

CASCADE WATER ALLIANCE

Financial Statements

For the Years Ended December 31, 2017 and 2016

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Independent Auditor's Report

**To the Board of Directors
Cascade Water Alliance
Bellevue, Washington**

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of Cascade Water Alliance (Cascade), which comprise the statements of net position as of December 31, 2017 and 2016, and the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements.

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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 entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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



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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the net position of Cascade as of December 31, 2017 and 2016, and the changes in its net position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matter

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and modified approach for White River/Lake Tapps Reservoir Project Infrastructure Capital Assets on pages 3 through 11 and on pages 34 through 39 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.



Certified Public Accountants
May 16, 2018

CASCADE WATER ALLIANCE

Management's Discussion and Analysis

Management's Discussion and Analysis presents our review of Cascade Water Alliance's (Cascade) net position as of December 31, 2017 and 2016, and Cascade's financial performance for the years then ended. These comments should be read in conjunction with Cascade's financial statements, which follow this section.

Overview of the Financial Statements

The financial statements include the Statements of Net Position, Statements of Revenues, Expenses, and Changes in Net Position, Statements of Cash Flows and Notes to Financial Statements.

The Statements of Net Position provide a record, or snapshot, of the assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position of Cascade at the close of the year. It provides information about the nature and amounts of investments in resources (assets) and obligations to creditors (liabilities). It provides a basis for evaluating the capital structure of Cascade and for assessing its liquidity and financial flexibility.

The Statements of Revenues, Expenses and Changes in Net Position present the results of the business activities over the course of the year. This information can be used to determine whether Cascade has successfully recovered all its costs through its user fees and other charges, and to evaluate its financial viability and credit worthiness.

The Statements of Cash Flows report cash receipts, cash payments and net changes in cash resulting from operating, capital and related financing and investing activities over the course of the year. The statements present information on where cash came from and what it was used for.

The Notes to Financial Statements provide useful information regarding Cascade's significant account balances and activities, certain material risks, estimates, obligations, commitments, contingencies, and subsequent events, if any.

Cascade's overall financial position is strong, with sufficient liquidity to finance operations and sufficient debt capacity to finance future capital asset acquisitions. Cascade is financed by equity and long-term debt.

Depreciable capital assets have increased due to Cascade obtaining sources of water supply and related water systems needed to deliver the supply. Cascade primarily serves a suburban area east of Lake Washington in King County.

Major debt financing to date includes:

- \$10,000,000 borrowed in 2004 from member Sammamish Plateau Water and Sewer District for acquisition of water supply sources and water systems (repaid from bond proceeds in 2006);
- \$25,904,442 owed to the City of Tacoma for acquisition of water supply sources and water systems (repaid from bond proceeds in 2006);
- Twenty-five year \$55,230,000 revenue bond proceeds (2006 revenue bonds) to pay the Sammamish Plateau Water and Sewer District and City of Tacoma and to finance system development (refunded by 2014 revenue bonds);
- Twenty-five year \$80,095,000 revenue bond proceeds (2009 revenue bonds) to acquire the Lake Tapps system from Puget Sound Energy (PSE) and to fund property acquisitions and pipeline construction along a potential water transmission corridor;

CASCADE WATER ALLIANCE

Management's Discussion and Analysis

Overview of the Financial Statements (Continued)

- Twenty-five year \$42,695,000 revenue bond proceeds (2012 revenue bonds) to acquire independent supply production capacity, to restructure the Tacoma Water Contract, to extend the Seattle Water Contract, and to fund Lake Tapps capital improvements; and
- Fifteen year \$29,220,000 refunding revenue bonds (2014 revenue bonds) to pay a portion of the cost of refunding the callable portion of the outstanding 2006 Bonds. The net proceeds were placed in an irrevocable trust with an escrow agent to provide funds for the future debt service payment on the refunded bonds. As a result, a portion of the 2006 bonds are considered defeased and the liability for those bonds has been removed from the statement of net position. The reacquisition price exceeded the net carrying amount of the old debt by \$2,692,477. This amount is being netted against the new debt and amortized over the remaining life of the refunding debt. The government advance refunded the 2006 revenue bonds to reduce its total debt service payments over 14 years by \$6,270,530 and to obtain an economic gain (difference between the present values of the debt service payments on the old and new debt) of \$5,462,625. At December 31, 2016, none of the defeased bonds remain outstanding.

Condensed Financial Statements

Statements of Net Position as of December 31, 2017, 2016 and 2015

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Current assets	\$ 34,455,947	\$ 21,144,611	\$ 21,027,024
Net capital assets	264,904,274	268,991,513	271,805,152
Other assets	<u>25,306,593</u>	<u>39,482,403</u>	<u>39,417,403</u>
Total Assets	<u>324,666,814</u>	<u>329,618,527</u>	<u>332,249,579</u>
Deferred Outflows of Resources	1,813,781	2,000,256	2,194,966
Current liabilities	27,105,308	15,609,607	14,964,179
Long-term liabilities	<u>217,216,599</u>	<u>241,207,476</u>	<u>253,018,894</u>
Total Liabilities	<u>244,321,907</u>	<u>256,817,083</u>	<u>267,983,073</u>
Net investment in capital assets	38,330,678	18,903,969	10,141,404
Restricted for-			
Debt service	18,192,395	18,258,323	23,158,989
Unrestricted	<u>25,635,615</u>	<u>37,639,408</u>	<u>33,161,079</u>
Total Net Position	<u>\$ 82,158,688</u>	<u>\$ 74,801,700</u>	<u>\$ 66,461,472</u>

CASCADE WATER ALLIANCE

Management's Discussion and Analysis

Financial Analysis

Current assets increased sharply in 2017 by over \$13 million over 2016 with the majority of the increase attributed to the increase in the current portion of restricted cash necessary to make the \$12 million Seattle payment in late 2018. Net capital assets decreased by \$4.1 million or 1.5% with the increases in capital projects offset by the amortization of the water contracts. Other assets decreased by \$14.2 million due largely as a result of restricted cash shifting to current assets. Deferred outflows of resources decreased by 9.3% due to the continued amortization of the deferred amount of bond refunding. Current liabilities increased in 2017 by \$11.5 million as the Seattle payment becomes due in 2018 while other payables and accrued liabilities decreased. Long-term liabilities decreased by 10.7%, due to payments to Tacoma and bond principal with no new long-term liabilities added. Invested in capital assets net of related debt increased by \$19.4 million as capital projects increased and related debt decreased. Restricted for debt service remained relatively flat in 2017. Unrestricted net assets which consist of accumulated assets that do not meet the definition of invested in capital assets, net of related debt or restricted decreased by 31.9% as overall net position increased by 9.8%.

Condensed Financial Statements

Statements of Revenues, Expenses and Changes in Net Position For the Years Ended December 31, 2017, 2016 and 2015

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Water sales	\$ 33,542,761	\$ 32,600,142	\$ 31,761,946
Administrative dues	3,303,660	3,103,512	2,966,435
Conservation program and other	991,476	1,062,670	2,911,519
Total Operating Revenue	37,837,897	36,766,324	37,639,900
Cost of water sold	23,025,616	21,451,656	19,909,486
Other operating costs	11,990,574	11,394,521	13,067,538
Total Operating Expenses	35,016,190	32,846,177	32,977,024
Operating Income	2,821,707	3,920,147	4,662,876
Nonoperating expenses	(5,102,745)	(5,332,041)	(5,597,562)
Capital contributions	9,638,026	9,752,122	8,854,373
Changes in Net Position	7,356,988	8,340,228	7,919,687
Net position, beginning of year	74,801,700	66,461,472	58,541,785
Net Position, End of Year	<u>\$ 82,158,688</u>	<u>\$ 74,801,700</u>	<u>\$ 66,461,472</u>

CASCADE WATER ALLIANCE

Management's Discussion and Analysis

Results of Operations

Operating revenues are received principally from water sales, administrative dues and conservation charges. Cascade commenced water sales in 2004 upon acquisition of the Seattle Water Contract from Seattle Public Utilities. Cascade collects capital contributions from its members. These contributions consist of Regional Capital Facilities Charges (RCFC's) and donated systems. RCFC's are due from members for new residential equivalent customers connecting to the members' systems. Donated systems consisted of a donation of a portion of the Bellevue Issaquah pipeline in 2004 valued at \$9,208,077.

Conservation charges decreased slightly in 2017 at \$799,767 from \$846,044 in 2016 as the corresponding conservation budget decreased slightly as well. Total operating revenues for 2017 were \$37,837,897 compared to \$36,766,324 for 2016, an increase of 2.9%, attributable to higher demand share and administrative dues. The cost of water sold increased by 7.3% in 2017. Increased water costs resulted in a 28.0% reduction in operating income for 2017. Nonoperating income/expenses increased by 4.3% due to better interest income in 2017. Capital contributions remained strong, down marginally by 1.2% in 2017 over 2016 as growth continued to exceed budget expectations. Overall net assets increased by 10.0% in 2017.

Capital Assets and Long-Term Debt

The capital assets of Cascade decreased \$4.1 million in 2017 with the amortization of the water contracts greater than expenditures related to ongoing capital projects. Capital asset expenditures have been funded from capital contributions and the 2006, 2009 and 2012 revenue bonds.

In 2012, Cascade issued revenue bonds in the amount of \$42,695,000. The proceeds of this obligation were used in 2012 and 2013 to acquire independent supply production capacity (by purchasing RCFC credits from Cascade members), to restructure the Tacoma Water Contract, to extend the Seattle Water Contract, and to fund Lake Tapps capital improvements.

In 2014, Cascade issued revenue bonds in the amount of \$29,220,000. The proceeds of this obligation were used to advance refund the 2006 bonds.

Seattle Water Contract - The Seattle water contract entitles Cascade to a specified amount of water each year for a fifty-year period ending December 31, 2053. The amount of the block can be amended based on new members joining Cascade or existing members withdrawing from Cascade prior to December 31, 2011, or a reduction in water yield available to Seattle due to an order of an appropriate federal or state regulatory agency. At the end of the contract term, Cascade may continue to purchase up to 5.3 million gallons per day (mgd) for members that cannot be economically served by any other means. In December 2008, this agreement was amended to entitle Cascade to a supplemental block of additional water through December 31, 2023.

In 2013, the negotiations were finalized that extend the contract with Seattle by 10 years, to 2063. The new contract extends current capacity of 30.3 mgd through 2039 and then ramps down throughout the remaining years. Under the contract extension, Cascade makes three scheduled capacity reservation payments to Seattle; the first payment was \$5 million in 2013 using bond proceeds, with subsequent payments in 2018 and 2024. Ratification of the contract occurred in July 2013.

CASCADE WATER ALLIANCE

Management's Discussion and Analysis

Capital Assets and Long-Term Debt (Continued)

Amortization of the Seattle water contract cost is based on the ratio of water to be supplied in that calendar year to total water to be supplied during the contract. Amortization expense for this contract was \$561,775 for the years ended December 31, 2017 and 2016, respectively.

Tacoma Water Contract - In December 2012, a new contract was signed with Tacoma. The new contract restructures the prior Tacoma supply contract, and it clarifies Cascade's rights and responsibilities for the previously purchased capacity to enable and transfer to specific third parties through a joint offering. Under the new contract, minimum water purchase volumes have been replaced by a structured capacity reservation schedule and a new capacity commitment of 8.0 mgd provided to Cascade through 2042. The 2012 bond proceeds are funding initial payments to Tacoma of \$20 million, which started with a payment of \$10 million in January 2013.

Prior costs incurred to obtain the 2005 Tacoma water contract consist of system development charges of \$16,484,000 and capacity reservation fees of \$9,420,442. The system development charges relate to the base amount of water, and capacity reservation fees relate to the additional water to be supplied. As part of the agreement with Tacoma, Cascade and Tacoma jointly offered the 2005 contract water supply to four cities (City of Bonney Lake, City of Auburn, City of Buckley, and City of Sumner) in 2013. In 2013, the City of Auburn agreed to purchase 2.5 mgd of the system development charges for \$7,893,300 and have an option to purchase all the capacity reservation fee portion of the 2005 Tacoma contract for \$1,427,864 with the option extending through June 2017. In 2017, the City of Auburn decided not to exercise their option and Cascade wrote off the remaining 2005 contract and the corresponding amortization.

In 2011, the City of Bonney Lake agreed to purchase \$2,747,334 as a base amount of 2005 Tacoma water contract from Cascade for the system development charge that Cascade had paid to Tacoma. In 2013, the City of Bonney Lake agreed to purchase an additional portion of the 2005 Tacoma water contract for \$391,222.

Interest Capitalization - Interest costs incurred for the acquisition and/or construction of assets are subject to capitalization based on the guidelines established by Governmental Accounting Standards Board (GASB) Statements No. 34 and 62. Interest paid was \$6,522,363 and \$6,825,660 for the years ended December 31, 2017 and 2016, respectively. Total interest incurred on bonds for the years ended December 31, 2017 and 2016, was \$6,422,774 and \$6,665,395, respectively. No interest was capitalized in 2017 and 2016.

System Infrastructure - In February 2012, a pipe leak at a delivery point of Seattle Public Utilities (SPU) water to a Cascade member utility (City of Tukwila) has prompted a review by attorneys and engineers of SPU and Cascade to determine which agency is financially responsible for pipe leaks and other unforeseeable incidents at water points of delivery, and to determine exactly at which physical system points each agency bears responsibility. The outcome of this review may lead to an increased annual operational financial obligation for Cascade.

Barrier Apron Improvement - In 2015, in coordination with the United States Army Corps of Engineers (USACE) and other interested parties, (Tribes, State and Federal fishery agencies) Cascade replaced the severely damaged downstream apron on the Barrier Structure with a newly designed and improved apron. The USACE Mud Mountain Dam Fish Passage Barrier Structure Apron Repair project (the Apron Repair Project) was a requirement of Reasonable and Prudent Alternative (RPA) action item under the Mud Mountain Biological Opinion and Conference Opinion issued to the USACE by the National Marine Fisheries Service in October 2014 (Bi-Op). Cascade performed the apron replacement on behalf of the USACE under the 2010 Cooperative Agreement. As with other Barrier Structure activities, the USACE was responsible for environmental and regulatory coordination, and obtaining all applicable environmental authorizations necessary to carry out the work.

CASCADE WATER ALLIANCE

Management's Discussion and Analysis

Capital Assets and Long-Term Debt (Continued)

Pipeline Routing: Tacoma Cascade Pipeline - The Tacoma Cascade Pipeline (TCP) is an eighteen-mile pipeline extending from the Tacoma Second Supply Pipeline to the Bellevue Issaquah pipeline. The TCP will deliver Tacoma water supply to Cascade members. Cascade has acquired property and easements for the entire eighteen-mile route, with the exception of portions along King County (County) roads for which a franchise with the County will be sought.

Projects in Process

The TCP project consists of three segments: 1) the 1.1-mile segment at the north end of the route along SR-900; 2) the northern segment between Segment 1 and Lake Youngs; and 3) the central segment between Lake Youngs to the Tacoma Second Supply Pipeline.

Construction of Segment 1 has been completed and the asset began depreciation in 2012. The pipeline's useful life is dependent on soil conditions, environment and other factors. Cascade will use a 50-year useful life for depreciation, which is consistent with other utilities' practices (like Seattle Public Utilities). Although construction is complete, the project will not be finalized until the Washington State Department of Transportation signs a final acceptance letter.

Prior to 2012, all three segments were considered as a single combined TCP project for the work and expenditures that occurred along the entire project. Starting in 2012, however, Segments 1, 2 and 3 are being accounted for separately, since separate decisions have been made for the future of each segment.

Previously capitalized expenditures related to Segment 2 were expensed in 2012 since it had become less probable that this segment would ultimately be put into service due to its complicated property and routing configuration.

Minor work and expenditures will continue on Segment 3, however, as it is far more likely than Segment 2 to ultimately be put into service. Segment 3 will not be operational until 2024 at the earliest. Starting in 2012, Segment 3 has been placed into "on hold" status until the project is more fully resumed. All or portions of the TCP are being evaluated for eventual integration into a region-wide water delivery resiliency system, and will be held as an asset by Cascade until the evaluation is completed by 2018 or so.

White River System Operator - Veolia Water started working on January 1, 2012, under contract by Cascade, to operate and maintain the White River - Lake Tapps Reservoir Project. For 2017, the fixed fee budget was \$1.8 million and a variable budget of \$.3 million. A Project Operations and Maintenance Manual was completed in 2012.

Security Improvements - After a security strategic plan was performed by Carollo Engineers in 2015, a study was conducted to look at each Cascade asset and evaluate them to determine the potential range of threats, liability, and impacts on operation in the event of a loss. Each asset was prioritized using a pairwise comparison, then prioritizations were refined based on operational importance, public safety, and economic value. Each asset was prioritized high, medium, or low. The majority of the construction for the security improvements project occurred in 2017.

CASCADE WATER ALLIANCE

Management's Discussion and Analysis

Projects in Process (Continued)

Powerhouse Valve #3 Replacement - An options analysis has been completed for powerhouse valve #3, with the recommended option being a configuration utilizing a new "plunger" valve and installing it in a cast in place of the concrete vault on the south side of the tailrace just outside the powerhouse. If successful, the new valve will dissipate energy, provide more flow capacity, be able to control flow and have a longer service life. Construction of the Valve #3 replacement was nearly complete at the end of 2016, with testing and calibration being performed in 2017.

Bellevue Issaquah Pipeline (BIP) - A Memorandum of Understanding was signed in 2013 between Cascade and the City of Bellevue to operate and maintain the BIP. A project to install meters along the BIP began in 2014 and will be completed in early 2018.

2012 Transmission and Supply Plan Update - The Cascade Water Alliance Board of Directors adopted the 2012 Transmission and Supply Plan (the 2012 TSP) in July 2012. This 2012 TSP fulfills Cascade's responsibility to submit a water system plan to the Washington State Department of Health. In addition, it supplements information on regional supply provided by each of its members in their respective individual water system plans. Cascade updates its TSP every six years. The TSP update includes analysis of regional growth and water demand. These have demonstrated that Cascade members will need less water than was anticipated in the 2004 TSP. The outcome of the TSP update determines Cascade's capital investment program for the next several years, including the extent of contracting with Seattle and Tacoma for water and the development schedule for Lake Tapps and water transmission systems. In 2010, Cascade determined that expenditures for TSP updates do not meet the criteria for being a capitalizable intangible asset, so expenditures for TSP update expenditures have been expensed accordingly.

Eastside Reservoir - Like the TCP, the Eastside Reservoir project is being evaluated for eventual integration into a region-wide water delivery resiliency system, and will be held as an asset by Cascade until the evaluation is completed, likely in 2018 as part of a larger board earthquake resiliency workshop.

Barrier Dam Intake Design Modifications - Cascade, working with the U.S. Army Corps of Engineers (USACE) to replace the 100 plus year old barrier dam with a more effective dam, hired an engineer to initially review the USACE's plans and then later to design the appropriate modifications. In 2017 the design of the modifications were completed and went out to bid as part of the USACE bid package. Subsequent to yearend Cascade and the USACE finalized four easements and a number of agreements moving the work forward. Additionally, USACE has awarded a bid for the construction of the project.

Other White River Lake Tapps Projects - Several repair and upgrade projects, as described more fully in Cascade's Capital Improvement Program, were advanced in 2017 and will continue in 2018, including:

- Network and IT architecture upgrades
- SCADA upgrades
- Valve house controls upgrade

CASCADE WATER ALLIANCE

Management's Discussion and Analysis

Invested Funds

In accordance with state investment laws, Cascade's governing body has entered into a formal interlocal agreement with Cascade'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 (Pool).

As of December 31, 2017, Cascade had the following investments:

Impaired Investments - As of December 31, 2017, 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. Additionally, the Impaired Pool accepted the cash out option for the residual investments in four commercial paper assets that were part of completed enforcement events. Cascade's share of the impaired investment pool principal is \$74,590 and Cascade's fair value of these investments is \$87,823.

Interest Rate Risk - As of December 31, 2017, the Pool's average duration was 1.02 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, 2017, Cascade'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, corporate note (rated at least "A"), municipal securities (rated at least "A" by two NRSROs), commercial paper (rated at least the equivalent of "A-1" by two NRSROs), certificates of deposit issued by qualified public depositories, repurchase agreements, and the Local Government Investment Pool managed by the Washington State Treasurer's Office.

Budget Variances

Capital expenditures in 2017 related to the White River Lake Tapps project improvements, the Tacoma contract, and other major capital expenditures, were held within budget.

RCFC revenue was budgeted to be \$8.4 million in 2017, but actual RCFC revenue was \$9.6 million due to improved construction growth in Cascade's service area. RCFC revenue is budgeted at \$9.0 million in 2018.

Interest revenue in 2017 was \$0.90 million greater than budgeted as interest rates improved slightly after years of prevailing and persistent low interest rates nationally.

The administrative and conservation dues were within budget in 2017.

Benefit costs in 2017 were 28% less than budgeted because of a switch to the Association of Washington Cities Employee Benefits Trust and having slightly fewer covered employees for the year.

Operation costs were \$.19 million higher in 2017 than 2016 due to an emergency repair to fix a leakage in the penstock and water quality monitoring efforts.

CASCADE WATER ALLIANCE

Management's Discussion and Analysis

Budget Variances (Continued)

Maintenance costs were \$.15 million higher in 2017 than 2016 due to additional methods being used to control milfoil.

USACE reimbursement was \$23,831 higher than budget due to a minor dam but \$24,917 lower than the 2016.

Total fund expenditures were held within budgeted amounts in 2017. In the Operating Fund, conservation program rebate expenditures were \$36,800 less than budgeted due to the lower than anticipated interest in the commercial rebate program. Unexpended funds are carried forward in fund balances and are incorporated into Cascade's rate model for future year budgeting and planning.

Requests for Information

This financial report has been prepared to provide readers with a general overview of the Cascade Water Alliance's finances. Questions concerning any of the information provided in this report, or requests for additional information, should be addressed to the Manager of Finance and Administration's Office, 520 112th Ave. NE, Suite 400, Bellevue, WA 98004.

CASCADE WATER ALLIANCE

**Statements of Net Position
December 31, 2017 and 2016**

	<u>2017</u>	<u>2016</u>
Assets		
Cash and cash equivalents	\$ 13,114,928	\$ 12,371,260
Regional capital facility charges receivable	2,888,869	2,438,363
Restricted cash and cash equivalents, current portion	17,520,404	5,412,161
Interest rebate receivable	367,964	378,949
Water rights receivable, current portion	391,222	391,222
Prepaid expenses	172,560	152,656
Total Current Assets	34,455,947	21,144,611
Capital Assets Net of Accumulated Depreciation:		
Equipment and furniture	1,659,422	1,626,343
Seattle water contract	22,267,611	22,267,611
Tacoma water contract	119,740,687	121,168,551
SR900 pipeline	10,021,201	10,021,201
Bellevue Issaquah pipeline	22,276,944	22,215,027
Lake Tapps buildings	2,644,405	2,644,405
	178,610,270	179,943,138
Less accumulated depreciation and amortization	(30,174,701)	(25,827,498)
	148,435,569	154,115,640
Capital Assets Not Being Depreciated:		
Lake Tapps - infrastructure	99,278,915	97,586,083
Projects in process and assets not yet in service-		
Tacoma Cascade Pipeline	16,927,223	17,027,223
Eastside reservoir	262,567	262,567
Total Capital Assets	264,904,274	268,991,513
Restricted cash and cash equivalents, net of current portion	17,022,069	30,806,657
Water rights receivable, net of current portion	8,284,524	8,675,746
Total Assets	\$ 324,666,814	\$ 329,618,527
Deferred Outflows of Resources:		
Advanced refunding of debt	\$ 1,813,781	\$ 2,000,256
Total Deferred Outflows of Resources	\$ 1,813,781	\$ 2,000,256

See accompanying notes.

CASCADE WATER ALLIANCE

Statements of Net Position (Continued)

December 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Liabilities and Net Position		
Payables and accrued liabilities	\$ 1,328,268	\$ 2,042,882
Payables related to Tacoma water contract, current portion	5,520,404	5,412,161
Payables related to Seattle water contract, current portion	12,000,000	
Long-term debt payable from unrestricted assets, current portion	<u>39,474</u>	<u>39,474</u>
	18,888,146	7,494,517
Payables From Restricted Assets:		
Accrued interest	2,612,162	2,710,090
Long-term debt payable from restricted assets, current portion	<u>5,605,000</u>	<u>5,405,000</u>
	<u>8,217,162</u>	<u>8,115,090</u>
Total Current Liabilities	27,105,308	15,609,607
Long-Term Debt, Net of Current Portion:		
Long-term debt payable from unrestricted assets	276,316	315,790
Long-term debt payable from restricted assets, net of bond issuance costs	<u>121,795,000</u>	<u>127,400,000</u>
	122,071,316	127,715,790
Other Long-Term Liabilities:		
Payable related to Seattle water contract, net of current portion	5,000,000	17,000,000
Payable related to Tacoma water contract, net of current portion	83,200,082	88,720,486
Bond premium, net of amortization	<u>6,945,201</u>	<u>7,771,200</u>
Total Liabilities	<u>\$ 244,321,907</u>	<u>\$ 256,817,083</u>
Deferred Inflows of Resources		
Net Position:		
Net investment in capital assets	\$ 38,330,678	\$ 18,903,969
Restricted for-		
Debt service	18,192,395	18,258,323
Unrestricted	<u>25,635,615</u>	<u>37,639,408</u>
Total Net Position	<u>\$ 82,158,688</u>	<u>\$ 74,801,700</u>

See accompanying notes.

CASCADE WATER ALLIANCE

**Statements of Revenues, Expenses and Changes in Net Position
For the Years Ended December 31, 2017 and 2016**

	<u>2017</u>	<u>2016</u>
Operating Revenue:		
Water sales	\$ 33,542,761	\$ 32,600,142
Administrative dues	3,303,660	3,103,512
Conservation program and other	991,476	1,062,670
Total Operating Revenue	37,837,897	36,766,324
Operating Expenses:		
Cost of water sold	23,025,616	21,451,656
Depreciation and amortization	4,594,420	4,473,988
Operations	2,439,263	2,258,840
Salaries and benefits	1,798,016	1,846,728
Professional services	1,619,771	1,524,482
Communication and public information	391,925	295,331
Maintenance	348,161	203,060
Rent	225,469	154,491
Miscellaneous	153,559	167,945
Conservation rebate program	125,895	175,031
Insurance	119,530	177,420
Office expenses	119,247	81,993
Dues and subscriptions	55,318	35,212
Total Operating Expenses	35,016,190	32,846,177
Operating Income	2,821,707	3,920,147
Nonoperating Revenue (Expenses):		
BAB rebate	1,125,861	1,137,660
Interest income	744,968	460,926
Interest expense	(6,618,925)	(6,930,627)
Loss on impairment of water rights	(354,649)	
Total Nonoperating Expenses	(5,102,745)	(5,332,041)
Capital Contributions:		
Regional capital facilities charges	9,638,026	9,752,122
Total Capital Contributions	9,638,026	9,752,122
Total Change in Net Position	7,356,988	8,340,228
Net position, beginning of year	74,801,700	66,461,472
Net Position, End of Year	\$ 82,158,688	\$ 74,801,700

See accompanying notes.

CASCADE WATER ALLIANCE

Statements of Cash Flows
For the Years Ended December 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Cash Flows From Operating Activities:		
Cash received from members	\$ 37,837,897	\$ 36,766,324
Cash paid to suppliers	(26,120,799)	(22,251,795)
Cash paid to and for employees	(4,601,840)	(4,471,386)
Net Cash Provided by Operating Activities	7,115,258	10,043,143
Cash Flows From Capital and Related Financing Activities:		
Regional capital facilities charges	9,187,520	8,713,687
Water rights receivable	391,222	391,222
Payments on long-term debt	(5,444,474)	(5,414,474)
Acquisition of capital assets	(7,779,843)	(8,725,318)
Loss on impairment of water rights	354,649	
Proceeds from disposition of land	100,000	
BAB rebate proceeds	1,125,861	1,137,660
Interest paid on bonds and other long-term debt	(6,727,838)	(7,028,290)
Net Cash Used in Capital and Related Financing Activities	(8,792,903)	(10,925,513)
Cash Flows From Investing Activities:		
Interest received	744,968	460,926
Net Cash Provided by Investing Activities	744,968	460,926
Net Change in Cash and Cash Equivalents	(932,677)	(421,444)
Cash and cash equivalents, beginning of year	48,590,078	49,011,522
Cash and Cash Equivalents, End of Year	\$ 47,657,401	\$ 48,590,078
Cash and Cash Equivalents Balance is Composed of the Following at December 31:		
Cash and cash equivalents	\$ 13,114,928	\$ 12,371,260
Restricted cash and cash equivalents	34,542,473	36,218,818
	\$ 47,657,401	\$ 48,590,078

See accompanying notes.

CASCADE WATER ALLIANCE

Statements of Cash Flows (Continued)
For the Years Ended December 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Reconciliation of Operating Income to Net Cash From Operating Activities:		
Net operating income	\$ 2,821,707	\$ 3,920,147
Adjustments to reconcile net operating income to net cash provided by operating activities-		
Depreciation and amortization	4,594,420	4,473,988
Changes in operating assets and liabilities-		
Prepaid expenses	(19,904)	37,564
Payables and accrued liabilities	<u>(280,965)</u>	<u>1,611,444</u>
Net Cash Provided by Operating Activities	<u>\$ 7,115,258</u>	<u>\$ 10,043,143</u>

See accompanying notes.

CASCADE WATER ALLIANCE

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

Note 1 - Organization and Summary of Significant Accounting Policies

Cascade Water Alliance (Cascade), established on April 1, 1999, converted from a Washington State nonprofit corporation to a Washington State joint municipal utility service corporation on July 12, 2012, in accordance with the Interlocal Cooperation Act (Chapter 39.34) and the Non-Profit Miscellaneous and Mutual Corporations Act (Chapter 24.06) as a public governmental body and an instrumentality of its members. Cascade exercises essential governmental functions by providing wholesale water to meet the current and future water supply needs of its members in a cost-effective and environmentally responsible manner.

Cascade members include the cities of Bellevue, Issaquah, Kirkland, Redmond and Tukwila, along with the Sammamish Plateau Water and Sewer District and the Skyway Water and Sewer District.

Basis of Accounting - Cascade uses the accrual basis of accounting and the total economic resources measurement focus. Expenses are recorded at the time liabilities are incurred, and revenues are recorded when earned.

Cash and Cash Equivalents - For purposes of the statements of cash flows, Cascade considers all highly liquid instruments purchased with an original maturity of three months or less and investments in the King County Treasurer's Investment Pool to be cash equivalents.

As of December 31, 2017 and 2016, the King County Investment Pool (the Pool) which holds Cascade investments 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 deposit issued by qualified public depositories, repurchase agreements, and the Local Government Investment Pool managed by the Washington State Treasurer's office.

Concentrations - Of the total operating revenue balance as of December 31, 2017, 75% is from four members. As of December 31, 2016, 80% of the balance was from three members.

Concentration of Credit Risk - Cascade maintains cash balances at financial institutions that at times exceed federally insured limits.

Capital Assets - Capital assets purchased at more than \$5,000, are recorded at cost. Water systems conveyed to Cascade by bill of sale are recorded at the contributing party's cost, contract price or appraised value. Major expenses for capital assets, including capital leases and major repairs that increase useful lives, are capitalized. Maintenance, repairs and minor renewals are expensed when incurred. Estimated useful lives for capital assets are as follows:

Computer equipment	5 years
Furniture and equipment	3 - 7 years
Tractors and heavy machinery	10 - 20 years
Pipelines	50 years

Cascade has elected to use the modified approach of accounting for the Lake Tapps asset. The modified approach allows Cascade to report as expenses in lieu of depreciation, infrastructure expenditures which maintain the asset but do not add to or improve the asset. Additions and improvements to the Lake Tapps asset are capitalized.

CASCADE WATER ALLIANCE

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

Note 1 - Continued

Regional Capital Facility Charges (RCFC) Receivable - RCFC receivables are stated at the amount management expects to collect from outstanding balances. Balances still outstanding after management has used reasonable collection efforts are written off through a charge to change in net position and a credit to accounts receivable.

Deferred Outflow of Resources - Deferred outflow of resources is the consumption of net position that is applicable to a future reporting period. A deferred outflow of resources involves no consumption of resources that results in either a net decrease in assets or a net increase in liabilities. Deferred outflows of resources presented in this manner on the accompanying financial statements are related to the advanced refunding of bonds.

Long-Term Debt - Long-term debt is reported net of discounts, premiums and issuance costs. Discounts, premiums and issuance costs incurred on issuance of long-term debt are amortized by the interest method over the period the related debt is outstanding. A portion of the long-term debt is funded by Build America Bonds and is eligible for an annual interest rebate of up to 35%. The amount of the subsidy payment for the Build America Bonds was reduced to 6.8% through September 30, 2016, increased to 6.9% effective October 1, 2016, and then further reduced to 6.6% effective October 1, 2017.

Net Position - Net position is classified in the following three components: 1) Invested in capital assets, net of related debt - This component of net position consists of capital assets, net of accumulated depreciation and amortization and reduced by the outstanding balances of any bonds, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. 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 invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net position component as the unspent proceeds. 2) Restricted - This component of net position consists of restrictions placed on net asset use by external creditors (such as through debt covenants), grantors or contributors. 3) Unrestricted net position - This component of net position consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

Revenues and Expenses - Revenues and expenses are distinguished between operating and nonoperating items. Operating revenues result from providing products in connection with the water system and services to members. Operating expenses include the costs associated with providing the products and services, general and administrative expenses and depreciation and amortization on capital assets. Nonoperating includes interest income rebates and expense, bond issuance costs, and losses on disposition of assets. All revenues and expenses not meeting these definitions are classified as nonoperating revenues and expenses.

Regional Capital Facilities Charges (RCFC) - RCFCs are paid to Cascade by each member for each new equivalent residential unit connected to its water distribution system, and are intended to allocate growth costs to those members that require capacity increases due to growth in customer demand. The RCFC for both 2017 and 2016 is \$6,005 per new Cascade Equivalent Residential Unit (CERU).

Federal Tax Status - Cascade Water Alliance is an authority and instrumentality of its governmental members, organized as a joint municipal utility service corporation pursuant to Washington State's Interlocal Cooperation Act (Chapter 39.34 RCW). As a governmental entity formed by political subdivisions of the State of Washington, it is exempt from federal income taxation under Section 115 of the Internal Revenue Code (the Code). As an instrumentality of its members, Cascade may issue obligations, the interest of which is exempt from federal income taxation under Section 103 of the Code.

CASCADE WATER ALLIANCE

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

Note 1 - Continued

Use of Estimates - The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures or expenses, as appropriate, during the reporting period. Actual results could differ from those estimates.

Compensated Absences - At termination of employment, employees may receive cash payments for accumulated vacation leave, based on current wages at termination for which an accrual has been provided.

Note 2 - Capitalizable Contracts

Seattle Water Contract - The Seattle Water Contract entitles Cascade to a specified amount (block) of water each year for a fifty year period ending December 31, 2053. The amount of the block can be amended based on new members joining Cascade prior to December 31, 2011, or a reduction in water yield available to Seattle due to an order of an appropriate federal or state regulatory agency. At the end of the contract term, Cascade may continue to purchase up to 5.3 million gallons per day (mgd) for members that cannot be economically served by any other means. In December 2008, this agreement was amended to entitle Cascade to a supplemental block of additional water through December 31, 2023.

In July 2013, a new contract was signed between the City of Seattle and Cascade which extends the contract by ten years, to 2063. The contract extends the current capacity of 30.3 mgd through 2039 and then ramps down through the remaining years. Under the contract extension, Cascade would make three scheduled capacity reservation payments to Seattle; the first payment of \$5 million was made in July 2013, with subsequent payments of \$12 million and \$5 million due in December 2018 and December 2024, respectively.

Amortization of the Seattle Water Contract cost is based on the ratio of water to be supplied in that calendar year to total water to be supplied during the contract. Amortization expense for this contract was \$561,775 for both years ended December 31, 2017 and 2016.

The Tacoma Water Contract - In December 2012, a water contract was signed between City of Tacoma and Cascade which superseded the Tacoma Water Contract signed in 2005. Under the water contract, minimum water purchase volumes have been replaced by a structured capacity reservation schedule, and a capacity commitment of 8.0 mgd is provided to Cascade through 2042. Cascade is required to make an annual installment payment in a range of \$1 million to \$6.8 million through 2042. The 2012 Tacoma Water Contract cost is amortized over the life of the contract which is 30 years. Amortization expense for this contract was \$3,991,356 for both years ended December 31, 2017 and 2016.

The system development charges relate to the base amount of water and the capacity reservation fees relate to the additional water to be supplied under the 2005 Tacoma Water Contract. The additional water supply will be amortized based on the ratio of the additional water to be supplied in that calendar year to total additional water to be supplied during the contract.

CASCADE WATER ALLIANCE

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

Note 2 - Continued

During 2011, the City of Bonney Lake entered into an agreement with Cascade for water rights purchase of the 2005 Tacoma Water Contract for a total of \$2,747,334. In 2013, City of Bonney Lake purchased an additional portion of water rights that extended the contract to 2019, with an annual payment of \$391,222 through maturity. At December 31, 2017 and 2016, the water rights receivable of \$782,446 and \$1,173,668, respectively, is included in the statements of net position.

During 2013, the City of Auburn entered into an agreement with Cascade for water rights purchase of the 2005 Tacoma Water Contract for a total of \$7,893,300 plus an annual interest at 3.20% starting in 2016 that expires 2029, with annual interest payments of \$252,586 from 2016 to 2019 and with annual principal and interest payments of \$934,805 thereafter. City of Auburn has an option to purchase all of the capacity reservation fees of the 2015 Tacoma Water Contract for a total price of \$1,427,864 with the option expiring June 2017. In 2017, Cascade was informed by the City of Auburn that they would not exercise their option to purchase 2.763 mgd worth of system development charge credits of the 6 mgd capacity reservation fee in Cascade's 2005 contract with Tacoma. With Auburn electing not to purchase the credits the remaining \$1,427,864 of the 2005 Tacoma Contract was written down in 2017, resulting in a loss on impairment of water rights of \$354,649. At December 31, 2017 and 2016, the water rights receivable of \$7,893,300 for both years is included in the statements of net position.

Interest Capitalization - Interest costs incurred for the acquisition and/or construction of assets are subject to capitalization based on the guidelines established by U.S. GAAP.

Total interest incurred on bonds for the years ended December 31, 2017 and 2016, was \$6,609,248 and \$6,930,627, respectively. The interest rebate related to the Build America Bonds was \$1,125,861 and \$1,137,660 for the years ended December 31, 2017 and 2016. No interest was capitalized in 2017 and 2016.

Project in Process -

Tacoma Cascade Pipeline - A pipeline extending from the Tacoma Water supply pipelines is under development to connect to the Bellevue Issaquah pipeline and deliver the Tacoma water supply to Cascade members. During the year ended December 31, 2009, management opted to defer completion of this project. The Transmission and Supply Plan was adopted by Cascade in July 2012 (and approved by King County in February 2013 and by the State Department of Health in March 2013) and projects 2024 as the estimated in-service date for this pipeline.

Eastside Reservoir - The Eastside Reservoir is a concrete reservoir and booster pump station constructed and owned by the City of Seattle to serve Cascade's members. The purchase of the Eastside Reservoir by Cascade was considered probable when the Tacoma Cascade Pipeline was moving forward and the project designs were capitalized. When the completion of the Tacoma Cascade Pipeline was deferred on December 31, 2009, plans to purchase the reservoir were deferred as well. In addition to its use as a potential storage facility for Tacoma water, Cascade is currently evaluating the purchase of the Eastside Reservoir as a method of providing earthquake resiliency to its members.

CASCADE WATER ALLIANCE

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

Note 3 - Cash and Cash Equivalents

In accordance with state investment laws, Cascade's governing body has entered into a formal interlocal agreement with Cascade'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 (Pool). Investments in the King County Investment Pool are measured at the net asset value per share of the pool shares held by Cascade. As of December 31, 2017, the net asset value at fair value price per share was \$0.9952.

As of December 31, Cascade had the following on deposit in the pool:

	<u>2017</u>	<u>2016</u>
Unrestricted cash and equivalents	\$ 13,205,411	\$ 12,701,225
Restricted cash and equivalents	<u>34,709,165</u>	<u>36,294,492</u>
	47,914,576	48,995,717
Add fair value adjustment	(230,101)	(102,335)
Less checks in excess of cash	<u>(27,074)</u>	<u>(303,304)</u>
Total Cash and Cash Equivalents	<u>\$ 47,657,401</u>	<u>\$ 48,590,078</u>

Impaired Investments - As of both December 31, 2017 and 2016, all impaired commercial paper investments had 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. Additionally, the Impaired Pool accepted the cash out option for the residual investments in four commercial paper assets that were part of completed enforcement events. At December 31, 2017 and 2016, Cascade's share of the impaired investment pool principal was \$74,590 and \$50,272, respectively, and Cascade's fair value of these investments was \$87,823 and \$119,944, respectively.

Interest Rate Risk - As of December 31, 2017 and 2016, the Pool's average duration was 1.02 and 1.10 years, respectively. 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 both December 31, 2017 and 2016, Cascade'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 deposit issued by qualified public depositories, repurchase agreements, and the Local Government Investment Pool managed by the Washington State Treasurer's Office.

CASCADE WATER ALLIANCE

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

Note 4 - Restricted Cash and Cash Equivalents

In accordance with the bond agreements, separate restricted accounts are required to be established. The assets held in these accounts are restricted for specific uses, including construction, debt service and other special reserve requirements. Current year disbursements from the restricted asset accounts are included in total expenditures in the financial statements.

Restricted cash and cash equivalents are presented in the statements of net position as of December 31 as follows:

	<u>2017</u>	<u>2016</u>
Restricted cash and cash equivalents, current portion	\$ 17,520,404	\$ 5,412,161
Restricted cash and cash equivalents, long-term	<u>17,022,069</u>	<u>30,806,657</u>
	<u>\$ 34,542,473</u>	<u>\$ 36,218,818</u>

Changes in restricted assets for the year ended December 31, 2017, are as follows:

	<u>Balance 12/31/2016</u>	<u>Additions</u>	<u>Disbursements</u>	<u>Net Return</u>	<u>Balance 12/31/2017</u>
Revenue bond funds	\$ 18,250,555	\$ 10,598,662	\$ (10,762,741)	\$ 94,665	\$ 18,181,141
Construction funds	<u>17,968,263</u>	<u>6,658,658</u>	<u>(8,308,637)</u>	<u>43,048</u>	<u>16,361,332</u>
	<u>\$ 36,218,818</u>	<u>\$ 17,257,320</u>	<u>\$ (19,071,378)</u>	<u>\$ 137,713</u>	<u>\$ 34,542,473</u>

For the year ended December 31, 2017, changes in restricted assets included interest earnings of \$182,598 and unrealized losses of \$87,933 for the revenue bond funds and interest earnings of \$121,907 and unrealized losses of \$78,859 for the construction funds.

Changes in restricted assets for the year ended December 31, 2016, are as follows:

	<u>Balance 12/31/2015</u>	<u>Additions</u>	<u>Disbursements</u>	<u>Net Return</u>	<u>Balance 12/31/2016</u>
Revenue bond funds	\$ 23,154,554	\$ 6,157,099	\$ (11,180,159)	\$ 119,061	\$ 18,250,555
Construction funds	<u>12,496,710</u>	<u>12,558,052</u>	<u>(7,118,988)</u>	<u>32,489</u>	<u>17,968,263</u>
	<u>\$ 35,651,264</u>	<u>\$ 18,715,151</u>	<u>\$ (18,299,147)</u>	<u>\$ 151,550</u>	<u>\$ 36,218,818</u>

CASCADE WATER ALLIANCE

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

Note 5 - Capital Assets

The following summarizes the changes in capital assets of Cascade:

	Balance 12/31/2016	Additions	Transfers	Deletions	Balance 12/31/2017
Capital Assets					
Being Depreciated:					
Equipment and furniture	\$ 1,626,343	\$ 33,079	\$ -	\$ -	\$ 1,659,422
Seattle water contract	22,267,611				22,267,611
Tacoma water 2005 contract	1,427,864			(1,427,864)	
Tacoma water 2012 contract	119,740,687				119,740,687
SR900 pipeline	10,021,201				10,021,201
Bellevue Issaquah pipeline	22,215,027	61,917			22,276,944
Lake Tapps buildings	2,644,405				2,644,405
Total Capital Assets					
Being Depreciated	179,943,138	94,996		(1,427,864)	178,610,270
Less accumulated depreciation and amortization	(25,827,498)	(5,420,417)		1,073,214	(30,174,701)
Depreciable Capital Assets, Net	154,115,640	(5,325,421)		(354,650)	148,435,569
Capital Assets Not					
Being Depreciated:					
Lake Tapps - infrastructure	97,586,083	1,692,832			99,278,915
Tacoma Cascade Pipeline	17,027,223			(100,000)	16,927,223
Eastside reservoir	262,567				262,567
Total Capital Assets Not					
Being Depreciated	114,875,873	1,692,832		(100,000)	116,468,705
Total Capital Assets	\$ 268,991,513	\$ (3,632,589)	\$ -	\$ (454,650)	\$ 264,904,274

CASCADE WATER ALLIANCE

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

Note 5 - Continued

	Balance 12/31/2015	Additions	Transfers	Deletions	Balance 12/31/2016
Capital Assets					
Being Depreciated:					
Equipment and furniture	\$ 1,579,426	\$ 46,917	\$ -	\$ -	\$ 1,626,343
Seattle water contract	22,267,611				22,267,611
Tacoma water 2005 contract	1,427,864				1,427,864
Tacoma water 2012 contract	119,740,687				119,740,687
SR900 pipeline	10,021,201				10,021,201
Bellevue Issaquah pipeline	22,176,148	38,879			22,215,027
Lake Tapps buildings	2,641,128	3,277			2,644,405
Total Capital Assets Being Depreciated	179,854,065	89,073			179,943,138
Less accumulated depreciation and amortization	(20,402,537)	(5,424,961)			(25,827,498)
Depreciable Capital Assets, Net	159,451,528	(5,335,888)			154,115,640
Capital Assets Not Being Depreciated:					
Lake Tapps - infrastructure	95,063,834	2,522,249			97,586,083
Tacoma Cascade Pipeline	17,027,223				17,027,223
Eastside reservoir	262,567				262,567
Total Capital Assets Not Being Depreciated	112,353,624	2,522,249			114,875,873
Total Capital Assets	\$ 271,805,152	\$ (2,813,639)	\$ -	\$ -	\$ 268,991,513

CASCADE WATER ALLIANCE

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

Note 6 - Long-Term Debt - Unrestricted

Long-term debt payable from unrestricted assets consisted of the following at December 31:

	<u>2017</u>	<u>2016</u>
<u>Public Works Trust Fund Loans (PWTF)</u>		
\$1,000,000 loan authorized, payable in equal annual principal payments based on the amount of the loan drawn to the payment due date with the first payment due July 2006 and the last payment due July 2025, plus interest at .50%, secured by net revenues.	\$ 315,790	\$ 355,264
Less current portion	<u>(39,474)</u>	<u>(39,474)</u>
Long-Term Portion	<u>\$ 276,316</u>	<u>\$ 315,790</u>

The estimated annual debt service requirements on long-term debt, payable from unrestricted assets are as follows:

For the Year Ending December 31,	<u>Principal</u>	<u>Interest</u>
2018	\$ 39,474	\$ 1,579
2019	39,474	1,382
2020	39,474	1,184
2021	39,474	987
2022	39,474	789
2023 - 2025	<u>118,420</u>	<u>1,184</u>
	<u>\$ 315,790</u>	<u>\$ 7,105</u>

Long-term debt, payable from unrestricted assets, activity was as follows:

	<u>Balance 12/31/2016</u>	<u>Proceeds</u>	<u>Repayments</u>	<u>Balance 12/31/2017</u>
Loan #PW-05-691-PRE-142	\$ 355,264	\$ -	\$ (39,474)	\$ 315,790
	<u>\$ 355,264</u>	<u>\$ -</u>	<u>\$ (39,474)</u>	<u>\$ 315,790</u>

	<u>Balance 12/31/2015</u>	<u>Proceeds</u>	<u>Repayments</u>	<u>Balance 12/31/2016</u>
Loan #PW-05-691-PRE-142	\$ 394,738	\$ -	\$ (39,474)	\$ 355,264
	<u>\$ 394,738</u>	<u>\$ -</u>	<u>\$ (39,474)</u>	<u>\$ 355,264</u>

CASCADE WATER ALLIANCE

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

Note 7 - Long-Term Debt - Restricted

Long-term debt outstanding payable from restricted assets consisted of the following at December 31:

	<u>2017</u>	<u>2016</u>
<u>Revenue Bonds</u>		
\$29,220,000 issued on August 5, 2014 for advanced refunding of the 2006 bonds and to pay the costs of issuing and selling the bonds. The bond is payable from and secured by a pledge of net revenues and assets held in the bond fund and construction fund; principal due serially through the year 2029, interest payable semi-annually at 4.00 annual percentage rate.	\$ 27,565,000	\$ 29,220,000
\$42,695,000 issued on December 27, 2012 for restructuring the Tacoma water contract in 2012, extending the Seattle water contract, acquiring independent supply production capacity, funding Lake Tapps capital improvements and cost of issuing the bond. The bond is payable from and secured by a pledge of net revenues and investments held in the bond fund and construction fund; principal due serially through the year 2038, interest payable semi-annually at 3.31 annual percentage rate.	38,550,000	39,645,000
\$80,095,000 issued October 15, 2009 for supporting capital program, providing for a debt service reserve and cost of issuing the bonds. The bonds are payable from and secured by a pledge of net revenues and investments held in the bond fund and construction fund.		
- \$4,940,000 term bonds due September 1, 2017, interest payable semi-annually 3.61 annual percentage rate.		
- \$75,155,000 due serially through September 1, 2034, with interest payable semi-annually 3.61 annual percentage rate.	<u>61,285,000</u>	<u>63,940,000</u>
	127,400,000	132,805,000
Less current portion	<u>(5,605,000)</u>	<u>(5,405,000)</u>
Total Long-Term Portion	<u><u>\$ 121,795,000</u></u>	<u><u>\$ 127,400,000</u></u>

The 2014 bonds were issued at a premium of \$4,396,430 which is being amortized over the life of the bonds. Amortization expense for the years ended December 31, 2017 and 2016 was \$512,437 and \$528,855, respectively.

The 2012 bonds were issued at a premium of \$5,764,037 which is being amortized over the life of the bonds. Amortization expense for the years ended December 31, 2017 and 2016 was \$313,563 and \$322,615, respectively.

CASCADE WATER ALLIANCE

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

Note 7 - Continued

The 2009 bonds were issued at a premium of \$761,955 which is being amortized over the life of the bonds. Amortization expense for the years ended December 31, 2017 and 2016 was \$0 and \$117,896 respectively.

The 2006 bonds were issued at a premium of \$1,857,106 which is being amortized over the life of the bonds. Amortization expense for the years ended December 31, 2017 and 2016 was \$0 and \$74,284, respectively.

On September 3, 2014, Cascade issued \$29,220,000 of Water System Refunding Revenue Bonds. The net proceeds of \$44,363,880 (after issuance costs of \$130,224) were used to advance refund a portion of the 2006 Series Revenue Bonds. The net proceeds were used to purchase U.S. government securities. Those securities were deposited into an irrevocable trust with an escrow agent to provide for future debt service payments on the refunded bonds. As a result, the refundable bonds are considered to be defeased, and the related liability for the bonds has been removed from Cascade's liabilities. This advanced refunding was undertaken to reduce total debt service payments over the next 15 years by \$17,630,530 and resulted in an economic gain of \$5,462,625. The net deferred amount of the advanced refunding was \$1,813,781 and \$2,000,256 as of December 31, 2017 and 2016, respectively.

The estimated annual debt service requirements on long-term debt payable from restricted assets are as follows:

For the Year Ending December 31,	<u>Principal</u>	<u>Interest</u>
2018	\$ 5,605,000	\$ 6,487,487
2019	5,830,000	6,233,097
2020	6,070,000	5,961,917
2021	6,320,000	5,676,845
2022	6,590,000	5,372,105
2023 - 2026	29,240,000	18,118,849
2027 - 2030	31,155,000	12,216,798
2031 - 2034	26,465,000	6,777,056
2035 - 2039	<u>10,125,000</u>	<u>1,874,817</u>
	<u>\$ 127,400,000</u>	<u>\$ 68,718,971</u>

Long-term debt, payable from restricted assets, activity was as follows:

	<u>Balance 12/31/2016</u>	<u>Proceeds</u>	<u>Repayments</u>	<u>Balance 12/31/2017</u>
Revenue bonds	\$ 132,805,000	\$ -	\$ (5,405,000)	\$ 127,400,000

	<u>Balance 12/31/2015</u>	<u>Proceeds</u>	<u>Repayments</u>	<u>Balance 12/31/2016</u>
Revenue bonds	\$ 138,180,000	\$ -	\$ (5,375,000)	\$ 132,805,000

CASCADE WATER ALLIANCE

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

Note 8 - Commitments

Lease Commitments - Cascade leases office space under a noncancelable lease agreement expiring in July 2023. The lease calls for payments of \$16,018 per month through July 2017, increasing to \$17,768 per month in August 2017, with additional annual stepped increases after the first year.

Future minimum rentals as of December 31 under noncancelable operating leases are as follows:

For the Year Ending December 31,

2018	\$ 215,905
2019	222,366
2020	228,827
2021	235,288
2022	241,749
2023	<u>143,219</u>

Total Minimum Rental Payments \$ 1,287,354

Rent expense for operating leases totaled \$225,469 and \$154,491 for the years ended December 31, 2017 and 2016, respectively.

Contracts - Cascade has entered into contracts with various vendors in relation to ongoing consulting services, construction services and financial services that extend beyond December 31, 2017.

Contracted services agreed to and expected to be expended in 2018 include the following:

Construction and design services	\$ 419,445
Consulting contracted services	<u>3,948,942</u>
	<u><u>\$ 4,368,387</u></u>

Note 9 - Retirement Benefits

Cascade provides a Section 401(a) defined contribution retirement plan (the Plan) to all full-time and certain part-time employees. Employees contribute 4% of their annual salary. Cascade contributes 7% of an employee's salary. In addition, as a replacement of the contribution to Social Security, employees contribute an additional 6.2% of their annual salary. Cascade contributes an additional 6.2% up to the limit (\$7,886 in 2017 and \$7,347 in 2016) established by the Internal Revenue Service. Employees are immediately vested upon enrollment and, therefore, have no forfeitures.

Employee and employer contributions were \$149,332 and \$178,865, respectively, for the year ended December 31, 2017 and \$150,289 and \$177,117, respectively, for the year ended December 31, 2016. As of December 31, 2017 and 2016, accrued expenses under the Plan totaled \$1,757 and \$36,905, respectively.

CASCADE WATER ALLIANCE

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

Note 9 - Continued

Cascade also provides a Section 457 retirement plan available to certain employees who make salary deferral contributions up to the maximum allowed by law. No employer contributions were made to the Section 457 retirement plan. Employee salary deferrals were \$170,586 and \$181,370 for the years ended December 31, 2017 and 2016, respectively.

Note 10 - Concentrations

All water purchases by Cascade were from the City of Seattle as further described in Note 2. Water sales, conservation revenues, administrative dues, regional capital facilities charges and contributions for member cities for the years ended December 31, 2017 and 2016 are as follows:

2017 Member Charges-

Members	Water Sales	Conservation Revenues	Administrative Dues	Regional Capital Facilities Charges	Total
Bellevue	\$ 17,746,629	\$ 320,766	\$ 1,325,012	\$ 2,690,240	\$ 22,082,647
Issaquah	1,362,252	67,746	279,842	1,921,600	3,631,440
Kirkland	4,798,055	91,435	377,698	693,578	5,960,766
Redmond	5,934,291	153,777	635,220	531,443	7,254,731
Sammamish	942,189	109,098	450,658	3,311,758	4,813,703
Skyway	368,039	18,307	75,624	243,203	705,173
Tukwila	2,391,306	38,638	159,606	246,204	2,835,754
	<u>\$ 33,542,761</u>	<u>\$ 799,767</u>	<u>\$ 3,303,660</u>	<u>\$ 9,638,026</u>	<u>\$ 47,284,214</u>

2016 Member Charges-

Members	Water Sales	Conservation Revenues	Administrative Dues	Regional Capital Facilities Charges	Total
Bellevue	\$ 17,740,677	\$ 347,005	\$ 1,272,906	\$ 2,555,128	\$ 21,915,716
Issaquah	969,014	62,444	229,060	831,693	2,092,211
Kirkland	4,663,342	99,332	364,378	1,176,980	6,304,032
Redmond	5,619,908	162,670	596,715	2,233,860	8,613,153
Sammamish	928,731	114,835	421,245	2,582,150	4,046,961
Skyway	341,880	19,483	71,468	3,003	435,834
Tukwila	2,336,590	40,275	147,740	369,308	2,893,913
	<u>\$ 32,600,142</u>	<u>\$ 846,044</u>	<u>\$ 3,103,512</u>	<u>\$ 9,752,122</u>	<u>\$ 46,301,820</u>

CASCADE WATER ALLIANCE

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

Note 11 - Stewardship, Compliance and Accountability

There have been no material violations of finance-related legal or contractual provisions, and there have been no expenditures exceeding legal appropriations.

Note 12 - Risk Management

Cascade Water Alliance is a member of the Water and Sewer Risk Management Pool (the Risk Pool). Chapter 48.62 RCW authorizes the governing body of any one or more governmental entities to form together into or join a pool 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 Risk Pool was formed on November 1987 when water and sewer districts 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. The Risk Pool currently has 61 members and a fiscal year of November 1st through October 31st.

The Risk Pool allows members to jointly purchase insurance coverage, establish a plan of self-insurance coverage, and provide related services, such as risk management and loss prevention. The Risk Pool provides the following forms of group purchased insurance coverage for its members: Property (including Building, Electronic Data Processing, Boiler and Machinery, and Mobile Equipment); General Liability; Automotive Liability; Excess Liability, Crime; Public Officials Liability; Identity Fraud Reimbursement Program; and bonds of various types. All coverages are on an “occurrence” basis.

Members make an annual contribution to fund the Pool. The Pool purchases insurance policies from unrelated underwriters as follows:

Type of Coverage	Member Deductible	Self-Insured Retention/Group	Excess limits
Property Loss:			
Buildings and Contents	\$1,000 - \$25,000 and See (C) below	\$25,000	\$1,000,000,000
Flood	See (A) below	See (A) below	\$50,000,000
Earthquake	See (B) below	See (B) below	\$110,000,000 (\$75,000,000 shared by all members, \$25,000,000 dedicated to Alderwood, \$5,000,000 dedicated to Sammamish Plateau, and \$5,000,000 dedicated to Cascade Water Alliance)
Terrorism	\$1,000 - \$25,000	\$25,000 Primary layer	\$100,000,000 Primary layer
Boiler and Machinery	\$1,000 - \$350,000 depending on object	\$25,000 - \$350,000 depending on object	\$100,000,000
Auto - Physical Damage	\$1,000-\$25,000	\$25,000	\$10,000,000

CASCADE WATER ALLIANCE

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

Note 12 - Continued

Type of Coverage	Member Deductible	Self-Insured Retention/Group	Excess limits
Liability:			
Commercial General Liability	\$1,000 - \$25,000	\$200,000	\$10,000,000
Auto Liability	\$1,000 - \$25,000	\$200,000	\$10,000,000
Public Officials Errors and Omissions	\$1,000 - \$25,000	\$200,000	\$10,000,000
Employment Practices	\$1,000 - \$25,000	\$200,000	\$10,000,000
Other:			
Public Officials Bonds	Various	N/A	Various
Crime	\$1,000 - \$25,000	\$25,000	\$2,000,000
Identity Fraud	\$0	\$0	\$25,000
A. \$100,000 member deductibles, per occurrence, in Flood zones except Zones A&V; \$250,000 member deductible per occurrence, in Flood Zones A&V.			
B. Member deductible for earthquakes is 5% subject to \$100,000 minimum Earthquake Shock. The deductible will apply per occurrence on a per unit basis, as defined in the policy form, subject to the stated minimum.			
C. Member deductible for Cyber liability is \$100,000 and where applicable the dollar amount of the business interruption loss during the policy's required 8 hour waiting period			

Pool members are responsible for a deductible on each coverage and the Pool is responsible for the remainder of the self-insured retention listed in the table above except where noted as follows. The insurance carriers then cover the loss to the maximum limit of the policy. Each member is responsible for the full deductible applicable to the perils of earthquake and flood (the Pool is not responsible for any deductible or self-insured retention for earthquake and flood claims). Each member is also responsible for the full deductible applicable to the Cyber Liability, and that part of a Boiler & Machinery deductible, which exceeds \$25,000.

Upon joining, the members contract to remain in the Pool for one full policy period. Following completion of one full policy period, members must give six months notice before terminating participation (e.g. to withdraw from the Pool on November 1, 2018, written notice must be in possession of the Pool by April 30, 2018). The Interlocal Governmental Agreement is renewed automatically each year. Even after termination of relationship with the Pool, a member is still responsible for contributions to the Pool for any unresolved, unreported, and in process claims, for the period that the District was a signatory to the Interlocal Governmental Agreement.

The Pool is fully funded by its member participants. Claims are filed by members with the Pool who determines coverage and performs claims adjustment in consultation with Arcadia Claims Services and Adjusters Northwest.

The Pool is governed by a Board of Directors, which is comprised of one designated representative from each participating member. An Executive Committee is elected at the annual meeting, and is responsible for overseeing the business affairs of the Pool and providing policy direction to the Pool's Executive Director.

CASCADE WATER ALLIANCE

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

Note 12 - Continued

Members make an annual contribution to fund the Risk Pool. The Risk Pool purchases insurance policies from unrelated underwriters as follows:

Type of Coverage	Member Deductible	Self-Insured Retention	Excess Limits
Property Loss:			
Buildings and contents	\$ 1,000	\$ 25,000	\$ 1,000,000,000
Flood	See (a) below	See (a) below	\$ 50,000,000
Earthquake	See (b) and (c) below	See (b) and (c) below	\$ 75,000,000
Terrorism	\$ 1,000	\$ 25,000	\$ 100,000,000
Boiler and machinery	\$ 1,000	\$ 25,000 - \$350,000	\$ 100,000,000
Auto - physical damage	\$ 1,000	\$ 25,000	\$ 10,000,000
Liability:			
Comprehensive general liability	\$1,000 (c) and (d)	\$ 200,000	\$ 10,000,000
Auto liability	\$ 1,000	\$ 200,000	\$ 10,000,000
Public officials errors and omissions	\$ 1,000	\$ 200,000	\$ 10,000,000
Employment practices	\$ 1,000	\$ 200,000	\$ 10,000,000
Other:			
Public officials bonds	Various	N/A	Various
Crime	\$ 1,000	\$ 25,000	\$ 2,000,000
Identity fraud	\$ -	\$ 25,000	\$ -

- a. \$100,000 member deductibles, per occurrence, in Flood zones except Zones A&V; \$250,000 member deductible per occurrence, in Flood Zones A&V.
- b. Member deductible for earthquakes is 5% subject to \$100,000 minimum Earthquake Shock. If the stated deductible is on a percentage basis, the deductible will apply per occurrence on a per unit basis, as defined in the policy form, subject to the stated minimum.
- c. In addition to the \$75,000,000 of shared earthquake coverage amongst pool members Cascade shares a \$10,000,000 policy with Sammamish Plateau Water that in the event that the earthquake did less than \$5,000,000 in damage to one of the parties then the other party would be able to collect the remaining available funds.
- d. Member deductible for Cyber liability is \$100,000 and where applicable the dollar amount of the business interruption loss during the policy's required 8 hour waiting period.

Risk Pool members are responsible for a deductible on each coverage and the Risk Pool is responsible for the remainder of the self-insured retention listed in the table above except where noted as follows. The insurance carriers then cover the loss to the maximum limit of the policy. Each member is responsible for the full deductible applicable to the perils of earthquake and flood (the Pool is not responsible for any deductible or self-insured retention for earthquake and flood claims). Each member is also responsible for the full deductible applicable to the Cyber Liability, and that part of a Boiler & Machinery deductible which exceeds \$25,000.

CASCADE WATER ALLIANCE

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

Note 12 - Continued

Upon joining, the members contract to remain in the Pool for one full policy period. Following completion of one full policy period, members must give six months' notice before terminating participation (e.g. to withdraw from the Pool on November 1, 2017, written notice must be in possession of the Risk Pool by April 30, 2017). The Interlocal Governmental Agreement is renewed automatically each year. Even after termination of relationship with the Risk Pool, a member is still responsible for contributions to the Risk Pool for any unresolved, unreported, and in process claims, for the period that the District was a signatory to the Interlocal Governmental Agreement.

The Risk Pool is fully funded by its member participants. Claims are filed by members with the Pool who determines coverage and performs claims adjustment in consultation with Arcadia Claims Services.

The Risk Pool is governed by a Board of Directors, which is comprised of one designated representative from each participating member. An Executive Committee is elected at the annual meeting, and is responsible for overseeing the business affairs of the Risk Pool and providing policy direction to the Risk Pool's Executive Director.

In the past three years (2016, 2015 and 2014), there have been no claim settlements, per occurrence or in aggregate, that have exceeded the coverage provided by excess/reinsurance contracts.

REQUIRED SUPPLEMENTARY INFORMATION

CASCADE WATER ALLIANCE

Required Supplementary Information For the Years Ended December 31, 2017 and 2016

Modified Approach for White River/Lake Tapps Reservoir Project Infrastructure Capital Assets

In accordance with GASB Statement No. 34, Cascade is required to account for and report infrastructure capital assets. Cascade defines infrastructure as the basic physical assets used by Cascade in the conduct of its business. Each major infrastructure system can be divided into subsystems. For example, the White River/Lake Tapps Reservoir Project (the Lake Tapps Project) can be divided into several distinct facilities: White River divergence; conveyance and sediment control systems; Lake Tapps Reservoir and embankments; outlet structure to forebay; penstocks; hydroelectric station; and tailrace and return to White River. For ease of defining the Lake Tapps Project, these facilities have been consolidated into three main subsystems: Upper Conveyance System (the White River divergence and conveyance and sediment control facilities); Reservoir and Embankments (or the Storage System consisting of the Lake Tapps Reservoir and dike facilities); and Lower Conveyance System (all facilities from the Lake Tapps outlet structure to the tailrace return to the White River). Subsystem detail is not presented in the basic financial statements; however, Cascade maintains detailed information on these subsystems.

Cascade has elected to use the “Modified Approach” as defined by GASB Statement No. 34 for infrastructure reporting for its Lake Tapps Project. Under GASB Statement No. 34, eligible infrastructure capital assets are not required to be depreciated under the following requirements:

- Cascade manages the eligible infrastructure capital assets using an asset management system with characteristics including: (1) an up-to-date inventory; (2) performance of condition assessments and summarization of the results using a measurement scale; and (3) an estimate of the annual amount required to maintain and preserve at the established condition assessment level.
- Cascade documents that the eligible infrastructure capital assets are being preserved approximately at or above the established and disclosed condition assessment level.

Capital Assets Assessment Prior to Cascade Ownership - In September 2006, prior to entering into the Asset Purchase Agreement with Puget Sound Energy, Inc. (PSE), Cascade received an Engineering Report (prepared by CH2MHill for Buck and Gordon, LLP and Cascade) which, among other things, included a Facility Condition Assessment and Capital Improvement Plan for the Lake Tapps Project. The condition assessment was based on a review of available documents (such as design documents, condition inspections conducted by or for PSE and operation and maintenance evaluations), cursory field inspections and observation and interviewing site (PSE) personnel. The report described the condition of major facilities constituting the Upper and Lower Conveyance Systems and recommended improvements. The following categories of improvements were used:

- Initial Capital Upgrade (ICU): Projects need to be completed immediately to allow proper operation, to reduce the rate of deterioration or to protect health and safety (by 2010).
- Short Term Improvement (STI): Projects recommended, but not necessary to maintain the current conditions of facilities (between 2011 and 2018).
- Long Term Improvement (LTI): Projects that should be replaced at the end of their projected useful life (between 2019 and 2050).
- Maintenance (M): Projects typically included in annual maintenance programs.

See independent auditor’s report.

CASCADE WATER ALLIANCE

**Required Supplementary Information
For the Years Ended December 31, 2017 and 2016**

Modified Approach for White River/Lake Tapps Reservoir Project Infrastructure Capital Assets (Continued)

The following is a listing of the major Lake Tapps Project facilities in the Upper Conveyance and Lower Conveyance Systems, with the category of facility improvement recommended by CH2MHill in 2006:

Upper Conveyance System:

Headworks Area Buildings	M; ICU; STI
Headgates	ICU; LTI
Rock Chutes	STI
Concrete Lined Canal	M
Timber Flume	LTI
6-Foot Outlet (Wolslegal Basin)	None
Fish Screen	STI
Twin Pipelines	M; STI; LTI

Lower Conveyance System:

Tunnel Inlet/Lake Outlet	ICU
12-Foot Concrete Tunnel	LTI
“Bear Pit” Overflow Shaft	LTI
Forebay Caisson and Building	M; LTI
Penstocks/Standpipes/Surge Chambers	ICU; STI; LTI
Powerhouse	ICU

In 2008, the Washington Department of Ecology’s Dam Safety Office (DSO) published the First Periodic Dam Safety Inspection Report for the Lake Tapps Project (Dikes 1 through 15). DSO inspected the Lake Tapps dikes in August 2007 and the report included an evaluation and analysis of the condition of the dikes and Printz Basin Backflow Prevention Structure.

The DSO report concluded that the dikes and the Backflow Prevention Structure “...appeared to be in good condition and the project meets current engineering standards for dam design and construction with regard to floods and earthquakes”. A few deficiencies were found and are summarized below:

- Refinements are necessary to the monitoring routines for Dikes 9,10 and 12;
- Dike 3 requires improvement to address potential for internal soil erosion, in conjunction with a proposed roadway improvement by Pierce County;
- Discharge capacity of the project may need to be increased to accommodate both the Local and General Storm Probable Maximum Flood;
- Relocating or adding weirs and adding seepage monitoring to Dike 8; and
- Completion of maintenance items, such as vegetation removal.

In 2012, DSO conducted the Second Periodic Dam Safety Inspection. Cascade addressed the issues raised by DSO.

See independent auditor’s report.

CASCADE WATER ALLIANCE

Required Supplementary Information For the Years Ended December 31, 2017 and 2016

Modified Approach for White River/Lake Tapps Reservoir Project Infrastructure Capital Assets (Continued)

DSO conducted a Dam Safety Inspection in February and July 2017. Overall, the condition of the dikes was considered Satisfactory, with no existing or potential safety deficiencies identified. Minor issues to be corrected to improve the maintenance and operation of the dikes were identified. Cascade addressed most of these issues, however the final inspection report was not received by the end of 2017, so any outstanding issues identified in the final report will be addressed in 2018.

Capital Assets Assessment Since Cascade Ownership - The Lake Tapps Project had been operated by PSE, under contract to Cascade, since Cascade acquired the Project from PSE in 2009. Cascade selected Veolia Water North America (Veolia) as its long-term contract operator for the project in January 2011. Veolia entered into the Transition Phase of the contract in January 2012 (observing PSE operation and training staff) and assumed all operation and maintenance responsibilities on April 16, 2012. During the Transition Phase (April through December 2012), Veolia, in addition to performing all necessary operation and maintenance activities:

- Developed Operation and Maintenance Manuals for all Project facilities;
- Selected and implemented a Maintenance Management System (MMS) for the Project; and
- Developed the 2013 Operations and Maintenance Budget for Cascade's approval.

The Manuals and 2013 budget were approved by Cascade and were the basis for Veolia's performance during 2013. The initial contract term was through 2016. Cascade extended the contract term for one additional five year period (through 2021) and may extend for one more additional period of up to five years. Annual revisions to the Manuals and Budget for 2014 through 2018 were negotiated and agreed upon and are the basis for Veolia's performance during these years.

CASCADE WATER ALLIANCE

Required Supplementary Information For the Years Ended December 31, 2017 and 2016

Modified Approach for White River/Lake Tapps Reservoir Project Infrastructure Capital Assets (Continued)

Since 2009, Cascade has conducted additional work including:

Facility Conditions Assessments:

- Contracted with AECOM to perform a condition assessment of certain Project facilities;
- Contracted with GeoEngineers to assess the condition of the dikes;
- Contracted with Carollo to develop security master plan;
- Contracted with Carollo Engineers to perform condition assessment on Lower Conveyance System;

Repair/Maintenance/Upgrade Activities:

- Contracted with NAES to repair and upgrade the Fish Screen Facility;
- Performed inspections and effected repairs to the Timber Flume and Twin Pipelines;
- Performed removal of sediment from settling basins during the 2010/2011, 2014/2015 outages, and 2017 outages;
- Implemented DSO recommended monitoring routines on Dikes 9,10 and 12;
- Implemented DSO recommendations on Dike 8 and Dike 10;
- Implemented seismic remediation project on Dike 3 in 2014/2015;
- Installed and upgraded piezometers in all Dikes and installed remote read capability on Dike 11;
- Demonstrated available discharge capacity;
- Completed PMP/PMF study;
- Performed repairs and inspection of the Barrier Structure in 2010, 2011, 2012, 2013, 2014, 2015, 2016, and 2017;
- Repaired the ecology block wall on Dike 13 in 2013;
- Repaired Tailrace "wingwall" adjacent to rail road crossing in 2011;
- Performed repairs on Dikes 2B, 3 and 11 in 2012;
- Performed repairs on Dikes 1, 3, 4 and 12 in 2013;
- Improved and upgraded Project security (fences, gates, locks, cameras, lighting, etc.);
- Improved and upgraded gaging stations;
- Repaired pipeline and valve leaks;
- Implemented plan for Powerhouse roof replacement;
- Replaced roofs on Headworks area buildings;
- Removed Gatekeeper residence and related outbuildings;
- Repaired pipeline and valve leaks;
- Implemented plan for Powerhouse roof replacement;
- Replaced roofs on Headworks area buildings;
- Removed Gatekeeper residence and related outbuildings;
- Upgraded SCADA system;

See independent auditor's report.

CASCADE WATER ALLIANCE

Required Supplementary Information For the Years Ended December 31, 2017 and 2016

Modified Approach for White River/Lake Tapps Reservoir Project Infrastructure Capital Assets (Continued)

- Developed plan to comply with L&I / DOSH recommendations; implementation is ongoing;
- Removed hazardous wastes from Powerhouse;
- Removed lead paint in Powerhouse;
- Installed electric meters and disconnected power to non-essential equipment;
- Removed and salvaged unnecessary or retired/obsolete equipment;
- Upgraded and replaced culverts at headworks and valve house;
- Stockpiled sand for emergencies at strategic locations;
- Replaced telephone system;
- Performed HPA required plantings along Tailrace and on Dike 11;
- Conducted inspections of all cranes and performed necessary maintenance and repairs;
- Implemented Lower Conveyance System repairs/improvements recommended by Carollo, including replacement of Tunnel Intake Trash Racks and Stop Logs, concrete repairs, maintenance of Tunnel Intake slide gate and replacement of fill gate; maintenance of Forebay slide gates, relief valve repairs and flow tube repairs;
- Contracted with HDR Engineering to design Timber Flume replacement and Headgate improvements;
- Completed replacement of the Timber Flume, including repairs to an existing section of concrete flume;
- Completed implemented Headgate Improvement Project;
- Performed repairs to slide gates at 6 foot valve in Dingle Basin;
- Inspected and performed repairs to ten 10 foot tunnels;
- Performed maintenance on Fish Screens;
- Installed new LED lighting in Powerhouse;
- Performed lead abatement measures, painting and repairs at Headworks structures;
- Installed new Valve No.3;
- Repaired Relief Valve No. 1;
- Repaired leak in Penstock No. 1 and 3;
- Performed routine maintenance and repairs on vehicles, pumps, valves and generators;
- Performed routine maintenance and repairs on roads; and
- Performed routine vegetation removal.

These activities expanded upon the CH2MHill assessment and implemented some of the recommendations from Carollo, CH2MHill, AECOM, GeoEngineers and DSO.

See independent auditor's report.

CASCADE WATER ALLIANCE

**Required Supplementary Information
For the Years Ended December 31, 2017 and 2016**

Modified Approach for White River/Lake Tapps Reservoir Project Infrastructure Capital Assets (Continued)

Capital Assets Funding - Based on the condition assessment work completed to date, Cascade has included funding for ongoing maintenance and repair of Lake Tapps Project Capital Assets in its annual operating budget as well as funding for upgrading and replacement of Lake Tapps Project Capital Assets in its Capital Improvement Plan (CIP). The Operation and Maintenance Budget and CIP for Cascade's 2017-2018 Biennium are summarized below:

Lake Tapps Project Operation and Maintenance Budget:

2018	\$	3,245,700
2019		3,343,071

Lake Tapps Project CIP Budget:

2018	\$	1,535,000
2019		1,835,000
2020		2,425,000
2021 - 2022		6,465,000

The Operation and Maintenance Budget and CIP for Cascade's 2017-2018 Biennium were adopted by the Board in October 2016.

The estimated and actual annual amount to maintain the infrastructure assets is summarized below:

For the Year Ending December 31,		<u>Estimate</u>	<u>Actual</u>
2013	\$	2,553,450	\$ 2,512,465
2014		2,553,450	3,071,494
2015		3,006,460	4,083,528
2016		2,076,415	2,461,900
2017		3,144,200	2,787,424

See independent auditor's report.