,000 in 2010 to under $300,000 each year beginning in 2011. During 2012 the District decided to call all remaining 2003 revenue bonds on May 1, 2013. The total long-term debt principal outstanding as of December 31, 2015 was $3.4 million consisting of only PWTF loans. See additional information in Note 6.

Comparative Statement of Net Position
As of December 31, 2015 and 2014

	2015	2014
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 39,667,427	$ 36,003,256
Accounts receivable	3,853,668	3,675,929
Estimated unbilled service revenue	1,829,269	1,896,951
Restricted Assets:		
Construction Fund:		
Cash and cash equivalents	1,071,345	656,170
Revenue Bond Fund:		
Cash and cash equivalents	196,375	121,015
Section 125 restricted cash	-	51,980
Inventory	497,807	446,298
Other current assets - prepaid items	188,802	849
TOTAL CURRENT ASSETS	$ 47,304,693	$ 42,852,448
Non-current and Other Assets:		
Assessments receivable	$ 166,055	$ 227,963
Installment contracts receivable	208,343	247,781
TOTAL NON-CURRENT AND OTHER ASSETS	$ 374,398	$ 475,744
Capital Assets:		
Non-depreciable - Land and land rights	$ 2,715,838	$ 2,715,838
Non-depreciable - Construction in progress	7,718,244	12,692,624
Depreciable assets:		
Buildings	14,128,766	14,128,766
Data processing and office equipment	1,935,577	1,863,236
Engineering equipment and vehicles	5,058,492	4,992,451
Sewer utility plant	97,393,353	96,220,710
Water utility plant	96,669,744	86,710,934
Less: Accumulated depreciation	(87,901,793)	(83,702,366)
Total Capital Assets	$ 137,718,221	$ 135,622,193
TOTAL NON-CURRENT AND OTHER ASSETS	$ 138,092,619	$ 136,097,937
TOTAL ASSETS	$ 185,397,312	$ 178,950,385
DEFERRED OUTFLOWS OF RESOURCES		
TOTAL DEFERRED OUTFLOWS OF RESOURCES	$ 260,655	-
TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	$ 185,657,967	$ 178,950,385

Comparative Statement of Net Position
As of December 31, 2015 and 2014

	2015	2014
LIABILITIES		
Current Liabilities:		
Accounts payable	$ 1,921,885	$ 1,956,554
Accrued employee benefits	340,134	336,890
Other liabilities	74,501	75,475
Current portion of State Public		
Trust Fund Loans	377,628	412,447
Payables from Restricted Assets:		
Accounts payable	374,127	636,565
Accrued interest payable	6,874	8,074
TOTAL CURRENT LIABILITIES	$ 3,095,149	$ 3,426,005
Non-current Liabilities:		
State Public Trust Fund Loans	$ 3,365,145	$ 3,735,003
TOTAL NON-CURRENT LIABILITIES	$ 3,365,145	$ 3,735,003
Net Pension Liability	$ 3,213,099	-
TOTAL LIABILITIES	$ 9,673,393	$ 7,161,008
DEFERRED INFLOWS OF RESOURCES		
Deferred Inflows Related to Pensions	$ 489,219	-
TOTAL DEFERRED INFLOWS OF RESOURCES	$ 489,219	-
NET POSITION		
Net investment in capital assets	$ 133,975,448	$ 131,474,743
Restricted net position	1,267,720	829,165
Unrestricted net position	40,252,187	39,485,469
TOTAL NET POSITION	$ 175,495,355	$ 171,789,377
TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION	$ 185,657,967	$ 178,950,385

Comparative Statement of Revenues, Expenses, and Changes in Net Position
For the Years Ended December 31, 2015 and 2014

	2015	2014
OPERATING REVENUES		
Utility Sales - Sewer service	$23,901,107	$22,056,886
Utility Sales - Water service	15,936,172	14,814,964
Utility Sales - Street light service	315,586	422,150
Less: Discounts and adjustments	(1,652,309)	(1,536,804)
Net Utility Sales	$38,500,556	$35,757,196
Other Operating Revenue	1,207,827	1,193,761
Total Operating Income	$39,708,383	$36,950,957
OPERATING EXPENSES		
Sewage treatment charges	$15,013,320	$14,050,599
Water purchased for resale	5,491,142	5,385,796
Cost of street lighting	187,394	344,198
Maintenance	3,430,402	3,431,886
Administration - General	6,531,198	6,434,492
Depreciation	4,313,412	4,248,370
Property, Excise, and B&O Tax	1,060,245	976,167
Total Operating Expenses	$36,027,113	$34,871,508
OPERATING INCOME (LOSS)	$3,681,270	$2,079,449
NON-OPERATING REVENUES (EXPENSES)		
Connection fees	$1,505,329	$1,531,876
Assessment interest income	33,209	41,252
Investment interest income	225,362	175,232
Gain (loss) from disposition of assets	14,149	9,147
Reimbursement agreement costs	0	(1,684)
Bond and loan interest expense	(21,540)	(16,486)
Bond discount, issuance, and registration costs	-	0
Total Non-operating Revenues	$1,756,509	$1,739,337
Income Before Capital Contributions	$5,437,779	$3,818,786
Capital Contributions - Developer donated plant	2,002,411	2,365,810
INCREASE IN NET POSITION	$7,440,190	$6,184,596
TOTAL NET POSITION, January 1, 2015	171,789,375	165,604,779
CHANGE IN ACCOUNTING PRINCIPLE (SEE NOTE 7)	(3,734,209)	-
TOTAL NET POSITION, December 31, 2015	$175,495,356	$171,789,375

Comparative Statement of Cash Flows
For the Years Ended December 31, 2015 and 2014

	2015	2014
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts for utility services	$39,648,162	$36,766,973
Payments to wholesale service providers	(20,991,136)	(18,862,553)
Payments for state and local taxes	(1,060,245)	(976,167)
Payments for payroll and related costs	(4,013,293)	(3,963,207)
Payments for administration and operations	(6,425,563)	(5,724,348)
Net cash provided by operating activities	$7,157,925	$7,240,698
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Purchase of capital assets - equipment	($579,854)	($909,647)
Purchase or Reclassification of system expansion	(3,861,994)	733,816
Purchase of land rights	-	(4,777,420)
Receipts from connection fees	1,505,327	1,530,192
Principal paid on capital debt	(369,858)	(412,064)
Interest paid on capital debt	(21,540)	(16,486)
Net receipts on disposal of capital assets	14,149	9,147
Net cash used in capital and related financing activities	($3,313,770)	($3,842,462)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Interest on investments	$225,362	$175,232
Interest on contracts	20,468	23,821
Interest on assessments	12,741	17,432
Net cash provided by investing activities	$258,571	$216,485
Net (decrease) increase in cash and cash equivalents	$4,102,726	$3,614,721
Cash balance - beginning of year	$36,832,420	$33,217,699
Cash balance - end of year	$40,935,146	$36,832,420
NON-CASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:		
Contribution of capital assets from developers *	$2,002,411	$2,365,810

* Utility plant donated by developers is recorded at the contract price paid by the developer for the facilities accepted by the district.

Comparative Statement of Cash Flows
For the Years Ended December 31, 2015 and 2014

	2015	2014
RECONCILIATION OF OPERATING INCOME TO NET CASH FROM OPERATING ACTIVITIES		
Operating income	$3,681,270	$2,079,449
Adjustments to reconcile operating income to net cash Provided by operating activities:		
Depreciation expense	4,313,412	4,248,370
GASB 68 pension expense not impacting cash	(292,546)	-
Changes in assets and liabilities		
(Increase)/Decrease in accounts receivable	(8,712)	(91,114)
(Increase)/Decrease in inventory	(51,509)	(92,870)
(Increase)/Decrease in other current assets	(187,953)	153,814
Increase/(Decrease) in accounts payable	(333,831)	917,087
Increase/(Decrease) in accrued payroll benefits	3,244	25,009
Increase/(Decrease) in other current liabilities	34,551	953
Net cash provided by operating activities	$7,157,926	$7,240,698

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of Northshore Utility District conform to generally accepted accounting principles (GAAP) as applicable to proprietary funds of governments. The following is a summary of the most significant policies (including identification of those policies which result in material departures from generally accepted accounting principles):

a. Reporting Entity

Northshore Utility District is a municipal corporation governed by an elected five-member board. 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.

b. Basis of Accounting and Presentation

The accounting records of the District are maintained in accordance with methods prescribed by the State Auditor under the authority of Chapter 43.09 of the Revised Code of Washington (RCW).

The District uses the full-accrual basis of accounting where revenues are recognized when earned and expenses are recognized when incurred. An exception to full accrual is that interest on assessments is recorded when received. Capital asset purchases are capitalized and long-term liabilities are accounted for in the appropriate funds.

The District distinguishes between operating revenues and expenses from non-operating. Operating revenues and expenses result from providing services and producing and delivering goods in connection with the District’s principal ongoing operations. The principle operating revenues of the District are charges to ratepayers for water, sewer and streetlight services. Unbilled utility service receivables are recorded at year-end. Operating expenses of the District include the cost of sales and services, administration expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The District implemented the Governmental Accounting Standards Board (GASB) Statement No. 34 in 2003, Statement No. 63 in 2013 and Statement No. 68 in 2015. These statements establish standards for external financial reporting for all state and local government entities.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

c. Cash and Cash Equivalents

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 maintains a deposit relationship with a local commercial bank, which was selected through the contracting of treasury services provided by King County.

d. Capital Assets

See Note 3

e. Restricted Funds

In accordance with bond resolutions (and certain related agreements) separate restricted depository accounts are required to be established. These depository accounts are with King County, the *ex officio* Treasurer for the District. King County refers to these depository accounts as “funds.” The assets held in these “funds” are restricted for specific uses, including construction, debt service, and other special reserve requirements. As of December 31, 2015 restricted “funds” included the following:

Water Construction Fund	$497,162
Sewer Construction Fund	$574,183
Bond Reserve Fund	$9,600
Debt Service Fund	$186,775

f. Receivables

The District records receivables when billing takes place. The District takes advantage of its authority to file liens against properties with delinquent utility charge balances. Such liens are recorded with the King County Recorder’s office and are maintained until the balances are paid in full. Interest is assessed on these accounts until paid. For this reason, there is not an allowance for bad debts.

g. Inventory

Inventory is valued at the average acquisition cost, which approximates the market value. The District performs an annual physical inventory count.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

h. Investments

District funds not required for immediate expenditure are invested via King County, the District's *ex officio* treasurer, in the King County Investment Pool. Investments are stated at cost. For various risks related to the investments, see Deposits and Investments Note No. 2.

i. Compensated Absences

Compensated absences are absences for which employees will be paid, such as vacation and sick leave. The District records unused/accrued leaves for compensated absences as an expense and liability when incurred.

Vacation pay, which may be accumulated up to 240 hours, is payable upon resignation, retirement or death. Sick leave may accumulate indefinitely and is payable upon the following conditions:

- The District will pay 100% of accrued and unused sick leave upon the death of an active employee.
- The District allows all employees to cash out accrued sick leave hours credited during the preceding calendar year less any sick leave used during the same calendar year up to a maximum of 56 hours if the employee has a balance of 224 hours in unused/accrued sick leave before cash-out.
- The District does not pay for unused sick leave upon termination of employment.

j. Unamortized Debt Expenses

Costs relating to the sale of bonds are expensed in the year of bond issuance. The District currently has no bonds outstanding.

k. Construction Financing

The District issued revenue bonds for long-term financing of capital improvements. These bonds were paid off entirely during 2013. See Note No. 6.

In 1985, the District started a series of public works projects to replace aging

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (concluded)

components of the District's sewer and water systems. The District also funds these select capital improvements of the District's sewer and water systems from accumulated reserves. Where applicable, property owners connecting to these facilities in the future will reimburse the District for the cost of these projects plus interest. In some instances, the District has started these projects in response to customers' needs, such as failed septic systems. In other instances, the District has tried to install facilities prior to major street resurfacing projects by King County and other municipalities for cost savings.

Developers also build regular system extensions. Upon the completion of the project, the developer donates those installed facilities to the District as system extensions. Developer donations are recorded at the developer's cost of the improvements.

NOTE 2 – DEPOSITS AND INVESTMENTS

a. Deposits

The District's deposits 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).

b. Investments

In accordance with State law, 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 invested in the King County Investment Pool (Pool). As of December 31, 2015 and 2014, the District had the following investments:

Year	Investment Type	Fair Value	Average Duration
2015	King County Investment Pool	$40,539,601	.93 Years
2014	King County Investment Pool	$36,624,781	1.23 Years

Impaired Investments: As of December 31, 2015, all impaired commercial paper investments have completed enforcement events. The King County Impaired Investment Pool (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 four commercial paper assets that were part of completed enforcement events, where the Impaired Pool accepted the cash-out

NOTE 2 – DEPOSITS AND INVESTMENTS (concluded)

option. The District's share of the impaired investment pool principal is $121,054 and its fair value of these investments is $75,966.

Interest Rate Risk: As of December 31, 2015, the Pool's average duration was .93 years. As a means of limiting its exposure to rising interest rates, securities purchased in the Pool must have a final maturity, or weighted average life of no longer than five years. While the Pool's market value is calculated on a monthly basis, unrealized gains and losses are not distributed to participants. The Pool distributes earnings monthly using an amortized cost methodology.

Credit Risk: As of December 31, 2015, the District's investment in the Pool was not rated by a nationally recognized statistical rating organization (NRSRO). In compliance with state statutes, Pool policies authorize investments in U.S. Treasury securities, U.S. agency securities and mortgage-backed securities, 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 are defined by the District as assets with initial individual cost of more than $5,000 and an estimated useful life in excess of one year.

Major expenses for capital assets, such as major repairs which increase useful lives, are capitalized. Maintenance, repairs, and minor renewals are accounted for as expenses when incurred.

Utility plants in service and other capital assets are recorded at cost. Donations by developers are recorded at the developer's cost.

NOTE 3 – CAPITAL ASSETS (continued)

Capital asset activity for the year ended December 31, 2015 was as follows:

2015	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets not being depreciated:				
Land & land rights	$2,715,838	-	-	$2,715,838
Construction in progress	12,692,624	$5,339,600	($10,313,980)	7,718,244
Total capital assets not being depre	$15,408,462	$5,339,600	($10,313,980)	$10,434,082
Capital assets being depreciated:				
Buildings	$14,128,765	-	-	$14,128,765
Data processing and office equip	1,863,236	$97,860	($25,518)	1,935,578
Engineering equipment and veh	4,992,451	168,959	(102,918)	5,058,492
Sewer utility plants	96,220,710	1,172,643	-	97,393,353
Water utility plants	86,710,935	10,083,007	(124,198)	96,669,744
Total capital assets being deprecia	$203,916,097	$11,522,469	($252,634)	$215,185,932
Less accumulated depreciation for:				
Buildings	($4,555,296)	($404,137)	-	($4,959,433)
Equipment and vehicles	(6,032,147)	(295,024)	$113,985	(6,213,186)
Sewer utility plants	(32,230,674)	(1,939,928)	-	(34,170,602)
Water utility plants	(40,884,248)	(1,674,324)	-	(42,558,572)
Total accumulated depreciation	($83,702,365)	($4,313,413)	$113,985	($87,901,793)
Total Capital Assets, net	$135,622,194	$12,548,656	($10,452,629)	$137,718,221

NOTE 3 – CAPITAL ASSETS (concluded)

Capital asset activity for the year ended December 31, 2014 was as follows:

	2014			
	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets not being depreciated:				
Land & land rights	$2,637,576	$122,459	($44,197)	$2,715,838
Construction in progress	18,826,454	6,253,492	(12,387,322)	12,692,624
Total capital assets not being depre	$21,464,030	$6,375,951	($12,431,519)	$15,408,462
Capital assets being depreciated:				
Buildings	$9,429,607	$4,699,158	-	$14,128,765
Data processing and office equip	1,775,356	87,880	-	1,863,236
Engineering equipment and veh	4,950,252	171,412	($129,213)	4,992,451
Sewer utility plants	89,658,530	8,793,952	(2,231,772)	96,220,710
Water utility plants	84,856,934	4,302,748	(2,448,747)	86,710,935
Total capital assets being deprecia	$190,670,679	$18,055,150	($4,809,732)	$203,916,097
Less accumulated depreciation for:				
Buildings	($4,232,742)	($322,554)	-	($4,555,296)
Equipment and vehicles	(5,750,762)	(410,640)	$129,255	(6,032,147)
Sewer utility plants	(30,381,325)	(1,849,349)	-	(32,230,674)
Water utility plants	(39,218,378)	(1,665,870)	-	(40,884,248)
Total accumulated depreciation	($79,583,207)	($4,248,413)	$129,255	($83,702,365)
Total Capital Assets, net	$132,551,502	$20,182,688	($17,111,996)	$135,622,194

The original cost of operating property retired or otherwise disposed of and the cost of installation, less salvage, is charged to accumulated depreciation. However, in the case of the sale of a significant operating unit or system, the original cost is removed from the utility plant accounts, accumulated depreciation related to the property sold is charged, and the net gain or loss on disposition is credited or charged to income.

Capital assets are depreciated using straight-line method of depreciation over the following estimated useful lives:

Buildings	20 to 30 years
Vehicles	3 to 10 years
Office and Engineering Equipment	3 to 10 years
Utility Plants	10 to 50 years

Preliminary costs incurred for proposed projects are deferred pending construction of the facility. Costs relating to projects ultimately constructed are transferred to utility plant; charges that relate to abandoned projects are expensed.

NOTE 4 – CONSTRUCTION IN PROGRESS

Construction in progress represents expenditures to date on capital projects, which totaled $7.7 million as of December 31, 2015 and $12.7 million as of December 31, 2014. Project details as of December 31, 2015, and 2014, were as follows:

PROJECT	2015	2014
CIP: 2012 CIPP Rehab Various Areas C947	$1,256,614	$137,863
CIP: Northshore Ridge Combined	1,034,381	1,003,147
Other Miscellanouse Projects	995,550	552,161
CIP: 145/100 Wtr Mn Relacement C815	571,679	71,848
CIP: 13-2203 Springbrook Sq. Main	524,278	44,886
CIP: 130/Totem Lake Blvd Main Repl.	466,331	51,487
CIP: 133/88 Sewer Ph II	415,145	312,694
CIP: HQ Builing A&B Roof Repairs and Other Improv	367,029	-
CIP: Inglemoor 24" Water Transmission Main Study	308,864	61,326
CIP: 137/95 Water Main Extension C892	258,726	256,942
CIP: 2014 Comp Plan Updates	207,369	167,209
CIP: PP&S: W-RWA New	181,612	181,612
CIP: Water Main Extension, SR 522, Phase I, C866	179,690	25,712
CIP: 150/106 WM Replacement Project	171,373	-
CIP: 145/81 Water Main Ext. C941	165,771	24,381
CIP: 120/89 Sewer Extension C729	150,863	46,594
CIP: Truck 04	126,105	-
CIP: Lift Station No. 3 Rehabilitation C879	124,575	79,151
CIP: Sewer Main Extension & Replacement, SR 522,	110,953	77,999
CIP: 181/73 Rd Repair & Water Main Rplcmt	101,336	49,051
CIP: Inglemoor Pump House Improvements	-	6,588,221
CIP: Inglemoor Res. 1 Improvements	-	1,207,208
CIP: 155/81 Water Main Repl	-	604,646
CIP: High Profile Facility Rehab	-	420,177
CIP: Inglemoor Rsrv 2 Damage Investigation and Re	-	394,251
CIP: High Profile Facility Rehab	-	149,480
CIP: 12-2105 Side Sewer Replacement	-	106,747
CIP: Sewer-NE 179st /72 Ave NE	-	77,831
Total Construction in Progress	$7,718,244	$12,692,624

NOTE 5 – LEASE COMMITMENTS

The District had no lease commitments for the periods ended December 31, 2015 and 2014.

NOTE 6 – LONG-TERM DEBT

a. Junior Lien Loans

The District had junior lien loans of $3,742,772 as of December 31, 2015 and $4,147,450 as of December 31, 2014 from the Washington Public Works Trust Fund, including current portions of $377,628 for 2015 and $412,447 for 2014.

The District has six loans currently outstanding from the Washington State Public Works Trust Fund.

Year	Term in Years	Interest Rate	Proceeds Received	Loan Balance as of 12/31/15
1995	20	1.0%	$661,138	$0
1996	20	1.0%	1,896,300	100,979
2002	20	0.5%	408,000	151,725
2004	20	0.5%	862,570	411,723
2005	20	0.5%	878,454	462,344
2011	20	0.5%	3,105,000	2,616,001
			$7,811,462	$3,742,772
			Less current maturity	(377,628)
			Long-term portion	$3,365,144

The proceeds from these low interest 20-year loans are used for water main replacement and sewer main extension programs. The principal is repaid in up to twenty equal annual installments.

The District has not obtained short-term debt in the past. It does not anticipate obtaining short-term debt in the future.

NOTE 6 – LONG-TERM DEBT (concluded)

b. Long-Term Debt Service Schedule

	Public Works Trust Fund Loans		Total
Year	Principal	Interest	Cash Flow
2016	377,628	12,658	390,286
2017	276,648	10,673	287,321
2018	276,648	9,697	286,345
2019	276,648	8,721	285,369
2020	276,648	7,746	284,394
2021-2025	1,272,470	24,417	1,296,887
2026-2031	977,952	8,557	986,509
Total	$3,734,642	$82,469	$3,817,111

c. Changes in Long-Term Liabilities

During the years ended December 31, 2015 and 2014 the following changes occurred in long-term liabilities:

	Beginning Balance 1/1/2015	Additions	Reductions	Ending Balance 12/31/2015	Due Within One Year
Public Works Trust Fund Loans	$4,147,450	$0	($412,808)	$3,734,642	$377,628

	Beginning Balance 1/1/2014	Additions	Reductions	Ending Balance 12/31/2014	Due Within One Year
Public Works Trust Fund Loans	$4,559,514	$0	($412,064)	$4,147,450	$412,447

NOTE 7 – PENSION PLAN

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of 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.

The following table represents the aggregate pension amounts for all plans subject to the requirements of the GASB Statement 68, *Accounting and Financial Reporting for Pensions* for the year 2015:

Aggregate Pension Amounts-All Plans	
Pension Liabilities	$3,213,099
Deferred Outflows of Resources	$260,655
Deferred Inflows of Resources	$489,219
Pension Expense	($292,546)

State Sponsored Pension Plans

Substantially all District 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. In addition, the DRS CAFR may be downloaded from the DRS website at www.drs.wa.gov.

Public Employees' Retirement System (PERS) Plans 1, 2, and 3

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.

NOTE 7- PENSION PLAN (continued)

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 2015 were as follows:

2015 PERS Plan 1-Actual Contribution Rates		
Period Covered	**District**	**Employee**
1/1/2015 – 6/30/2015	9.21%	6.00%
7/1/2015 – 12/31/2015	11.18%	6.00%

The District's actual contributions to the plan were $6,332 for the year ended December 31, 2015.

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

NOTE 7- PENSION PLAN (continued)

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.

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 2015 were as follows:

NOTE 7- PENSION PLAN (continued)

2015 PERS Plans 2 & 3-Actual Contribution Rates		
Period Covered	**District-PERS Plan 2**	**Employee-PERS Plan 2**
1/1/2015 – 6/30/2015	9.21%	4.92%
7/1/2015 – 12/31/2015	11.18%	6.12%
Employee PERS Plan 3		Varies

The District's actual contributions to the plans were $374,598 for the year ended December 31, 2015.

Actuarial Assumptions

The total pension liability (TPL) for each of the DRS plans was determined using the most recent actuarial valuation completed in 2015 with a valuation date of June 30, 2014. 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*.

Additional assumptions for subsequent events and law changes are current as of the 2014 actuarial valuation report. The TPL was calculated as of the valuation date and rolled forward to the measurement date of June 30, 2015. Plan liabilities were rolled forward from June 30, 2014, to June 30, 2015, reflecting each plan's normal cost (using the entry-age cost method), assumed interest and actual benefit payments.

- Inflation: 3% total economic inflation; 3.75% salary inflation.
- Salary increases: In addition to the base 3.75% salary inflation assumption, salaries are also expected to grow by promotions and longevity.
- Investment rate of return: 7.5%

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 minor changes in methods and assumptions since the last valuation.

- The OSA updated demographic assumptions, consistent with the changes from the *2007-2012 Experience Study Report*, used when valuing the PERS 1 Basic Minimum COLA.
- The OSA corrected how valuation software calculates a member's entry age under the entry age normal actuarial cost method. Previously, the funding

age was rounded, resulting in an entry age one year higher in some cases. For purposes of calculating the Plan 2/3 Entry Age Normal Cost contribution

NOTE 7- PENSION PLAN (continued)

rates, the OSA now uses the current blend of Plan 2 and Plan 3 salaries rather than using a long-term membership assumption of two-thirds Plan 2 members and one-third Plan 3 members.

- The OSA changed the way it applies salary limits, as described in the *2007-2012 Experience Study Report*.

Discount Rate

The discount rate used to measure the total pension liability for all DRS plans was 7.5 percent. To determine this rate, an asset sufficiency test included an assumed 7.7 percent long-term discount rate to determine funding liabilities for calculating future contribution rate requirements (all plans use 7.7 percent). Consistent with the long-term expected rate of return, a 7.5 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, which rates include a component for the PERS 1 plan liability). 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 7.5 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 7.5 percent was determined using a building-block-method. The Washington State Investment Board (WSIB) used a best estimate of expected future rates of return (expected returns, net of pension plan investment expense, including inflation) to develop each major asset class. Those expected returns make up one component of WSIB's capital market assumptions. The WSIB uses the capital market assumptions and their target asset allocation to simulate future investment returns at various future times. The long-term expected rate of return of 7.5 percent approximately equals the median of the simulated investment returns over a 50-year time horizon.

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, 2015, are summarized

NOTE 7- PENSION PLAN (continued)

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 Arithmetic Real Rate of Return
Fixed Income	20%	1.7%
Tangible Assets	5%	4.4%
Real Estate	15%	5.8%
Global Equity	37%	6.6%
Private Equity	23%	9.6%
Total Allocation	100%	

Sensitivity of the Net Pension Liability

The table below presents the District's proportionate share* of the net pension liability calculated using the discount rate of 7.5 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 one percentage point lower (6.5 percent) or one percentage point higher (8.5 percent) than the current rate.

	6.5 Percent	7.5 Percent	8.5 Percent
PERS 1	$2,114,017	$1,736,355	$1,411,600
PERS 2/3	$4,318,077	$1,476,744	($698,758)

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, 2015, the District reported a total pension liability of $3,213,099 for its proportionate share of the net pension liabilities as follows:

	Liability (Asset)
PERS 1	$1,736,355
PERS 2/3	$1,476,744

NOTE 7- PENSION PLAN (continued)

At June 30, the District's proportionate shares of the collective net pension liabilities were as follows:

	6/30/2014	6/30/2015	Change
PERS 1	.036074%	.033194%	(.00288%)
PERS 2/3	.044762%	.041330%	(.00343%)

Employer contribution transmittals received and processed by the DRS for the 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 Non-employer Allocations.*

The collective net pension liability (asset) was measured as of June 30, 2015, and the actuarial valuation date on which the total pension liability (asset) is based was as of June 30, 2014, with update procedures used to roll forward the total pension liability to the measurement date.

Pension Expense

For the year ended December 31, 2015, the District's recognized pension expense as follows:

	Pension Expense
PERS 1	($213,863)
PERS 2/3	($78,683)
TOTAL	($292,546)

Deferred Outflows of Resources and Deferred Inflows of Resources

At December 31, 2015, the District reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

NOTE 7- PENSION PLAN (continued)

PERS 1	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$0	$0
Net difference between projected and actual investment earnings on pension plan investments	$0	$94,998
Changes of assumptions	$0	$0
Changes in proportion and differences between contributions and proportionate share of contributions	$0	$0
Contributions subsequent to the measurement date	$3,529	$0
TOTAL	$3,529	$94,998

PERS 2	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$156,978	$0
Net difference between projected and actual investment earnings on pension plan investments	$0	$394,221
Changes of assumptions	$2,379	$0
Changes in proportion and differences between contributions and proportionate share of contributions	($110,430)	$0
Contributions subsequent to the measurement date	$208,199	$0
TOTAL	$257,126	$394,221

NOTE 7- PENSION PLAN (concluded)

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, 2016. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year Ending December 31st:	PERS 2/3 (Outflows)
2016	($32,479)
2017	($32,479)
2018	($32,479)
2019	($12,993)

Required Supplementary Information (RSI) - all cost-sharing employers

Under GASB Statement 68, local governments that participate in one or more of the State's cost-sharing, multiple employer pension plans (PERS, SERS, PSERS, TRS, and LEOFF) must present as RSI:

- Schedule of Proportionate Share of the Net Pension Liability
- Schedule of Employer Contributions

These are 10-year schedules. Until a full 10-year trend is compiled, local governments should present information only for those years for which information is available. This RSI is included at the end of this report.

NOTE 8 – PRIOR PERIOD ADJUSTMENTS

The District had no prior period adjustments for 2015 or 2014.

NOTE 9 – JOINT VENTURE

Snohomish River Regional Water Authority (SRRWA)
From the early 1950s to 1992, the Weyerhaeuser Company (Weyco) owned and operated a pulp mill in Everett, Washington, using a water right that allowed up to 36 million gallons per day (mgd) to be drawn from the adjacent Snohomish River for industrial use. Although Weyco closed the mill, it kept the 36 mgd water right.

In 1996, three public water utilities; The City of Everett, the Northshore Utility District (Northshore), and Woodinville Water District (Woodinville) formed the SRRWA, and acquired Weyerhaeuser's water right to help meet water demands

NOTE 9 – JOINT VENTURE (concluded)

projected for the SRRWA service area. The Washington State Department of Ecology approved the water right transfer, with an instantaneous withdrawal rate of 36 mgd and an annual quantity of 23.7 mgd. Following completion of the water right change process and related litigation, the SRRWA has engaged in strategic planning, preliminary engineering, and costing work to assess capital project development and operational path issues. This work is ongoing and projected to achieve initial beneficial use of the SRRWA water right by 2021, unless an extension is requested and granted.

In December 2004, the District signed a fixed quantity long-term supply agreement with Seattle Public Utilities (SPU). The supply quantity in the 60-year agreement is sufficient to supply the District for the duration of the agreement. This gives the District ample time to develop the Weyco source for the future. The District's goal is to have supply from both regional systems (Seattle and Everett) for added reliability. Since the cost for planning is not significant, the partners have agreed to explore all possible ways to develop the new source over the coming years. Transmission systems would need to be built to deliver the water to Northshore and/or Woodinville. Portions of the existing transmission systems might be utilized, including the new Clearview pipeline and reservoir. However, additional new pipelines would still be needed to extend from Clearview to Northshore and Woodinville. Any use of the Clearview pipeline and reservoir would need to be negotiated with the Clearview Water Supply Agency, which owns those facilities.

Until it is determined that this joint venture will ever be used to supply water to the District's customers, all costs incurred are being expensed immediately. There are, however, amounts that have been capitalized over the years. The capitalized amounts on the District's books include land valued at $264,610 and construction in progress of $181,611.

NOTE 10 – RISK MANAGEMENT

The District is a member of the Washington Cities Insurance Authority (WCIA). Utilizing Chapter 48.62 RCW (self-insurance regulation) and Chapter 39.34 RCW (Interlocal Cooperation Act), nine cities originally formed WCIA on January 1, 1981. WCIA was created for the purpose of providing a pooling mechanism for jointly purchasing insurance, jointly self-insuring, and/or jointly contracting for risk management services. WCIA has a total of 162 Members.

New members initially contract for a three-year term, and thereafter automatically renew on an annual basis. A one-year withdrawal notice is required before membership can be terminated. Termination does not relieve a former member from its unresolved loss history incurred during membership.

NOTE 10 – RISK MANAGEMENT (concluded)

Liability coverage is written on an occurrence basis, without deductibles. Coverage includes general, automobile, police, public officials' errors or omissions,

stop gap, and employee benefits liability. Limits are $4 million per occurrence in the self-insured layer, and $16 million per occurrence in the reinsured excess layer. The excess layer is insured by the purchase of reinsurance and insurance and is subject to aggregate limits. Total limits are $20 million per occurrence subject to aggregate sub-limits in the excess layers. The Board of Directors determines the limits and terms of coverage annually.

Insurance coverage for property, automobile physical damage, fidelity, inland marine, and boiler and machinery are purchased on a group basis. Various deductibles apply by type of coverage. Property insurance and auto physical damage are self-funded from the members' deductible to $750,000, for all perils other than flood and earthquake, and insured above that amount by the purchase of insurance.

In-house services include risk management consultation, loss control field services, claims and litigation administration, and loss analyses. WCIA contracts for the claims investigation consultants for personnel issues and land use problems, insurance brokerage, and lobbyist services.

WCIA is fully funded by its members, who make annual assessments on a prospectively rated basis, as determined by an outside, independent actuary. The assessment covers loss, loss adjustment, and administrative expenses. As outlined in the inter-local, WCIA retains the right to additionally assess the membership for any funding shortfall.

An investment committee, using investment brokers, produces additional revenue by investment of WCIA's assets in financial instruments which comply with all State guidelines.

A Board of Directors governs WCIA, which is comprised of one designated representative from each member. The Board elects an executive committee and appoints a treasurer to provide general policy direction for the organization. The WCIA executive director reports to the executive committee and is responsible for conducting the day to day operations of WCIA.

NOTE 11 – PENDING LITIGATION

There was no pending litigation as of December 31, 2015.

REQUIRED SUPPLEMENTAL INFORMATION

The Northshore Utility District is presenting Required Supplemental Information (RSI) to meet minimum financial reporting requirements. This RSI, generally composed of schedules, statistical data and other information, is an integral part of the accompanying financial statements.

Northshore Utility District
Schedule of Proportionate Share of the Net Pension Liability
PERS Plans 1, 2 and 3
As of December 31, 2015
Last 10 Fiscal Years*

	2015 PERS 1	2015 PERS 2/3
Employer's proportion of the net pension liability (asset)	0.001194%	0.041330%
Employer's proportion of the net pension liability (asset)-PERS 1 UAAL	0.032000%	N/A
Employer's proportionate share of the net pension liability (asset)	$1,736,355	$1,476,744
Employer's covered employee payroll	$1,596,354	$2,144,044
Employer's proportionate share of the net pension liability as a percentage of covered employee payroll	108.77%	68.88%
Plan fiduciary net position	$2,041,687	$1,692,522
Plan fiduciary net position as a percentage of the total pension liability	117.58%	114.61%

*** Until a full 10-year trend is compiled, the District is presenting information only for those years which the information is available.**

REQUIRED SUPPLEMENTAL INFORMATION (concluded)

Northshore Utility District
Schedule of Employer Contributions
PERS Plans 1, 2 and 3
As of December 31, 2015
Last 10 Fiscal Years*

	2015 PERS 1	2015 PERS 2/3
Statutorily or contractually required contributions	$168,908	$212,022
Contributions in relation to the statutorily or contractually required contributions	($168,908)	($212,022)
Contribution deficiency (excess)	$0	$0
Covered employer payroll	$1,658,518	$2,081,880
Contributions as a percentage of covered employee payroll	10.2%	10.2%

*** Until a full 10-year trend is compiled, the District is presenting information only for those years which the information is available.**

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	(360) 902-0370
Toll-free Citizen Hotline	(866) 902-3900
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