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**PROVIDENCE WATER SUPPLY BOARD  
(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)**

**FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED JUNE 30, 2016 AND 2015**

**PROVIDENCE WATER SUPPLY BOARD**  
**(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)**  
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## **Independent Auditors' Report**

To the Board of Directors of  
Providence Water Supply Board

### **Report on the Financial Statements**

We have audited the accompanying financial statements of Providence Water Supply Board (Water Supply Board) of the City of Providence, Rhode Island, as of and for the year ended June 30, 2016 and the related notes to the financial statements, as listed in the table of contents.

#### ***Management's Responsibility for the Financial Statements***

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

#### ***Auditors' Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

#### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Water Supply Board as of June 30, 2016 and the respective changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

## **Change in Accounting Principle**

During the fiscal year ended June 30, 2016, the City adopted new accounting guidance, GASB Statement No. 72, *Fair Value Measurement and Application*. Our opinion is not modified with respect to this matter.

## ***Emphasis of Matter***

### *Presentation*

As discussed in Note 1, the financial statements of the Water Supply Board are intended to present the financial position, the changes in financial position and, where applicable, cash flows of only that portion of the business-activities of the City of Providence that are attributable to the transactions of the Water Supply Board. They do not purport to, and do not, present fairly the financial position of the City of Providence as of June 30, 2016 and 2015, the changes in its financial position, or where applicable, its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

## ***Other Matters***

### *Prior Year Financial Statements*

The financial statements of the Providence Water Supply Board as of June 30, 2015 were audited by other auditors whose report dated April 1, 2016 expressed an unmodified opinion on those statements.

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 7 and the pension schedules on pages 28 through 30 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

## ***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated December 29, 2016, on our consideration of the Water Supply Board's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Water Supply Board's internal control over financial reporting and compliance.

*Blum, Shapiro & Company, P.C.*

Cranston, Rhode Island  
December 29, 2016

**PROVIDENCE WATER SUPPLY BOARD  
(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
JUNE 30, 2016 AND 2015**

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The management of the Providence Water Supply Board (the Water Supply Board) offers readers of our financial statements the following narrative overview and analysis of our financial activities for the years ended June 30, 2016 and 2015.

**Financial Statements**

Our financial statements are prepared using proprietary fund (enterprise fund) accounting that uses the same basis of accounting as private-sector business enterprises. Under this method of accounting an economic resources measurement focus and the accrual basis of accounting are used.

Revenue is recorded when earned and expenses are recorded when incurred. The financial statements include statements of net position, statements of revenues, expenses and changes in net position, and statements of cash flows. These statements are followed by notes to the financial statements.

- The statements of net position present information on the assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Water Supply Board is improving or deteriorating.
- The statements of revenues, expenses and changes in net position report the operating and non-operating revenues and expenses of the Water Supply Board for the fiscal year with the difference – the net income or loss – being combined with any capital contributions to determine the change in net position for the fiscal year. That change combined with the previous year-end net position total reconciles to the net position at the end of the fiscal year.
- The statements of cash flows report cash and cash equivalents activity for the fiscal year resulting from operating activities, non-capital financing activities, capital and related financing activities, and investing activities. The net result of these activities added to the beginning of the year cash balance reconciles to the cash and cash equivalents balance at the end of the fiscal year.

**PROVIDENCE WATER SUPPLY BOARD**  
**(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**JUNE 30, 2016 AND 2015**

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**Condensed Financial Information**

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Total current assets	\$ 62,360,519	\$ 56,860,298	\$ 50,845,457
Net property, plant and equipment	359,674,679	317,261,613	299,812,331
Total assets	<u>422,035,198</u>	<u>374,121,911</u>	<u>350,657,788</u>
Total current liabilities	13,183,282	13,498,670	9,928,198
Total long-term liabilities	157,876,249	123,484,780	75,559,279
Total liabilities	<u>171,059,531</u>	<u>136,983,450</u>	<u>85,487,477</u>
Deferred inflows of resources	<u>178,623</u>	-	<u>2,709,308</u>
Net position:			
Net investment in capital assets	256,129,467	239,087,594	225,543,538
Restricted fund	37,233,166	36,145,168	32,410,386
Unrestricted fund	<u>(42,565,589)</u>	<u>(38,094,301)</u>	<u>4,507,079</u>
Total Net Position	<u>\$ 250,797,044</u>	<u>\$ 237,138,461</u>	<u>\$ 262,461,003</u>
Total operating revenue	\$ 69,209,492	\$ 69,231,217	\$ 62,872,231
Total operating expenses	44,687,516	43,179,067	41,750,117
Depreciation	10,673,384	11,313,363	12,643,922
Total operating expenses including depreciation	<u>55,360,900</u>	<u>54,492,430</u>	<u>54,394,039</u>
Operating income	13,848,592	14,738,787	8,478,192
Nonoperating expense	(673,210)	(1,811,838)	(1,562,494)
Capital grants and contributions	<u>483,201</u>	<u>1,098,257</u>	<u>3,303,600</u>
Change in Net Position	<u>\$ 13,658,583</u>	<u>\$ 14,025,206</u>	<u>\$ 10,219,298</u>

**PROVIDENCE WATER SUPPLY BOARD  
(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
JUNE 30, 2016 AND 2015**

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**Financial Highlights**

During the year, the Water Supply Board had operating revenues that exceeded operating expenses by \$13.8 million. These are primarily due to rate relief to support the continued commitment to the replacement of aging infrastructure, careful management of operating costs, and unexpended revenues allocated for restricted funds. Total assets were \$422.0 million, up \$47.9 million from last year's total assets of \$374.1 million. Current assets, principally cash, decreased by \$1.0 million, and net plant increased by \$42.4 million.

The Water Supply Board's net position totaled \$250.8 million at June 30, 2016, an increase of \$13.66 million from June 30, 2015. The increase is the result of unexpended revenue allocated for restricted funds. Also, reflected in the change to our net position is net operating income of \$13.8 million, net non-operating expenses of \$0.67 million, and capital contributions of \$.48 million.

The Water Supply Board's net position totaled \$237.1 million at June 30, 2015, a decrease of \$25.3 million from June 30, 2014. The decrease is the result of recording the net pension liability in the amount of \$41.3 million to reflect implementation of GASB Statement No. 68. Also reflected in the change of our net position is net operating income of \$14.7 million, net non-operating expenses of \$1.8 million, capital contributions of \$1.1 million, and a prior period adjustment of \$2 million.

The Water Supply Board's total operating revenues were \$69.2 million for fiscal year 2016, which is consistent with the prior year. Total operating expenses of the water system amounted to \$55.4 million, which is a slight increase over the prior year's amount of \$54.5 million. Fiscal year 2016 non-operating revenue consisted of interest income amounting to \$404,534 and other revenue which is derived from a tax relief payment agreement between the Water Supply Board and Town of Foster. The agreement called for Town of Foster to reimburse Water Supply Board a total of \$1.6 million plus interest over the next 10 years. Non-operating expense of \$2.7 million was principally interest expense on long-term debt. Capital grants and contributions in fiscal year 2016 amounted to \$0.48 million.

The Water Supply Board's total operating revenues were \$69.2 million for fiscal year 2015, an increase of \$6.4 million over prior year's revenue of \$62.9 million. Total operating expenses of the water system amounted to \$54.5 million, which is slight increase over the prior year's amount of \$54.4 million. The increase in revenue in 2015 was attributable to the increase in rates authorized by the RI Public Utilities Commission (PUC) in December 2013. Fiscal year 2015 represents the first full fiscal year which reflects that increase in rates. Fiscal year 2015 non-operating revenue, principally interest, amount to \$324,754, and non-operating expenses of \$2.1 million was principally interest on long-term debt. Capital grants and contributions in fiscal year 2015 amounted to \$1.1 million.

The increase in revenue in fiscal year 2016 as compared to fiscal year 2015 was combinations of recognizing the Tax relief payment from Town of Foster, slight increase in consumption in retail customers, increase in Impact fees, miscellaneous revenue, and decrease in consumption in wholesale customers.

**PROVIDENCE WATER SUPPLY BOARD  
(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
JUNE 30, 2016 AND 2015**

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**Capital Assets and Debt Administration**

**Capital Assets:**

At June 30, 2016, the Water Supply Board had \$359.7 million invested in various capital assets, including land, buildings and improvements, transmission and distribution mains, reservoirs, services, hydrants and appurtenances, machinery and equipment, and construction work in progress. This amount represents a net increase in capital assets of \$42.4 million, or 11.8%, over the prior year.

At June 30, 2015, the Water Supply Board had \$317.3 million invested in various capital assets. This amount represented a net increase of \$17.4 million, or 5.8%, over the previous year.

**Major project expenditures in fiscal year 2016 included (in millions):**

*	Replace / upgrade water mains	\$	15.67
*	Administration Building Site Design/Land Acquisition	\$	11.20
*	Replace sand filters	\$	6.70
*	Supplemental Tunnel - Investigation Rehabilitation (2016)	\$	1.30
*	Pretreatment Pilot-Scale Evaluation	\$	1.06
*	Sludge handling / disposal	\$	1.01
*	Plant Influent and Aerator Rehabilitation	\$	0.92
*	Treatment Process Studies	\$	0.44
*	Replace fire hydrants	\$	0.41
*	Various Distribution System Improvements	\$	0.37
*	Unidirectional Flushing (UDF) Program Development	\$	0.31
*	Install Transmission Mains (W. Cranston)	\$	0.30
*	Replace distribution valves	\$	0.28
*	Replace lead services	\$	0.26
*	Aerated, Settled, and Filter Influent Conduits	\$	0.18
*	Replace 16 inch & larger valves	\$	0.15
*	90" influent conduit - inspection	\$	0.12
*	Treatment Plant On-Site Wastewater Treatment System	\$	0.12
*	COF - Operating Expenses	\$	0.12
*	Other Miscellaneous Projects	\$	0.55

The Water Supply Board's fiscal year 2016 capital budget included project expenditures of \$27.1 million for infrastructure and capital projects. The major projects were: water main replacements and upgrades, treatment plant filter replacements, plant influent and aerator upgrades, sludge removal and disposal, source water improvements, aerated settled and filter conduits, various distribution system improvements and installing transmission mains in Western Cranston. The Water Supply Board, in December 2015 purchased a new central operating facility and embarked on major improvements and renovations on the new facility which will be the new headquarters of the company. The majority of infrastructure projects are financed on a pay-as-you-go, cash basis from rate revenues. Some projects were funded from bond proceeds issued in fiscal year 2016. New capital additions, that will benefit ratepayers for many years, are generally funded with long-term debt financing.



**PROVIDENCE WATER SUPPLY BOARD  
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MANAGEMENT'S DISCUSSION AND ANALYSIS  
JUNE 30, 2016 AND 2015**

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**Debt:**

At June 30, 2016, the Water Supply Board had \$103.5 million in bonds and notes outstanding versus \$78.2 million in the previous year. This represented an increase of \$25.4 million or 24.5%. Providence Water Supply Board sought and received approval from the RI Division of Public Utilities (the Division) to borrow \$30 million from the RI Infrastructure Bank to finance the purchase and renovation of a new Central Operating Facility (COF). The Division's approval for this borrowing was the basis of rate relief authorized by the PUC that will generate additional revenue of \$2.1 million per year to fund the debt service associated with this borrowing.

A new \$30.0 million bond was issued in December 2016.

At June 30, 2015, the Water Supply Board had \$78.2 million in bonds and notes outstanding versus \$74.3 million in the previous year. This represented an increase of \$3.9 million, or 5%. A new \$8.0 million bond was issued in 2015 to fund various water main improvements.

**Subsequent Events**

Providence Water Supply Board has applied to the Public Utility Commission (PUC) for full rates increase across all classes of the Water Supply Board customer, effective February 2017. These rates range from 6.7% for the wholesale customers to 15.0% for the retail customers. The rates increase, if approved, would generate additional revenue of \$7.9 million, and allow the Water Supply Board to continue to improve and replace the aging infrastructure and maintain the continued supply of safe drinking water to the two thirds of the state of Rhode Island population it serves. The rates increase would also allow the water board to generate additional revenue to fund the debt service associated with future debt it will borrow. The increase would bring the annual revenue of the Water Supply Board to \$77.2 million.

Providence Water Supply Board is in the final stage of a merger and annexation with East Smithfield Water District to its water operation. The East Smithfield Water District currently serves about 2,400 customers in East Smithfield, and North Providence. When the merger and annexation is completed, Providence Water Supply Board customers' counts would increase to approximately 74,400 customers including its wholesalers. The merger is expected to be completed by mid-January 2017.

**Union Contract**

The labor force of the Water Supply Board, with the exception of management, is covered by a union contract which is effective for the period January 1, 2011 to June 30, 2016. A new contract was in negotiations at fiscal year-end and subsequently approved by the union and City. The new contract is effective for the period of July 1, 2016 through June 30, 2018.

**Contacting Providence Water's Financial Management**

This financial report is designed to provide our customers, investors and creditors with a general overview of the Providence Water Supply Board's finances and to illustrate the Providence Water Supply Board's accountability for the monies it receives. If you have questions about this report or need additional financial information, please contact the Finance Department at the Providence Water Supply Board, 552 Academy Avenue, Providence, RI 02908.

**PROVIDENCE WATER SUPPLY BOARD**  
**(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)**  
**STATEMENTS OF NET POSITION**  
**JUNE 30, 2016 AND 2015**

	<u>2016</u>	<u>2015</u>
Assets:		
Current unrestricted assets:		
Cash and cash equivalents	\$ 2,364,040	\$ 4,796,887
Accounts receivable, net of allowance for uncollectible accounts of \$1,242,827 in 2016 and \$1,247,078 in 2015	6,696,642	6,332,160
Accounts receivable - unbilled	2,843,801	3,441,854
Inventory	569,051	826,530
Other assets		300,455
Total current unrestricted assets	<u>12,473,534</u>	<u>15,697,886</u>
Current restricted assets:		
Cash and cash equivalents	42,041,914	39,989,014
Accounts receivable	60,571	16,959
Notes receivable - short term	127,439	
Total current restricted assets	<u>42,229,924</u>	<u>40,005,973</u>
Total current assets	<u>54,703,458</u>	<u>55,703,859</u>
Capital assets:		
Land	23,836,137	22,613,760
Building and improvements	103,048,502	84,679,611
Improvements other than buildings	326,348,497	311,430,903
Machinery and equipment	31,999,221	31,586,324
Scituate Reservoir Project	18,681,695	18,681,695
Construction in progress	73,252,031	55,087,340
	<u>577,166,083</u>	<u>524,079,633</u>
Less accumulated depreciation and amortization	217,491,404	206,818,020
Total capital assets, net	<u>359,674,679</u>	<u>317,261,613</u>
Other noncurrent assets:		
Notes receivable - long term	<u>1,308,387</u>	
Deferred Outflows of Resources:		
Pension-related deferred outflows of resources	<u>6,348,674</u>	<u>1,156,442</u>
Total assets and deferred outflows of resources	<u>422,035,198</u>	<u>374,121,914</u>

The accompanying notes are an integral part of the financial statements

**PROVIDENCE WATER SUPPLY BOARD**  
**(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)**  
**STATEMENTS OF NET POSITION (CONTINUED)**  
**JUNE 30, 2016 AND 2015**

	<u>2016</u>	<u>2015</u>
Liabilities:		
Current:		
Current portion of long-term debt	\$ 3,892,845	\$ 4,628,807
Due to City of Providence General Fund	643,624	1,394,422
Accounts payable	1,049,299	1,231,083
Accrued liabilities	<u>2,600,756</u>	<u>2,383,551</u>
	<u>8,186,524</u>	<u>9,637,863</u>
Amounts to be paid from current restricted assets:		
Due to Water Resources Board	360,017	400,400
Accounts payable	<u>4,636,741</u>	<u>3,460,405</u>
	<u>4,996,758</u>	<u>3,860,805</u>
Total current liabilities	<u>13,183,282</u>	<u>13,498,668</u>
Noncurrent liabilities:		
General revenue bonds	99,652,367	73,545,212
Net pension liability	50,365,882	43,268,573
Other post employment benefit obligations payable	<u>7,858,000</u>	<u>6,671,000</u>
Total noncurrent liabilities	<u>157,876,249</u>	<u>123,484,785</u>
Total liabilities	<u>171,059,531</u>	<u>136,983,453</u>
Deferred Inflows of Resources:		
Pension-related deferred inflows of resources	<u>178,623</u>	
Net Position:		
Net investment in capital assets	256,129,467	239,087,594
Restricted	37,233,166	36,145,168
Unrestricted	<u>(42,565,589)</u>	<u>(38,094,301)</u>
Total Net Position	<u>\$ 250,797,044</u>	<u>\$ 237,138,461</u>

The accompanying notes are an integral part of the financial statements

**PROVIDENCE WATER SUPPLY BOARD**  
**(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)**  
**STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION**  
**FOR THE YEARS ENDED JUNE 30, 2016 AND 2015**

	<u>2016</u>	<u>2015</u>
Operating Revenues:		
Charges for services:		
Water sales:		
General customers	\$ 47,413,514	\$ 46,859,419
Other local water suppliers	16,929,522	17,732,754
Fire protection services	2,322,938	2,308,161
Maintenance charges and other revenue	<u>2,543,518</u>	<u>2,330,883</u>
Total operating revenues	<u>69,209,492</u>	<u>69,231,217</u>
Operating Expenses:		
Source of supply	2,785,157	2,654,218
Pumping operations	755,951	724,018
Water treatment	7,376,945	8,227,250
Transmission and distribution	6,158,189	5,086,495
Charge for services provided by other City departments	839,167	839,167
Customer accounts and service	3,738,236	3,593,293
Administrative and general	16,014,991	15,031,845
Depreciation	10,673,384	11,313,363
Property taxes - other local governments	<u>7,018,880</u>	<u>7,022,781</u>
Total operating expenses	<u>55,360,900</u>	<u>54,492,430</u>
Operating Income (Loss)	<u>13,848,592</u>	<u>14,738,787</u>
Nonoperating Revenue (Expense):		
Interest income	404,534	324,754
Interest expense and other	(2,682,272)	(2,136,592)
Other revenues	<u>1,604,528</u>	<u>1,604,528</u>
Net nonoperating revenue (expense)	<u>(673,210)</u>	<u>(1,811,838)</u>
Capital Grants and Contributions	<u>483,201</u>	<u>1,098,257</u>
Change in Net Position	13,658,583	14,025,206
Net Position - Beginning of Year	<u>237,138,461</u>	<u>223,113,255</u>
Net Position - End of Year	<u>\$ 250,797,044</u>	<u>\$ 237,138,461</u>

The accompanying notes are an integral part of the financial statements

**PROVIDENCE WATER SUPPLY BOARD**  
**(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED JUNE 30, 2016 AND 2015**

	<u>2016</u>	<u>2015</u>
Cash Flows from Operating Activities:		
Receipts from customers	\$ 71,148,337	\$ 69,062,726
Payments to vendors	(24,401,681)	(25,137,957)
Payments to employees	(17,785,511)	(13,593,617)
Net cash provided by (used in) operating activities	<u>28,961,145</u>	<u>30,331,152</u>
Cash Flows from Capital and Related Financing Activities:		
Acquisition and construction of capital assets	(53,086,450)	(28,779,604)
Interest and issuance costs paid on debt	(2,682,272)	(2,136,592)
Principal payments on long-term debt	(4,628,807)	(4,094,774)
Proceeds from long-term debt	30,000,000	8,000,000
Proceeds from note receivable	168,702	
Capital grants	483,201	1,098,257
Net cash provided by (used in) capital and related financing activities	<u>(29,745,626)</u>	<u>(25,912,713)</u>
Cash Flows from Investing Activities:		
Investment income (loss)	404,534	324,754
Net cash provided by (used in) investing activities	<u>404,534</u>	<u>324,754</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(379,947)	4,743,193
Cash and Cash Equivalents - Beginning of Year	<u>44,785,901</u>	<u>40,042,708</u>
Cash and Cash Equivalents - End of Year	\$ <u>44,405,954</u>	\$ <u>44,785,901</u>
Unrestricted Cash and Cash Equivalents	\$ 2,364,040	\$ 4,796,887
Restricted Cash and Cash Equivalents	<u>42,041,914</u>	<u>39,989,014</u>
	\$ <u>44,405,954</u>	\$ <u>44,785,901</u>
Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used in) Operating Activities:		
Operating income (loss)	\$ 13,848,592	\$ 14,738,787
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:		
Depreciation	10,673,384	11,313,363
Provision for doubtful accounts	4,251	(269,904)
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	185,708	370,165
(Increase) decrease in inventories	257,479	53,282
(Increase) decrease in other assets	300,455	(268,752)
(Increase) decrease in deferred outflows of resources	(5,192,232)	(1,156,442)
Increase (decrease) in due to other funds	(750,798)	16,773
Increase (decrease) in accounts payable and accrued expenses	1,171,374	3,019,665
Increase (decrease) net pension liability	7,097,309	1,911,599
Increase (decrease) OPEB obligation	1,187,000	1,285,739
Increase (decrease) in deferred inflows of resources	<u>178,623</u>	<u>(683,123)</u>
Net Cash Provided by (Used in) Operating Activities	\$ <u>28,961,145</u>	\$ <u>30,331,152</u>

The accompanying notes are an integral part of the financial statements

**PROVIDENCE WATER SUPPLY BOARD  
(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)  
NOTES TO FINANCIAL STATEMENTS**

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**1. NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES**

**A. REPORTING ENTITY**

The Providence Water Supply Board, an enterprise fund of the City of Providence, (the Water Supply Board) was created in 1940 by Chapter 832 of the Public Laws of the State of Rhode Island. Membership of the Water Supply Board is comprised of four persons appointed by the Mayor, who serve for four-year staggered terms and two City Council members elected by the City Council who serve during their four-year City Council term. The Finance Director of the City of Providence also serves as an ex-officio Water Supply Board member.

The Water Supply Board provides water supply services through metered sales in Providence and parts of the surrounding communities of North Providence, Johnston and Cranston. The Water Supply Board also sells water to other local water supply systems on a wholesale basis. The Water Supply Board's source of water supply is the Scituate Reservoir, located in the Town of Scituate, Rhode Island, and five tributary reservoirs.

**B. SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation**

The Water Supply Board is considered an enterprise fund of the City of Providence (the City). The operations of the Water Supply Board are accounted for with a separate set of self-balancing accounts organized on a Proprietary Fund type (Enterprise Fund) basis.

Enterprise Funds are used to account for operations (a) that are financed and operated in a manner similar to private business enterprises where the intent of the governing body is that the costs (including depreciation) of providing goods and services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or change in net position is appropriate for capital maintenance, public policy, management control, accountability or other purposes.

The Water Supply Board utilizes the accrual basis of accounting, under which revenues are recognized when earned and expenses are recognized when incurred regardless of the timing of the related cash flows.

**Regulations and Operations**

The Water Supply Board is subject, as to rates and other matters, to the regulatory authority of the State of Rhode Island Public Utilities Commission (PUC).

**Cash Equivalents**

The Water Supply Board considers all highly liquid instruments with an original maturity of three months or less, when purchased, to be cash equivalents.

**Investments**

The Water Supply Board accounts for investments at fair values, which are established by quoted market prices in active markets that are accessible at the measurement date for identical, unrestricted assets. Fair value is defined as the price that two parties are willing to pay to acquire an asset or settle a liability in an orderly transaction in the market place.

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**Inventory**

Inventory, consisting of materials and supplies, is valued at the lower of average cost or market using the first-in, first-out method.

**Capital Assets, Depreciation and Amortization**

Capital assets owned by the Water Supply Board are stated at cost and are defined as assets with an initial cost of more than \$3,000 and an estimated useful life in excess of 1 year. Depreciation and amortization is provided over the estimated useful lives using the straight-line method. The estimated useful lives are as follows:

Building, source of supply structures and improvements	5-75 years
Improvements other than buildings	3-75 years
Equipment	3-50 years

Depreciation expense is not reflected for construction in progress until such time as it is placed in service. Assets under capital leases are amortized under the Water Supply Board's normal depreciation policies for similar assets.

**Restricted Funds for Construction of Assets**

Restricted funds for construction of assets represent unexpended revenue bond proceeds obtained specifically for construction of water facilities, as well as revenues restricted for capital improvements by the PUC. These funds are included in restricted assets.

**Capital Contributions**

Capital contributions consist of property and equipment paid for by customers for water installations. Once the installation is complete, the property and equipment transfers to the Water Supply Board at fair value.

**Impact Fees**

The impact fees assessment was established in 1996 when the Water Supply Board acquired the water distribution system in the City of Cranston. As part of the agreement for the acquisition, the Water Supply Board assumed all operation obligation, benefits and assets, and debt service related to the water distribution system, and created an impact fee agreement with the City of Cranston. In accordance with the City of Cranston ordinance, impact fee for the water system improvement must be set aside by the City of Cranston and paid to the Water Supply Board or deducted from the debt services the Water Supply Board pays to the City of Cranston.

The impact fee is assessed by the City of Cranston based on the agreement with the Water Supply Board. If new water systems facilities are required to serve areas where no water system presently exists, the Water Supply Board will collect a subdivision processing fee, and the City of Cranston will collect a water impact fee for the benefit of the Water Supply Board as follows: 1) residential \$1,352 per unit; 2) industrial and commercial \$6,003 per acre. The Water Supply Board in turn agreed to use the said impact fee solely for the purpose of construction of new water system facilities required to serve areas where no water system presently exists. In 2016, the \$60,570 in fees that had been collected was recognized by the Water Supply Board as revenue.

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**Revenues, Operating Revenues and Expenses**

Revenues include amounts billed and unbilled to all customers, including those customers outside the City of Providence. All billed charges are based on rates approved by the PUC. Revenues for unbilled amounts to general customers are estimated based on billing amounts subsequent to year-end. The Water Supply Board distinguishes operating revenues and expenses from nonoperating. Operating revenues result from charges to customers for water and related services. Operating expenses include the cost of operations, maintenance, sales and service, administrative expenses and depreciation. All revenues and expenses not meeting this definition are reported as nonoperating or capital contributions.

**Concentration of Credit Risk**

The Water Supply Board's financial instruments that are exposed to concentrations of credit risk consist primarily of accounts receivable. Exposure to losses on receivables is principally dependent on each customer's financial condition. Concentration of credit risk with respect to receivables is limited due to the large number of customers. The Water Supply Board monitors its exposure for credit losses and maintains allowances for anticipated losses.

**Use of Estimates**

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Compensated Absences**

Employees accumulate sick leave hours for subsequent use or for payment upon retirement. Sick leave and vacation may be carried forward into the following calendar year, but not to exceed 135 days and 30 days, respectively.

Vested sick leave and accumulated vacation leave are recorded as expenses and liabilities as the benefits accrue to employees.

**Deferred Outflows/Inflows of Resources**

In addition to assets, the statement of net position can report deferred outflows of resources. Deferred outflow of resources represents a consumption of net position that applies to a future period which will not be recognized as an outflow of resources (expense) until that later date. At June 30, 2016, the Water Supply Board reports deferred outflows related to pension in the statement of net position. A deferred outflow of resources related to pension results from differences between expected and actual experience, changes in assumptions or other inputs. These amounts are deferred and included in pension expense in a systematic and rational manner over a period equal to the average of the expected remaining service lives of all employees that are provided with benefits through the pension plan (active employees and inactive employees).



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In addition to liabilities, the statement of net position can report deferred inflows of resources. Deferred inflows of resources represent the acquisition of net position that applies to a future period and which will not be recognized as an inflow of resources (revenue) until a later date. A deferred inflow of resources related to pension results from differences between expected and actual experience, changes in assumptions or other inputs. These amounts are deferred and included in pension expense in a systematic and rational manner over a period equal to the average of the expected remaining service lives of all employees that are provided with benefits through the pension plan (active employees and inactive employees).

## **2. RESTRICTED ASSETS**

The State of Rhode Island enacted the Public Drinking Water Protection Act of 1987 (the Act) that empowers suppliers of public drinking water to levy a surcharge (the surcharge) of one cent (\$0.01) per hundred gallons of water for all customers. The surcharge has been amended several times since 1987. The last increase was on July 1, 2002, when the surcharge increased to \$0.0292 per hundred gallons of water for all customers. Of those collected funds, the Water Supply Board will retain 36.1% of the surcharge in its Water Quality Protection Fund, remit 57.0% to the State Water Resources Board and retain 6.9% for general operations. The funds collected in the Water Quality Protection Fund are to be expended in the following manner:

- at a minimum, 55% of the funds are to be spent for the acquisition of land or land rights or physical improvements to acquired land to protect the quality of the raw water of the water supply system;
- 35% may be used to acquire a fee simple interest or a conservation restriction that directly protects the quality and safety of the public drinking water supply; and
- 0% may be used by the supplier for any purpose relating to its operations.

The restricted investments are pooled with the cash and cash equivalents and investments of other funds maintained by the City of Providence. The earnings from investments are allocated in proportion to each fund's balance.

## **3. CASH**

The following is a summary of cash and investments:

	<u>2016</u>	<u>2015</u>
Cash and cash equivalents	\$ 2,364,040	\$ 4,796,887
Restricted cash and cash equivalents	<u>42,041,914</u>	<u>39,989,014</u>
	<u>\$ 44,405,954</u>	<u>\$ 44,785,901</u>

Responsibility for custodial credit risk of deposits, investment risk, interest rate risk and concentration of investments rests with the City. However, the deposits for the Water Supply Board are supported by collateralization agreements with its main banking institutions. These agreements collateralize the deposits at 102%. Of the cash and cash equivalent balances of \$44,405,954, \$250,000 is covered by Federal Deposit Insurance Corporation (FDIC) insurance and \$2,114,040 is uncollateralized.

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**4. CAPITAL ASSETS**

The following is a summary of the activity in capital assets as of June 30, 2016:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Disposals/ Transfers</u>	<u>Ending Balance</u>
Capital assets not being depreciated:				
Land	\$ 22,613,760	\$ 1,222,377	\$	\$ 23,836,137
Scituate Reservoir Project	18,681,695			18,681,695
Construction in progress	55,087,340	71,876,564	53,711,873	73,252,031
Total capital assets not being depreciated	<u>96,382,795</u>	<u>73,098,941</u>	<u>53,711,873</u>	<u>115,769,863</u>
Capital assets being depreciated:				
Buildings and improvements	84,679,611	18,368,891		103,048,502
Sewer and infrastructure	311,430,903	14,917,594		326,348,497
Equipment	31,586,324	412,897		31,999,221
Total capital assets being depreciated	<u>427,696,838</u>	<u>33,699,382</u>	<u>-</u>	<u>461,396,220</u>
Less accumulated depreciation for:				
Buildings and improvements	61,474,932	5,328,975		66,803,907
Sewer and infrastructure	117,431,723	4,600,171		122,031,894
Equipment	27,911,365	744,238		28,655,603
Total accumulated depreciation	<u>206,818,020</u>	<u>10,673,384</u>	<u>-</u>	<u>217,491,404</u>
Total capital assets being depreciated, net	<u>220,878,818</u>	<u>23,025,998</u>	<u>-</u>	<u>243,904,816</u>
Capital Assets, Net	<u>\$ 317,261,613</u>	<u>\$ 96,124,939</u>	<u>\$ 53,711,873</u>	<u>\$ 359,674,679</u>

The following is a summary of the activity in capital assets as of June 30, 2015:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Disposals/ Transfers</u>	<u>Ending Balance</u>
Capital assets not being depreciated:				
Land	\$ 21,958,397	\$ 655,363	\$	\$ 22,613,760
Scituate Reservoir Project	18,681,695			18,681,695
Construction in progress	47,609,161	24,438,961	16,960,782	55,087,340
Total capital assets not being depreciated	<u>88,249,253</u>	<u>25,094,324</u>	<u>16,960,782</u>	<u>96,382,795</u>
Capital assets being depreciated:				
Buildings and improvements	79,135,020	5,544,591		84,679,611
Improvements other than buildings	297,055,247	14,375,656		311,430,903
Machinery and equipment	30,877,466	708,858		31,586,324
Total capital assets being depreciated	<u>407,067,733</u>	<u>20,629,105</u>	<u>-</u>	<u>427,696,838</u>
Less accumulated depreciation for:				
Buildings and improvements	55,267,185	6,207,747		61,474,932
Sewer and infrastructure	113,064,008	4,367,715		117,431,723
Equipment	27,173,462	737,903		27,911,365
Total accumulated depreciation	<u>195,504,655</u>	<u>11,313,365</u>	<u>-</u>	<u>206,818,020</u>
Total capital assets being depreciated, net	<u>211,563,078</u>	<u>9,315,740</u>	<u>-</u>	<u>220,878,818</u>
Capital Assets, Net	<u>\$ 299,812,331</u>	<u>\$ 34,410,064</u>	<u>\$ 16,960,782</u>	<u>\$ 317,261,613</u>

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**5. LONG-TERM DEBT**

Long-term debt activity for the years ended June 30, 2016 and 2015, was as follows:

		<b>2016</b>				
		<u><b>Beginning Balance</b></u>	<u><b>Additions</b></u>	<u><b>Reductions</b></u>	<u><b>Ending Balance</b></u>	<u><b>Due Within One Year</b></u>
Bonds payable:						
Revenue bonds	\$	<u>78,174,019</u>	<u>\$ 30,000,000</u>	<u>\$ 4,628,807</u>	<u>\$ 103,545,212</u>	<u>\$ 3,892,845</u>
Long-Term Liabilities	\$	<u><u>78,174,019</u></u>	<u><u>30,000,000</u></u>	<u><u>4,628,807</u></u>	<u><u>103,545,212</u></u>	<u><u>3,892,845</u></u>
		<b>2015</b>				
		<u><b>Beginning Balance</b></u>	<u><b>Additions</b></u>	<u><b>Reductions</b></u>	<u><b>Ending Balance</b></u>	<u><b>Due Within One Year</b></u>
Bonds payable:						
Revenue bonds	\$	<u>74,268,793</u>	<u>\$ 8,000,000</u>	<u>\$ 4,094,774</u>	<u>\$ 78,174,019</u>	<u>\$ 4,628,807</u>
Long-Term Liabilities	\$	<u><u>74,268,793</u></u>	<u><u>8,000,000</u></u>	<u><u>4,094,774</u></u>	<u><u>78,174,019</u></u>	<u><u>4,628,807</u></u>

The following is a summary of bonds and notes outstanding at June 30, 2016 and 2015:

<u><b>Description</b></u>	<u><b>Amount of Interest Rate (%)</b></u>	<u><b>Outstanding June 30, 2016</b></u>	<u><b>Outstanding June 30, 2015</b></u>
Safe Drinking Water Bonds (CWFA FY2002)	3.61%	\$ 924,704	\$ 1,061,245
Scituate Reservoir Project (PPBA FY 2011)	5.40%	368,258	504,774
Safe Drinking Water Bonds (CWFA FY2008)	2.85%	26,703,000	28,181,000
Safe Drinking Water Bonds (CWFA FY2010)	.0410% to 3.14%	7,458,250	8,660,000
Safe Clean Water Bonds (CWFA FY2012)	.072% to 3.26%	2,621,000	2,748,000
Safe Clean Water Bonds (CWFA FY2013)	.019% - 2.53%	3,842,000	4,021,000
Safe Drinking Water Bonds (CWFA FY2013)	.022% - 2.63%	23,960,000	24,998,000
Safe Drinking Water Bonds (CWFA FY2013)	.022% - 3.01%	7,668,000	8,000,000
Safe Drinking Water Bonds (CWFA FY2015)	.022% - 3.01%	30,000,000	
Total		<u>\$ 103,545,212</u>	<u>\$ 78,174,019</u>

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Scheduled principal maturities of long-term debt are as follows:

<u>Fiscal Year</u>	<u>Principal</u>	<u>ARRA Principal Forgiveness</u>	<u>Interest and Fees</u>	<u>Total</u>
2017	\$ 3,892,845	\$ (203,572)	\$ 2,542,880	\$ 6,232,153
2018	5,284,015	(270,262)	2,660,271	7,674,024
2019	5,312,106	(274,967)	2,557,456	7,594,595
2020	5,349,503	(280,369)	2,444,485	7,513,619
2021	5,474,936	(286,671)	2,322,402	7,510,667
2022-2026	28,850,557	(1,541,365)	8,912,270	36,221,462
2027-2031	30,804,250	(1,779,034)	5,047,793	34,073,009
2032-2036	<u>18,577,000</u>	<u>(1,027,296)</u>	<u>1,262,685</u>	<u>18,812,389</u>
Total	\$ <u>103,545,212</u>	\$ <u>(5,663,536)</u>	\$ <u>27,750,242</u>	\$ <u>125,631,918</u>

## **6. TRANSACTIONS WITH CITY OF PROVIDENCE, RHODE ISLAND**

The City of Providence performs various services for the Water Supply Board including certain accounting, personnel and cash management services and working capital support. The total billing to the Water Supply Board for services performed amounted to \$839,167 for each of the years ended June 30, 2016 and 2015. This amount is established by the City, approved by the Water Supply Board and ultimately approved by the PUC. The Water Supply Board also provides services to various City funds and departments, the charges for which have been included as revenue in the accompanying financial statements. Included within the due to City of Providence General Fund balance on the statements of net position are the related balances due for the services described above. The balance also includes payments for pension and post-employment benefits. The total balance due to the City of Providence General Fund at June 30, 2016 and 2015, totaled \$643,624 and \$1,394,422, respectively.

## **7. LINE OF CREDIT**

The Water Supply Board opened a line of credit with Century Bank of \$5,000,000 in 2013. This line of credit is used for infrastructure replacement and renewed annually per the agreement terms. The balance as of June 30, 2016 and 2015 was \$-0-.

## **8. COMMITMENTS AND CONTINGENCIES**

### **Risk Management**

The Water Supply Board has a complete comprehensive insurance program protecting all facilities, employees and liability claims.

The Water Supply Board is subject to various claims and litigation that arise in the ordinary course of its operations. Legal counsel and management are of the opinion that the Water Supply Board's liabilities in such cases, if decided adversely to the Water Supply Board, would not materially affect the financial statements.

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**Union Contract**

The labor force of the Water Supply Board, with the exception of management, is covered by a union contract, which is effective for the period July 1, 2015 to June 30, 2018.

**Lead Service Replacement Program**

The Environmental Protection Agency (EPA) Lead and Copper Rule (the Rule) requires that systems monitor drinking water at the customer tap. In accordance with the Rule, if after corrosion control optimization is implemented lead concentrations exceed an action level of 15 ppb in more than 10% of customer taps sampled, the system is required to replace lead service lines under its ownership. The regulations require that the utility must replace annually 7% of the total amount of lead services in the system. In accordance with EPA requirements, the Rhode Island Department of Health (RIDOH) found that the Water Supply Board exceeded the lead action level on September 30, 2006 (the date of conclusion of that monitoring period) and was required to begin the annual replacement of 7% of its 25,600 lead services. Because of lead-time in gearing up for an undertaking of this magnitude, RIDOH and the Water Supply Board agreed to a compliance schedule that fulfilled the intent of the regulation whereby 14% of the lead services were to be replaced over the two-year period ending September 30, 2008 and 7% annually thereafter.

By September 2010, the Water Supply Board exceeded the lead service replacement requirement by over 2,200 services and as a result of being approximately one year ahead of the regulatory required pace, we were informed by RIDOH that the mandated replacements of lead service could be suspended until October 2011.

During this period, various concerns were raised about the effectiveness of partial lead service replacements, the persistence of lead levels in the water, and the difficulty of finding a proven solution for reducing the levels. In June 2012 the RIDOH, in concert with the EPA, agreed to enter into a consent agreement with the Water Supply Board, which granted a stay of the lead service replacement requirement for construction season 2012. As part of the agreement, RIDOH and the EPA required that the Water Supply Board convene a panel of national water quality experts, to include regulators, water professionals and members of academia, to recommend studies and/or treatment modifications with the objective of reducing lead levels in the water. In 2013, the Water Supply Board was granted a stay of the lead services replacement requirement for the 2013 construction season.

In April 2014, RIDOH granted the Water Supply Board a stay of the lead service replacement requirement for the 2014 construction season. By consent order the City of Providence is required to:

1. Continue with the consultation with its expert panel to evaluate corrosion control treatment in the system.
2. Conduct studies to examine alternative treatment schemes for optimization of corrosion control.
3. Continue a unidirectional flushing program.
4. Continue to rehabilitate and replace unlined cast iron mains that are usually found to be problematic in terms of both water quality and delivery capacity.

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Even though the lead service replacement program is temporarily suspended, lead services are still replaced in conjunction with the water main replacement program. Lead services are also replaced on an ongoing basis where customers are voluntarily replacing their private side lead services. Lead services continue to be replaced in areas of local and state road resurfacing projects, and on projects initiated by private or outside entities. The Water Supply Board's own crews replace lead services that are found to be leaking. The replacement work is subject to all of the EPA regulatory notification, testing and reporting requirements.

Since inception of the reporting of the IFR program and the lead service replacement program to the RIPUC (July 1, 1996), The Water Supply Board has replaced 16,894 lead services to the end of fiscal year 2016 (June 30, 2016) at a cost of \$55,870,855.

## **9. DEFINED BENEFIT PENSION PLANS**

Substantially all employees of the Water Supply Board participate in the Employees' Retirement System of the City of Providence (ERS or the Plan), a defined-benefit, single-employer plan. Water Supply Board employees participating in the Plan are eligible to retire at age 55 if hired prior to July 1, 2004, at age 60 if hired between July 1, 2004 and June 30, 2009, at age 62 with 10 years of service if hired on or after July 1, 2009 or at any age after 25 years of service if hired prior to July 1, 1995, or at any age after 30 years of service if hired on or after July 1, 1995. The total retirement allowance is equal to an annuity, which is the actuarial equivalent of accumulated contributions at the time of retirement, plus a pension, which when added together either; 1) equals 1/40 of final compensation for each year of total service up to 20 years and 1/50 of final compensation for each year of service in excess of 20 years if hired prior to July 1, 1996 or; 2) equals 1/50 of final compensation for each year of total service credited if hired on or after July 1, 1996. These benefit provisions and all other requirements are established by City ordinance.

ERS is governed by an Employee Retirement Board provided by the Providence Home Rule Charter. The ERS consists of elected officials, management and employee representation and provides for establishing rules and regulations and is responsible for the administration and operation of the City employee retirement system. The Board has the discretion and authority to interpret the Plan and to determine the eligibility and benefits of participants and beneficiaries pursuant to the provisions of the Plan. On all such matters, the decision of a majority of the then members of the Board shall govern and be binding upon the employer, participants and beneficiaries.

Membership of the ERS plan for the City of Providence consisted of the following at June 30, 2015, the date of the latest actuarial valuation:

Inactive plan members or beneficiaries currently receiving benefits	3,097
Inactive employees entitled to but not yet receiving benefits	432
Active employees	<u>3,012</u>
Total	<u><u>6,541</u></u>

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The Plan's investment policy in regard to the allocation of invested assets is established and may be amended by the City. It is the policy of the City to pursue an investment strategy that reduces risk through the prudent diversification of the portfolio across a broad selection of distinct asset classes. The pension Plan's investment policy discourages the use of cash equivalents, except for liquidity purposes, and aims to refrain from dramatically shifting asset class allocations over short time spans. The following was the asset allocation as of June 30, 2016:

<b>Asset Class</b>	<b>Target Allocation</b>
Domestic equity	39.25%
International developed markets equity	13.25
International emerging markets equity	1.50
Core fixed income	29.00
Hedge fund, GTAA, risk parity	13.00
Private equity	4.00
	<u>100.00%</u>

The total pension liability was determined by an actuarial valuation as of June 30, 2015, using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.50%
Salary increases	3.50% per year, before reflecting increases due to longevity
Investment rate of return	8.25%, net of pension plan investment expense, including inflation

For the year ended June 30, 2016, the annual money-weighted rate of return on pension plan investments, net of pension plan investment expenses, was 2.60%. The money-weighted rate of return expresses investment performance, net of investment expense, adjusted for the changing amounts actually invested.

The long-term expected rate of return on Plan investments was determined using a building block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target allocation as of June 30, 2016 are summarized as follows:

<b>Asset Class</b>	<b>Target Allocation</b>	<b>Long-Term Expected Real Rate of Return</b>	<b>Weighted Real Rate of Return</b>
Domestic equity	39.25%	6.49%	(2.20)%
International developed markets equity	13.25	7.16	(5.50)
International emerging markets equity	1.50	9.46	(5.50)
Core fixed income	29.00	1.68	4.40
Hedge fund, GTAA, Risk parity	13.00	3.60	26.70
Private equity	4.00	11.04	(15.30)
	<u>100.00%</u>		<u>2.60%</u>

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**Contributions**

Class A members and police officers are required to contribute 8% of their salary to the Plan. Class B members, other than police officers, are required to contribute 9.5% of their salary to the Plan. Water Supply Board employees are Class A members. The Mayor and City Council contribute to the Plan at a rate of \$350 per year. Additionally, the City shall contribute from time to time amounts sufficient with the contributions of elected officials to provide the special pensions granted to them. The Water Supply Board's contributions to the ERS for the years ended June 30, 2016, 2015 and 2014 were \$3,615,102, \$3,212,354 and \$2,945,209, respectively.

**Investment Policy**

The City policy for pension investments is under the oversight of the Board of Investment Commissioners (the Board). The Board contracts with an investment advisory firm and approves any new investment vehicles presented by the consultant. The Board follows all applicable state statutes and Section 17-189 of the City Ordinance, which states, "The Board of Investment Commissioners is authorized and empowered to execute the disposition and investment of the funds which are within its control in any securities and investments as would be acquired by prudent persons of discretion and intelligence in these matters, who are seeking a reasonable income and the preservation of their capital.

**Net Pension Liability**

The net pension liability was measured as of June 30, 2016, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date.

The components of the net pension liability of the Retirement System for the Water Supply Board were as follows:

	<b>June 30, 2016</b>	<b>June 30, 2015</b>
Total pension liability	\$ 67,406,877	\$ 60,131,939
Plan fiduciary net position	17,040,995	16,863,406
Net Pension Liability	<u>\$ 50,365,882</u>	<u>\$ 43,268,533</u>
Plan fiduciary net position as a percentage of the total pension liability	25.28%	28.04%



**PROVIDENCE WATER SUPPLY BOARD**  
**(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)**  
**NOTES TO FINANCIAL STATEMENTS**

**Changes in the Net Pension Liability for the Water Supply Board**

	<b>Increase (Decrease)</b>		
	<b>Total Pension Liability (a)</b>	<b>Plan Fiduciary Net Position (b)</b>	<b>Net Pension Liability (a)-(b)</b>
Balances as of June 30, 2015	\$ 60,131,939	\$ 16,863,406	\$ 43,268,533
Changes for the year:			
Service cost	941,053		941,053
Interest on total pension liability	5,130,041		5,130,041
Differences between expected and actual experience	(223,279)		(223,279)
Change from difference in proportionate share	3,875,236	1,086,733	2,788,503
Effect of assumptions changes or inputs	3,083,805		3,083,805
Employer contributions		3,615,102	(3,615,102)
Member contributions		615,760	(615,760)
Net investment income		401,320	(401,320)
Benefit payments, including refund to employee contributions	(5,531,918)	(5,531,918)	-
Administrative expenses		(9,408)	9,408
Net changes	7,274,938	177,589	7,097,349
Balances as of June 30, 2016	\$ 67,406,877	\$ 17,040,995	\$ 50,365,882

**PROVIDENCE WATER SUPPLY BOARD**  
**(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)**  
**NOTES TO FINANCIAL STATEMENTS**

	Increase (Decrease)		
	<b>Total Pension Liability (a)</b>	<b>Plan Fiduciary Net Position (b)</b>	<b>Net Pension Liability (a)-(b)</b>
Balances as of June 30, 2014	\$ 58,311,217	\$ 16,954,283	\$ 41,356,934
Changes for the year:			
Service cost	854,182		854,182
Interest on total pension liability	5,509,989		5,509,989
Differences between expected and actual experience	79,253		79,253
Effect of assumptions changes or inputs	40,391		40,391
Employer contributions		3,212,354	(3,212,354)
Member contributions		1,037,505	(1,037,505)
Net investment income		331,724	(331,724)
Benefit payments, including refund to employee contributions	(4,663,093)	(4,663,093)	-
Administrative expenses		(9,367)	9,367
Net changes	1,820,722	(90,877)	1,911,599
Balances as of June 30, 2015	\$ 60,131,939	\$ 16,863,406	\$ 43,268,533

Additional information as of the latest actuarial valuation follows:

Valuation Date	July 1, 2015
Actuarial cost method	Individual entry age method
Amortization cost method	Approximate level percent of payroll-open
Remaining amortization period	25 years
Asset valuation method	5-year smoothed market value
Actuarial assumptions: Investment rate of return	8.25%
Inflation rate	3.5%
Projected salary increases	3.5% per year before reflecting increases due to longevity compensation
Cost of living adjustments	No COLA for next 8 years, 3% thereafter

Mortality rates were based on the RP-2014 Healthy Annuitant Mortality Table for Males or Females, as appropriate, with no assumed pre-retirement mortality or turnover.

Mortality rates for healthy retirees were based on RP-2014 Employee and Healthy Annuitant Mortality Tables with MP-2014 improvement projections backed out to a base year of 2006 and projected generationally with Scale BB2D, set forward 1-year post-retirement for Class A employees and the RP-2014 Blue Collar Employee and Healthy Annuitant Mortality Tables with MP-2014 improvement projections based out to a base year of 2006 and projected generationally with Scale BB2D, set forward 1-year post-retirement for Class B employees. Disabled retiree mortality rates were based on RP-2014 Blue Collar Healthy Annuitant Mortality Table with MP-2014 improvement projections backed out to a base year of 2006 and projected generationally with Scale BB2D, set forward 3 years.

**PROVIDENCE WATER SUPPLY BOARD**  
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**NOTES TO FINANCIAL STATEMENTS**

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**Discount Rate**

The discount rate used to measure the total pension liability at June 30, 2016 was 8.00%. The projection of cash flows used to determine the discount rate assumed plan member contributions will be made at the current contribution rate and that the City of Providence's contributions will be made at the actuarially determined contribution rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

**Sensitivity of the Net Pension Liability to Changes in the Discount Rate.**

The following presents the net pension liability of the Retirement System, calculated using the discount rate of 8.00%, as well as what the System's net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (7.00%) or 1-percentage-point higher (9.00%) than the current rate at June 30, 2016:

	<u>1% Decrease (7.00%)</u>	<u>Discount (8.00%)</u>	<u>1% Increase (9.00%)</u>
Net pension liability	\$ 57,962,738	\$ 50,365,882	\$ 44,011,621

The following presents the net pension liability of the Retirement System, calculated using the discount rate of 8.25%, as well as what the System's net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (7.25%) or 1-percentage-point higher (9.25%) than the current rate at June 30, 2015:

	<u>1% Decrease (7.25%)</u>	<u>Discount (8.25%)</u>	<u>1% Increase (9.25%)</u>
Net pension liability	\$ 49,571,509	\$ 43,268,533	\$ 37,941,170

**Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions**

For the years ended June 30, 2016 and 2015, the Water Supply Board recognized pension expense of \$5,698,801 and \$3,967,510, respectively.

**PROVIDENCE WATER SUPPLY BOARD**  
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**NOTES TO FINANCIAL STATEMENTS**

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At June 30, 2016, the Water Supply Board reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>
Differences between expected and actual experience	\$ 50,616	\$ 178,623
Changes of assumptions	2,492,840	
Changes in proportion and differences between employer contributions and proportionate share of contributions	2,528,207	
Net difference between projected and actual earning on pension plan investments	<u>1,277,011</u>	
Total	<u>\$ 6,348,674</u>	<u>\$ 178,623</u>

At June 30, 2015, the Water Supply Board reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>
Differences between expected and actual experience	\$ 63,403	\$
Changes of assumptions	32,313	
Net difference between projected and actual earning on pension plan investments	<u>1,060,726</u>	
Total	<u>\$ 1,156,442</u>	<u>\$ -</u>

Amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

**Year Ending June 30:**

2017	\$ 1,622,650
2018	1,622,650
2019	1,622,650
2020	<u>1,302,101</u>
Thereafter	<u>\$ 6,170,051</u>

**Payable to the Plan**

At June 30, 2016, the Water Supply Board had made full payment of the required pension contribution for the year ended June 30, 2016.

**PROVIDENCE WATER SUPPLY BOARD**  
**(AN ENTERPRISE FUND OF THE CITY OF PROVIDENCE, RHODE ISLAND)**  
**NOTES TO FINANCIAL STATEMENTS**

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**10. POST EMPLOYMENT BENEFITS**

The Water Supply Board follows GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*.

The Water Supply Board's Post-Retirement Benefits Program of the City of Providence (the Program) is a defined-benefit, single-employer post-retirement health and life insurance program. The Program provides lifetime health care and life insurance benefits to retired employees and their spouses when retirement was effective prior to 1996. Disclosures about this program, as a whole, are presented in the City of Providence, Rhode Island's basic financial statements. As of June 30, 2016 and 2015, the City recorded a liability for unpaid post-retirement contributions of \$278,037,000 and \$241,723,000, respectively. Separate actuarial information related to the Water Supply Board employees is not available. Accordingly, only disclosures about the Water Supply Board's participation in the Plan are presented herein.

<u>Year Ended June 30,</u>	<u>Annual Required Contribution</u>	<u>Actual Contribution</u>	<u>Percentage Contributed</u>	<u>Net OPEB Obligation</u>
2016	\$ 1,841,000	\$ 678,000	36.8%	\$ 7,858,000
2015	1,774,000	507,000	28.6%	6,671,000
2014	1,755,357	437,598	24.9%	5,385,261

The historical schedules of employer contributions and funding progress for the Program are included in the City of Providence, Rhode Island's basic financial statements.

**11. RECLASSIFICATIONS**

Certain reclassifications have been made to the Water Supply Board's financial statement presentation as of and for the year ended June 30, 2015 to correspond to the current year's format.

**12. SUBSEQUENT EVENTS**

Effective January 1, 2017, the Providence Water Supply Board entered into an agreement to merge with the East Smithfield Water District in Smithfield, Rhode Island. As part of the agreement, the Providence Water Supply Board has agreed to spend no less than \$4 million to upgrade the East Smithfield Water District's infrastructure over a 10-year period.

**PROVIDENCE WATER SUPPLY BOARD**  
**SCHEDULE OF CHANGES IN NET PENSION LIABILITY AND RELATED RATIOS**  
**LAST THREE FISCAL YEARS\***

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Total pension liability:			
Service cost	\$ 941,053	\$ 854,182	\$ 893,162
Interest	5,130,041	5,509,989	4,946,549
Differences between expected and actual experience	(223,279)	79,253	
Change from difference in proportionate share	3,875,236		
Changes of assumptions	3,083,805	40,391	
Benefit payments, including refunds of member contributions	<u>(5,531,918)</u>	<u>(4,663,093)</u>	<u>(4,973,233)</u>
Net change in total pension liability	7,274,938	1,820,722	866,478
Total pension liability - beginning	<u>60,131,939</u>	<u>58,311,217</u>	<u>57,444,739</u>
Total pension liability - ending	<u>67,406,877</u>	<u>60,131,939</u>	<u>58,311,217</u>
Plan fiduciary net position:			
Contributions - employer	3,615,102	3,212,354	2,945,209
Contributions - member	615,760	1,037,505	911,508
Net investment income	401,320	331,724	1,210,438
Change from difference in proportionate share	1,086,733		
Benefit payments, including refunds of member contributions	(5,531,918)	(4,663,093)	(4,973,233)
Administrative expense	<u>(9,408)</u>	<u>(9,367)</u>	<u>(71,955)</u>
Net change in plan fiduciary net position	177,589	(90,877)	21,967
Plan fiduciary net position - beginning	<u>16,863,406</u>	<u>16,954,283</u>	<u>16,932,316</u>
Plan fiduciary net position - ending	<u>17,040,995</u>	<u>16,863,406</u>	<u>16,954,283</u>
Net Pension Liability - Ending	\$ <u>50,365,882</u>	\$ <u>43,268,533</u>	\$ <u>41,356,934</u>
Plan fiduciary net position as a percentage of the total pension liability	25.28%	28.04%	29.08%
Covered-employee payroll	\$ 13,096,208	\$ 12,930,447	\$ 11,900,000
Net pension liability as a percentage of covered-employee payroll	384.58%	334.63%	347.54%

**\*Notes:**

1. The amounts presented for each fiscal year were determined as of a June 30 measurement date prior to the fiscal year end
2. This schedule is intended to show information for 10 years - additional years will be displayed as they become available

**PROVIDENCE WATER SUPPLY BOARD  
SCHEDULE OF EMPLOYER CONTRIBUTIONS  
LAST THREE FISCAL YEARS\***

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Actuarially determined contribution	\$ 3,615,102	\$ 3,212,354	\$ 2,945,209
Contributions in relation to the actuarially determined contribution	<u>3,615,102</u>	<u>3,212,354</u>	<u>2,945,209</u>
Contribution Deficiency (Excess)	\$ <u>-</u>	\$ <u>-</u>	\$ <u>-</u>
Covered-employee payroll	\$ 13,096,208	\$ 12,930,447	\$ 11,900,000
Contributions as a percentage of covered-employee payroll	27.60%	24.84%	24.75%

Notes to Schedule

Valuation date: July 1, 2015  
Measurement date: June 30, 2016  
Actuarially determined contribution rates are calculated as of July 1, two years prior to the end of the fiscal year in which contributions are reported

Methods and assumptions used to determine contribution rates:

Actuarial cost method	Entry Age Normal Cost Method
Amortization method	Level dollar for the 1995 deferral liability and increasing 3.5% per year for the remaining unfunded liability.
Remaining amortization period	25 years remaining as of July 1, 2015 (16 years remaining as of July 1, 2015 for the 1995 deferral).
Asset valuation method	Market value of assets as reported by the City less unrecognized returns in each of the last five years. Unrecognized return is equal to the difference between the actual market return and the expected market return and is recognized over a five-year period, further adjusted, if necessary, to be within 20% of the market value.
Inflation	3.50%
Salary increases	3.5% per year before reflecting increases due to longevity compensation
Investment rate of return	8.25%, net of pension plan investment and administrative expenses, including inflation.
Cost of living adjustments	10-year freeze as of January 1, 2013 and 3% thereafter.
Benefit changes	There have been no changes in benefit provisions since GASB 67/68 implementation.
Assumption changes	The actuarial assumptions used reflect the assumptions proposed in the Experience Investigation for the Five Year Period Ending June 30, 2011 submitted to the Board on April 2, 2012, with the following exception: The retirement rate for Class B participants is 100% at age 60.

\*Note - This schedule is intended to show information for ten years - additional years will be displayed as they become available

**PROVIDENCE WATER SUPPLY BOARD  
SCHEDULE OF INVESTMENT RETURNS  
LAST THREE FISCAL YEARS\***

	<b>2016</b>	<b>2015</b>	<b>2014</b>
Annual money-weighted rate of return, net of investment expense	2.60%	5.56%	14.04%

**\*Notes:**

1. The amounts presented for each fiscal year were determined as of a June 30 measurement date prior to the fiscal year end
2. This schedule is intended to show information for 10 years - additional years will be displayed as they become available





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**Independent Auditors' Report on Internal Control over Financial Reporting and  
on Compliance and Other Matters Based on an Audit of Financial Statements  
Performed in Accordance with *Government Auditing Standards***

To the Board of Directors  
Providence Water Supply Board

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, the financial statements of the Providence Water Supply Board (the Water Supply Board), as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Water Supply Board's basic financial statements, and have issued our report thereon dated December 29, 2016.

**Internal Control over Financial Reporting**

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

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

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

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Water Supply Board's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the Water Supply Board's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Water Supply Board's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Blum, Shapiro & Company, P.C.*

Cranston, Rhode Island  
December 29, 2016