Basic Financial Statements and Report of Independent Certified Public Accountants

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

September 30, 2016

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

FINANCIAL STATEMENTS

For Fiscal Year Ended September 30, 2016

TABLE OF CONTENTS

Grant Thornton

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

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The Honorable Mayor and Members of the City Council
City of Dallas, Texas

Report on the financial statements
We have audited the accompanying statement of net position of the Dallas Water Utilities Fund (the "Fund"), an Enterprise Fund of the City of Dallas, Texas (the "City") as of September 30, 2016, and the related statements of revenues, expenses and changes in fund net position, and cash flows for the year then ended, and the related notes to the financial statements, which collectively comprise the Fund's basic 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.

Auditor's responsibility
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 Fund'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 Fund'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 financial position of the Dallas Water Utilities Fund of the City of Dallas, Texas as of September 30, 2016, and the changes in its financial position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of a matter

As discussed in Note 1, the financial statements present only the Dallas Water Utilities Fund and do not purport to, and do not, present fairly the financial positon of the City of Dallas, Texas, as of September 30, 2016, the changes in its financial position, or, where applicable, its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other matters

Required supplementary information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 10, and the Schedule of Changes in the City's Net Pension Liability and Related Ratios, Schedule of City Contributions to the Pension Plan, Notes to Schedule of City Contributions to the Pension Plan, and Schedule of Funding Progress-Other Postemployment Benefits on pages 48 through 52 be presented to supplement the basic financial statements. Such information, although not a required 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. This required supplementary information is the responsibility of management. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America. These limited procedures 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.

Grant Thornton LLP

Dallas, Texas
May 24, 2017

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)

September 30, 2016

As management of the Dallas Water Utilities ("DWU"), an enterprise fund of the City of Dallas, Texas ("the City"), we offer readers of the financial statements this narrative overview and analysis of the financial activities of the DWU for the fiscal year ended September 30, 2016. The DWU's management's discussion and analysis is designed to: (1) assist the reader in focusing on significant issues; (2) provide an overview of the DWU financial activity; (3) identify changes in the DWU's financial position (its ability to address the next and subsequent year's challenges); and (4) identify issues or concerns. We encourage readers to consider the information presented here in conjunction with the accompanying basic financial statements. All dollar amounts, unless otherwise indicated, are expressed in thousands.

FINANCIAL HIGHLIGHTS

- The assets and deferred outflows of resources of the DWU exceeded its liabilities and deferred inflows of resources at the close of the 2016 fiscal year by $2.47 billion and in the 2015 fiscal year by $2.45 billion (net position). Of this amount, $34.6 million in fiscal year 2016 (unrestricted net position) may be used to meet the DWU on-going obligations to citizens and creditors in accordance with the City's fund designation and fiscal policies.

- The DWU total net position increased by $18.8 million in fiscal year 2016 and increased by $63.6 million in fiscal year 2015. This represents a decrease of $44.8 million in the net increase in net position from 2015 to 2016. Operating revenues increased $34 million, primarily due to increases in customer charges from a 5.3 percent retail rate increase and a 14.2 percent wholesale rate increase. Additionally, personnel services increased by $85.0 million and supplies and other operation and maintenance expenses increased $8.1 million.

- The DWU revenue bonds increased $132.3 million (net of premiums and discounts) from 2015 to 2016. DWU issued $540.3 million in revenue bonds during fiscal year 2016.

OVERVIEW OF THE FINANCIAL STATEMENTS

The DWU basic financial statements comprises three components: 1) management's discussion and analysis; 2) financial statements; and 3) notes to the basic financial statements.

OVERVIEW OF THE FINANCIAL STATEMENTS - Continued

Financial Statements

The financial statements are designed to provide readers with a broad overview of the DWU's finances, in a manner similar to a private-sector business and are made up of the statement of net position, statement of revenues, expenses, and changes in fund net position and statement of cash flows.

These statements are prepared using the economic resources measurement focus and the accrual basis of accounting.

The statement of net position presents information on all of the DWU assets and deferred outflows of resources and liabilities and deferred inflows of resources, with the difference between these reported as net position. The DWU follows the utility method for reporting statement of net position information. Under this method, capital assets appear first, followed by current assets, other noncurrent assets, and deferred outflows of resources. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the DWU is improving or deteriorating. Other non-financial factors should also be taken into consideration, such as changes in the DWU customer base and the condition of the DWU infrastructure (i.e., water and wastewater lines, mains, etc.), to assess the overall health or financial condition of the DWU.

The statement of revenues, expenses, and changes in fund net position presents information showing how the DWU net position changed during the fiscal year. All changes in net position are reported when the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., revenues earned but unbilled and earned but unused compensated absences).

The statement of cash flows reflects changes to the beginning cash and cash equivalent balance. Cash flows are categorized into operating, non-capital financing, capital and related financing, and investing activities.

Notes to the Basic Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes can be found immediately following the financial statements.

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City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)

September 30, 2016

FINANCIAL ANALYSIS

Current assets and other non-current assets (other than capital) increased $14.0 million. Accounts receivable, net of allowance for uncollectible accounts, decreased $6.5 million primarily as a result of improvements to the collection process. Future pipeline reserve capacity rights increased $22.8 million, due to the issuance of $140 million in bonds related to the Water Transmission Facilities Financing Agreement (see Note 5), net of proceeds spent on the construction of the project during fiscal year 2016, in the amount of $117.2 million.

Capital assets, net of depreciation, increased $288.3 million, mainly due to improvements and additions to the water and wastewater system.

Long-term bonds increased $131.1 million, mostly due to the issuance of refunding bonds, offset by debt service payments and related amortizations. Other long-term debt increased $399 million, primarily due to an increase in net pension liability and the water transmission facilities financing agreement.

As of September 30, 2016, unrestricted net position was $34.6 million. This represents 8.6 percent of the total operating expenses, excluding depreciation expense.

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FINANCIAL ANALYSIS - Continued

Table 1
Condensed Statement of Net Position
(In thousands)

	2016	2015
Current and other noncurrent assets	$ 718,132	$ 704,148
Capital assets, net	4,889,043	4,600,703
Deferred outflows of resources	353,518	111,344
Total assets and deferred outflows of resources	5,960,693	5,416,195
Current liabilities	234,054	234,514
Long-term debt	2,771,237	2,556,383
Other long-term liabilities	480,277	171,917
Deferred inflows of resources	6,315	3,341
Total liabilities and deferred inflows of resources	3,491,883	2,966,155
Net position:		
Net investment in capital assets	2,229,460	2,134,907
Restricted	204,714	213,006
Unrestricted	34,636	102,127
Net position	$2,468,810	$2,450,040

The largest portion of the DWU net position reflects its investments in capital assets (e.g., land, building, equipment, improvements, construction in progress, and infrastructure), less any debt used to acquire those assets that is still outstanding. DWU uses these capital assets to provide service to customers; consequently, these assets are not available for future spending. Although DWU investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources since the capital assets themselves cannot be used to liquidate these liabilities.

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FINANCIAL ANALYSIS - Continued

An additional portion of DWU's net position, 8.3 percent, represents resources that are subject to external restrictions such as sinking fund balances which include accrued amounts of principal and interest for debt service purposes, and the reserve fund to be used for any future debt service payments in case the sinking fund is not appropriately funded. The balance of unrestricted net position of $34.6 million may be used to meet ongoing obligations to customers and creditors.

Analysis of DWU Operations

The net position increased $18.8 million during fiscal year 2016, and increased $63.6 million during fiscal year 2015. While DWU had increased revenues related to increases in retail and wholesale rates charged to customers, this was offset by increases in operating expenses. Revenues from sale of water accounted for $367.9 million and revenues from the treatment of wastewater accounted for $239.4 million. Operating revenues increased $34 million in 2016 over 2015, compared to an increase from 2014 to 2015 of $8.8 million. Retail water and wastewater rates increased 5.3 percent and wholesale rates increased 14.2 percent in fiscal year 2016. Capital contributions increased due to increases in amounts spent on construction by outside developers. Operating expenses increased $95.6 million in 2016. Personnel services increased by $85.0 million due mainly to pension expense recognized as a result of the changes in assumptions to measure the net pension liability. This expense reflects the changes in net pension liability and related pension deferred outflows and inflows of resources. Other operation and maintenance expenses increased $8.6 million due to increases in communication, reimbursements to the City general fund, security services, repair and maintenance on equipment, equipment rentals, and legal fees.

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FINANCIAL ANALYSIS - Continued

Table 2
Changes in Fund Net Position
(In thousands)

	2016	2015
Revenues:		
Operating revenues	$ 607,329	$ 573,327
Investment income	4,101	3,995
Gain/(Loss) on property disposal	(61)	40
Total revenues	611,369	577,362
Expenses:		
Personnel services	184,352	99,304
Supplies and materials	106,135	106,558
Other operation and maintenance	113,545	104,995
Depreciation and amortization	115,500	113,036
Interest expense	66,912	75,732
Total expenses	586,444	499,625
Increase in net position before capital contributions and transfers	24,925	77,737
Capital contributions	15,869	7,005
Transfers in from other city funds	739	766
Transfers out to other city funds	(22,763)	(21,936)
Change in net position	18,770	63,572
Beginning net position	2,450,040	2,386,468
Ending net position	$2,468,810	$2,450,040

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

During the current fiscal year, DWU had $4.9 billion invested in a broad range of capital assets net of accumulated depreciation, including water and sewer lines, mains, pump stations, buildings, and vehicles. This amount represents a net increase (including additions, deductions and depreciation) of $288.3 million, or 6.3 percent, over the prior fiscal year. The current fiscal year included project awards related to water and wastewater treatment plant expansion and improvement.

Some of the major projects contributing to this increase include:

- $80.3 million Pipeline Replacement and Pump Station Program;
- $30 million in Improvements at East Side Water Treatment Plant; and
- $37.4 million in improvements to the Central and Southside Wastewater Treatment Plants.

During 2012, the City entered into the Water Transmission Facilities Agreement with the Tarrant Regional Water District (TRWD) to jointly participate in the design, construction, financing, and operation of water transmission facilities capable of delivering additional raw water supply to the Dallas Fort/Worth Metroplex. This will also help to ensure the continued availability of a reliable water supply for their respective customers at the least cost. The TRWD issued bonds to construct the project, $474 million of which are being used to fund the DWU portion of the project. At September 30, 2016, DWU has recorded an intangible asset in progress of $353.8 million, including capitalized interest. The remaining $155.7 million in unspent proceeds held by TRWD were recorded in other noncurrent assets.

Water supply is now available to the City from six surface water impoundments and from water in the Elm Fork of the Trinity River. The City has obtained most of its water supply through contractual agreements with surface reservoir operating entities. DWU provides treated water to its customers within the City on a "retail" basis. Treated and untreated water is provided on a "wholesale" basis to other cities and governmental entities outside of Dallas. A small portion of the City's wastewater is treated by the Trinity River Authority.

Debt

At year-end, DWU had $2.3 billion in revenue bonds (including premiums) outstanding. This represents a 6.2 percent increase from fiscal year 2015.

The DWU share of pension obligation bonds was $71.5 million (including premium of $21.6 million) plus $28.1 million of accreted interest.

CAPITAL ASSETS AND DEBT ADMINISTRATION – Continued

In July 2016, DWU issued Waterworks and Sewer System Revenue Refunding Bonds Series 2016A and 2016B of $540.3 million with an interest rate range of 0.6 percent to 5 percent and a final maturity of October 1, 2045. The bonds were issued to refund previously issued waterworks and sewer system bonds and to refund outstanding commercial paper used by DWU to fund capital construction projects.

The DWU Waterworks and Sewer System Revenue Refunding and Improvement Bonds' underlying ratings are Aa1 by Moody's Investors Service, AAA by Standard & Poor's, and AA+ with Fitch. See Note 5 for additional information.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

Retail water and wastewater rates were increased 2.6 percent in the fiscal year 2017 budget. With the multitude of water challenges across Texas, the City will continue to focus on maintaining infrastructure, conserving resources, and providing for future needs through replacement of aged water and wastewater mains, improve reliability, water quality, and increased capacity at water treatment plants, continue water conservation efforts, and the TRWD integrated pipeline project to connect Lake Palestine to Dallas' water supply system to meet future needs. In order to achieve these goals, it was necessary to implement a water rate increase.

On November 8, 2016, City of Dallas voters approved changes to the Employees' Retirement Fund (ERF) for employees hired on or after January 1, 2017. The changes included a reduction in the benefit multiplier from 2.75 percent to 2.5 percent; an increase in the normal retirement age from 60 to 65; an actuarially reduced benefit for retirees under age 65 whose age plus years of service equal 80; an increase in service retirement from 30 to 40 years; and elimination of the health benefit supplement. On May 9, 2017, the ERF board of trustees also voted to decrease the interest rate used for certain economic assumptions. The effect of these changes will be reflected in the DWU basic financial statements for the fiscal year ending September 30, 2017.

CONTACTING THE DALLAS WATER UTILITIES FINANCIAL MANAGEMENT

The financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the DWU finances and to demonstrate accountability for the money it receives. If you have questions about this report or need any additional financial information, contact the City Controller's Office, at City of Dallas, 1500 Marilla, Room 2BS, Dallas, Texas 75201.

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

STATEMENT OF NET POSITION

As of September 30, 2016
(in thousands)

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES

CAPITAL ASSETS	
Completed utility plant	$ 5,888,586
Less accumulated depreciation and amortization	(2,064,984)
Total completed utility plant, net	3,823,602
Land	100,987
Construction in progress	964,454
Total capital assets	4,889,043
CURRENT ASSETS	
Cash and cash equivalents	173,400
Accounts receivable, less allowance for uncollectible accounts ($8,244)	65,389
Interest receivable	637
Inventories, at cost	13,595
Due from other city funds	268
Prepaid assets	9,975
Other assets	123
Restricted assets	
Customer assessment receivable	625
Debt service	
Cash and cash equivalents	139,595
Held for construction purposes	
Pooled cash and cash equivalents	27,032
Customer deposits	
Pooled cash and cash equivalents	16,083
Total current assets	446,722
OTHER NONCURRENT ASSETS	
Future pipeline reserve capacity rights	155,720
Notes receivable from other city funds	6,251
Restricted assets	
Cash and cash equivalents held by escrow agent for future debt service	6,143
Cash and cash equivalents for future debt service	13,342
Investments for future debt service	89,954
Total other noncurrent assets	271,410
Total assets	5,607,175
DEFERRED OUTFLOWS OF RESOURCES	
Deferred loss on refunding	72,109
Deferred outflows of resources related to pensions	281,409
Total deferred outflows of resources	353,518
Total assets and deferred outflows of resources	$ 5,960,693

See accompanying notes to basic financial statements.

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

STATEMENT OF NET POSITION - CONTINUED

September 30, 2016
(in thousands)

LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION

LIABILITIES	
Long-term debt, less current maturities:	
Revenue bonds payable	$2,178,079
Commercial paper notes payable	48,322
Water transmission facilities financing agreement, payable from restricted assets	446,795
Pension obligation bonds payable	69,985
Accreted interest pension obligation bonds	28,056
Total long-term debt	2,771,237
Current liabilities payable from restricted assets	
Water transmission facilities financing agreement	9,025
Construction accounts payable	59,135
Revenue bonds	100,980
Accrued interest payable	38,177
Total current liabilities (payable from restricted assets)	207,317
Current liabilities payable from current assets	
Accrued payroll payable	1,101
Accounts payable	18,729
Compensated absences payable	5,140
Pension obligation bonds payable	1,543
Accrued interest pension obligation bonds	224
Total current liabilities (payable from current assets)	26,737
Other long-term liabilities	
Customer deposits, payable from restricted assets	16,469
Compensated absences payable	6,179
Net pension liability	427,999
Other postemployment benefits	28,453
Customer and developer construction advances	1,177
Total other long-term liabilities	480,277
Total liabilities	3,485,568
DEFERRED INFLOWS OF RESOURCES	
Deferred inflows of resources related to pension	6,315
Total liabilities and deferred inflows of resources	3,491,883
NET POSITION	
Net investment in capital assets	2,229,460
Restricted:	
Revenue bond requirements	204,714
Unrestricted	34,636
Total net position	$2,468,810

See accompanying notes to basic financial statements.

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION

For the Year ended September 30, 2016
(in thousands)

Operating revenues:	
Water	$ 367,892
Wastewater	239,437
Total operating revenues	607,329
Operating expenses:	
Personnel services	184,352
Supplies and materials	106,135
Other operation and maintenance	113,545
Depreciation and amortization	115,500
Total operating expenses	519,532
Operating income	87,797
Non-operating income (expense)	
Investment income	4,101
Interest expense on bonds and commercial paper	(66,912)
(Loss) on property disposal	(61)
Total non-operating income (expenses)	(62,872)
Income before capital contributions and transfers	24,925
Capital contributions	15,869
Transfers in from other city funds	739
Transfers out to other city funds	(22,763)
Change in net position	18,770
Net position, beginning of year	2,450,040
Net position, end of year	$2,468,810

See accompanying notes to basic financial statements.

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

STATEMENT OF CASH FLOWS

For the Year ended September 30, 2016
(in thousands)

Cash flows from operating activities:	
Cash received from customers	$ 615,424
Cash payments to suppliers for goods and services	(105,435)
Cash payments to employees for services	(92,900)
Cash payments for contractual services	(114,211)
Net cash provided by operating activities	302,878
Cash flows from non-capital financing activities:	
Principal paid on pension obligation bonds	(1,512)
Interest paid pension obligation bonds	(4,707)
Transfers from other funds	873
Transfers to other funds	(22,763)
Net cash used in non-capital financing activities	(28,109)
Cash flows from capital and related financing activities:	
Acquisition and construction of capital assets	(275,638)
Proceeds from obligation for revenue bonds	622,786
Payment to refunded bond escrow agent	(366,097)
Principal paid on revenue bonds	(96,675)
Principal paid on notes payable and other obligations	(6,403)
Interest paid on bonds, notes and other obligations	(117,932)
Proceeds from sale of commercial paper notes	180,004
Retirement of commercial paper notes	(222,140)
Net cash used in capital and related financing activities	(282,095)
Cash flows from investing activities:	
Purchase of investments	(80,000)
Maturity of investments	80,000
Investment income	4,466
Net cash provided by investing activities	4,466
Net decrease in cash and cash equivalents	(2,860)
Cash and cash equivalents, beginning of year	378,455
Cash and cash equivalents, end of year	$ 375,595

See accompanying notes to basic financial statements.

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

STATEMENT OF CASH FLOWS - CONTINUED

For the Year ended September 30, 2016
(In thousands)

Reconciliation of operating income to net cash provided by operating activities:	
Operating income	$ 87,797
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation and amortization	115,500
Change in assets and liabilities	
Decrease in accounts and other receivables	7,603
Decrease in customer assessments receivable	22
Decrease in inventories	677
Increase in deferred outflows for pension contributions	(216,924)
Increase in accounts payable	23
Increase in accrued payroll	750
Decrease in compensated absences	(42)
Decrease in allowance for doubtful accounts	(1,151)
Increase in customer deposits	1,621
Increase in other postemployment benefits	950
Decrease in customer construction and developer advances	(666)
Increase in net pension liability	306,718
Total adjustments	215,081
Net cash provided by operating activities	$ 302,878
Current Assets:	
Pooled cash and cash equivalents	$ 173,400
Pooled cash and cash equivalents for current debt service	139,595
Held for construction purposes pooled cash and cash equivalents	27,032
Customer deposits pooled cash and cash equivalents	16,083
Cash and cash equivalents held by escrow agent for future debt service	6,143
Pooled cash and cash equivalents for future debt service	13,342
Total cash and cash equivalents end of year	$ 375,595
Noncash investing, capital, and financing activities:	
Capital contributions	$ 15,869
Change in fair value of non-pooled investments	(421)
Premium/discount amortization	28,426
Accretion on capital appreciation bonds	4,005
Amortization of deferred gain/loss on refunding	6,574
Capital assets acquired through water transmission financing agreement	117,211
Decrease in future pipeline reserve capacity rights	(117,211)

See accompanying notes to basic financial statements.

NOTE 1 - FINANCIAL STATEMENT PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements include only Dallas Water Utilities (DWU), an enterprise fund of the City of Dallas, Texas (the City). The DWU financial statements are not intended to present the financial position or results of operations of the City. The City also administers other departments, whose operations are reflected in the Comprehensive Annual Financial Report of the City. However, certain disclosures are for the City as a whole, since such information is not available for the fund on a separate fund basis (see Notes 2, 8, 10, 11, 12 and 13).

DWU provides water and wastewater services to customers within the City and to other nearby cities and governmental entities. Chapter XI, Section 14 of the Dallas City Charter requires all costs of service to be paid from revenues arising from customer service rates. This City Charter section also establishes that all customer receipts and revenues shall be used only to provide water and wastewater services, and to provide for any charges made by the City in lieu of ad valorem taxes or that would be due the City if the Water Utilities Department were not a city-owned public utility.

Basis of Accounting

The accounting policies of DWU, as reflected in the accompanying accrual-basis financial statements, conform to accounting principles generally accepted in the United States of America (GAAP) for local government enterprises as prescribed by the Governmental Accounting Standards Board (GASB). The DWU is accounted for using the economic resources measurement focus. Revenues are recognized when earned and expenses are recognized when a liability is incurred, regardless of the timing of related cash flow.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting year. Actual results could differ from those estimates.

Cash, Deposits and Investments

In accordance with City policies, DWU participates in the City's pooled cash and investment program which is administered by the City Controller's Office. A significant portion of cash and investments held by the City is pooled. The pooled cash and investment program of the City is operated under the provisions of City ordinance and a specific City investment policy. The policy states that the City shall invest cash balances over the anticipated amount needed to meet operating requirements. Investments are stated at fair value. The balance reported as "Pooled Cash and Cash Equivalents" represents the equity of the Fund in the pooled cash and investments of the City. The Fund's share of the interest earnings of the pooled investments is determined by allocating interest to each of the participating funds based on average daily balances.

Cash includes amounts in demand deposits as well as short-term investments with original maturities of three months or less. DWU's portion of the City's investment pool is displayed on the statement of net position as cash and cash equivalents. DWU treats pooled investments and short-term non-pooled investments as cash equivalents. Long-term pooled investments are reported as investments on the statement of net position. Investments in U.S. government obligations and other investments are recorded at fair value based on quoted market prices (Note 2).

NOTE 1 - FINANCIAL STATEMENT PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES - Continued

Capital Assets

Capital assets include property, plant, equipment and improvements/infrastructure assets. Generally, equipment with an individual cost of at least $5 thousand, infrastructure with a cost of at least $25 thousand and buildings with a cost of at least $50 thousand and an estimated useful life of more than one year, are capitalized. Purchased or constructed capital assets are stated at cost or at estimated historical cost if original cost is not available. Assets acquired by donation are recorded at acquisition value on the date received.

Depreciation and amortization are provided using the straight-line method over estimated useful lives as shown below, stated in the number of years by property.

Infrastructure and rights to water supply	50 to 100
Reservoirs and water rights	100
Buildings	10 to 50
Improvements other than buildings	10 to 100
Equipment	3 to 25
Utility property	33 to 75

For constructed property, capitalized costs include amounts applicable to construction for payroll, payroll-related costs, and general and administrative overhead.

Maintenance and repairs are charged to operations as incurred. Improvements which extend the useful lives of capital assets are capitalized. Interest costs during construction are capitalized. The accompanying financial statements reflect capitalization of interest costs of $32.2 million.

Transactions with Other City Departments

Operating revenues include billings and charges to other City departments for water and wastewater services, for which other departments made payments of $6.7 million during fiscal year 2016. Operating expenses include payments to other City departments of $108.7 million in 2016, including health benefit payments for employees, office supplies, vehicle fuel and maintenance, communications and data services, programming and batch processing, street rental and other miscellaneous city services. DWU also reimburses other City departments for other construction-related costs paid by those departments for DWU. Current assets and other non-current assets at September 30, 2016 include advances of $6.3 million due from other City funds bearing original interest at rates of 1.5 percent to 4.3 percent, subject to change based on interest received on City investments. All other nonreciprocal transactions between funds which are not reimbursements and where the funds do not receive equivalent goods and services for the transactions are classified as transfers (i.e. payments in lieu of taxes).

NOTE 1 - FINANCIAL STATEMENT PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES - Continued

Compensated Absences

The City's employees earn vacation up to maximum periods based on length of service. Employees may either take vacation leave or receive cash payment upon retirement or termination. Sick leave accrues to employees based on hours worked, up to an unused maximum accrual, but is subject to specified reduction if paid in cash upon retirement or termination. The City accrues vacation and sick leave attributable to employee services already rendered, in amounts of estimated payments. A liability is recorded for accumulated sick leave that is likely to vest, to the extent of probable payment upon termination for employees with 20 or more years of continuous service.

Accounts Receivable

Accounts receivable includes billed and unbilled customer receivables at September 30, 2016. Unbilled receivables include estimated revenues for water and wastewater services provided and yet to be billed at September 30, 2016.

Inventory

Inventory consists of construction and operating materials, which are valued at average cost and is recorded as an expense when consumed.

Prepaid Items

Prepaid items are payments made to vendors for services that will benefit periods beyond September 30, 2016. Prepaid items are recorded using the consumption method.

Operating Revenues and Expenses

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of DWU are derived from treatment and supply of water, and collection of wastewater. Operating expenses for proprietary funds include the cost of services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Restricted vs. Unrestricted

Restricted assets include debt service, investments for future debt service, cash held for construction purposes and customer deposits. Unrestricted assets can be used for any allowable purpose. When both restricted and unrestricted resources are available for use, it is the City's policy to use the restricted resources first and then unrestricted resources as they are needed.

NOTE 1 - FINANCIAL STATEMENT PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES - Continued

Deferred Outflows/Inflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period and will not be recognized as an outflow of resources (expense/expenditure) until then. DWU has the following items that qualify for reporting in this category.

- Deferred charges on refunding – A deferred charge on refunding results from the difference in the carrying value of refunded debt and its reacquisition price. The amount is deferred and amortized over the shorter of the life of the refunded or refunding debt.
- Pension contributions after measurement date – The pension contributions made from the measurement date of the pension plan to the current fiscal year end are deferred and will be recognized in the subsequent fiscal year.
- Difference in projected and actual earnings on pension assets, difference between estimated and actual experience and changes in assumptions – These are amortized as a component of pension expense over a closed period equal to the average of the expected remaining service lives of all employees that are provided with pensions through the pension plan (active employees and inactive employees) determined as of the beginning of the measurement period.

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and will not be recognized as an inflow of resources (revenue) until that time. DWU has one item that qualifies as deferred inflows of resources as a result of pension activity. A deferred inflow of resources is recorded in the statement of net position for the difference in projected and actual experience in the actuarial measurement of the total pension liability not recognized in the current year. The difference is amortized over the average remaining service life of all participants in the respective pension plans and recorded as a component of pension expense beginning with the period in which they are incurred.

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NOTE 1 - FINANCIAL STATEMENT PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES - Continued

New Accounting Pronouncements

During fiscal year 2016, DWU adopted the following Governmental Accounting Standard Board (GASB) Statements:

GASB Statement No. 72, Fair Value Measurement and Application, was implemented by the City as required by GASB during fiscal year ending September 30, 2016. The objective of this statement is to address accounting and financial reporting issues related to fair value measurements. The definition of fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. The implementation of this statement did not result in any changes to DWU's financial statements; however, changes were made to the note disclosures in Note 2, Cash, Deposits and Investments.

GASB Statement No. 76, "The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments", was implemented as required by GASB during the fiscal year ending September 30, 2016. The Statement supersedes Statement No. 55, The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments. This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. The implementation of this statement did not result in any changes to the financial statements.

GASB Statement No. 79, "Certain External Investment Pools and Pool Participants", was implemented by the City as required by GASB during fiscal year ending September 30, 2016. This Statement establishes additional note disclosure requirements for qualifying external investment pools that measure all of their investments at amortized cost for financial reporting purposes and for governments that participate in those pools. Those disclosures for both the qualifying external investments pools and their participants include information about any limitations or restrictions on participant withdrawals. The implementation of this statement did not result in any changes to DWU's financial statements; however, changes were made to the note disclosures in Note 2, Cash, Deposits and Investments.

The GASB has issued the following statements which will be effective in future years as described below:

GASB Statement No. 73, "Accounting and Financial Reporting for Pensions and Related Assets That Are Not Within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68", will be implemented as required by GASB during the fiscal year ending September 30, 2017. This statement establishes requirements for defined benefit pensions that are not within the scope of Statement No. 68, "Accounting and Financial Reporting for Pensions", as well as for the assets accumulated for purposes of providing those pensions. In addition, it establishes requirements for defined contribution pensions that are not within the scope of Statement 68. It also amends certain provisions of Statement No. 67, "Financial Reporting for Pension Plans", and Statement No. 68 for pension plans and pensions that are within their respective scopes. DWU is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

NOTE 1 - FINANCIAL STATEMENT PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES - Continued

GASB Statement No. 74, "Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans", will be implemented as required by GASB during the fiscal year ending September 30, 2017. The Statement replaces Statements No. 43, "Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, as amended", and No. 57, "OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans". It also includes requirements for defined contribution OPEB plans that replace the requirements for those OPEB plans in Statement No. 25, "Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans, as amended", Statement No. 43, and Statement No. 50, Pension Disclosures. DWU is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

GASB Statement No. 75, "Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions", will be implemented as required by GASB during the fiscal year ending September 30, 2018. This Statement replaces the requirements of Statements No. 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, as amended", and No. 57, OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans, for OPEB plans. DWU is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

GASB Statement No. 77, "Tax Abatement Disclosures", will be implemented as required by GASB during the fiscal year ending September 30, 2017. This Statement requires governments that enter into tax abatement agreements to disclose the following information about the agreements:

- Brief descriptive information, such as the tax being abated, the authority under which tax abatements are provided, eligibility criteria, the mechanism by which taxes are abated, provisions for recapturing abated taxes, and the types of commitments made by tax abatements recipients,
- The gross dollar amount of taxes abated during the period, and
- Commitments made by a government, other than to abate taxes, as part of a tax abatement agreement.

DWU is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

GASB Statement No. 78, "Pensions Provided Through Certain Multiple-Employer Defined Benefit Pension Plans", will be implemented as required by GASB during the fiscal year ending September 30, 2017. This Statement amends the scope and applicability of Statement 68 to exclude pensions provided to employees of state or local governmental employers through a cost-sharing multiple-employer defined benefit pension plan that (1) is not a state or local governmental pension plan, (2) is used to provide defined benefit pensions both to employees of state or local governmental employers and to employees of employers that are not state or local governmental employers, and (3) has no predominant state or local governmental employer (either individually or collectively with other state or local governmental employers that provide pensions through the pension plan). This Statement establishes requirements for recognition and measurement of pension expense, expenditures, and liabilities; note disclosures; and required supplementary information for pensions that have the characteristics described above. The implementation of this statement is not expected to result in any changes to the financial statements.

NOTE 1 - FINANCIAL STATEMENT PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES - Continued

GASB Statement No. 80, "Blending Requirements for Certain Component Unit – An Amendment of GASB Statement No. 14, will be implemented by the City as required by GASB during fiscal year ending September 30, 2017. This Statement amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of Statement No 39, "Determining Whether Certain Organization are Component Units". DWU is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

GASB Statement No. 81, "Irrevocable Split-Interest Agreements," will be implemented by the City as required by GASB during fiscal year ending September 30, 2018. The objective of this statement is to improve accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. DWU is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

GASB Statement No. 82, "Pension Issues", will be implemented as required by GASB during the fiscal year ending September 30, 2017. This Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. DWU is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

GASB Statement No. 83, "Certain Asset Retirement Obligations", will be implemented as required by GASB during the fiscal year ending September 30, 2019. This Statement establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. DWU is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

GASB Statement No. 84, "Fiduciary Activities", will be implemented as required by GASB during the fiscal year ending September 30, 2020. This Statement improves guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. DWU is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

GASB Statement No. 85, "Omnibus 2017", will be implemented as required by GASB during the fiscal year ending September 30, 2018. This Statement addresses several different accounting and financial reporting issues identified by GASB during the implementation and application of certain GASB pronouncements. DWU is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

NOTE 1 - FINANCIAL STATEMENT PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES - Continued

GASB Statement No. 86, "Certain Debt Extinguishment Issues", will be implemented as required by GASB during the fiscal year ending September 30, 2018. This statement improves consistency in accounting and financial reporting for in-substance defeasance of debt. This statement also improves accounting and financial reporting for prepaid insurance on debt that is extinguished and notes to the financial statements for debt that is defeased in substance. The City is currently evaluating potential changes to the financial statements as a result of the implementation of this statement.

NOTE 2 - CASH, DEPOSITS, AND INVESTMENTS

A summary of the carrying amount of cash on hand, deposits, and investments at September 30, 2016 is as follows:

	Cash and Pooled Investments with City Treasury
Deposits	$ 34,219
Investments – cash equivalents	341,376
Investments – restricted	89,954
Total	$465,549

DWU categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of an asset. Level 1 inputs are quoted prices in active markets for identical assets, Level 2 inputs are significant other observable inputs, and Level 3 inputs are significant unobservable inputs.

NOTE 2 - CASH, DEPOSITS, AND INVESTMENTS - Continued

At September 30, 2016, the investments held for the DWU General and Investment Pool Programs are as follows:

		Fair Value Measurement Using	
	Total	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Investments by Fair Value Level			
Federal Agricultural Mortgage Corp. Notes	$ 48,537	$ -	$ 48,537
Federal Agricultural Mortgage Corp. Notes Callable	1,284	-	1,284
Federal Farm Credit Bank Notes	61,042	-	61,042
Federal Home Loan Bank Notes	26,791	-	26,791
Federal Home Loan Bank Notes Callable	23,202	-	23,202
Federal Home Loan Mortgage Corp. Notes	68,723	-	68,723
Federal Home Loan Mortgage Corp. Notes Callable	41,473	-	41,473
Federal National Mortgage Association Notes	18,198	-	18,198
Federal National Mortgage Association Notes Callable	69,843	-	69,843
Total Investments by Fair Value Level	$359,093	$ -	$359,093
Investments Measured at the Net Asset Value (NAV)			
Money Market Funds			
Blackrock Fed Fund Money Market Fund	11,333		
Blackrock T-Fund Money Market Fund	6		
Morgan Stanley Government Money Market Fund	9		
First American Government Obligation Money Market Fund	6,143		
Total Money Market Funds	17,491		
Local Government Investment Pools			
LOGIC – Local Government Investment Pool	49,396		
TexPool – Local Government Investment Pool	4		
TexPool Prime – Local Government Investment Pool	4,491		
TexStar – Local Government Investment Pool	855		
Total Local Government Investment Pools	54,746		
Total Investments Measured at Net Asset Value	72,237		
Total Investments	$431,330		

NOTE 2 - CASH, DEPOSITS, AND INVESTMENTS - Continued

The City invests in TexSTAR, TexPool, TexPool Prime, and LOGIC, which are Local Government Investment Pools (LGIP) created under the Interlocal Cooperation Act, Texas Government Code Chapter 791 and the Public Funds Investment Act, Texas Government Code Chapter 2256. These two acts provide for the creation of LGIP's and authorize eligible governmental entities to invest their public funds and funds under their control through the investment pools. The LGIP's follow all requirements of the Public Funds Investment Act, including being rated by a nationally recognized rating agency, and seek to maintain a net asset value of $1.00 per unit.

J.P. Morgan Investment Management Inc. and First Southwest Company serve as co-administrators for the TexSTAR and LOGIC programs under agreements with each pool's respective board of directors. The TexSTAR governing board is a five-member Board consisting of three representatives of employees, officers, or elected officials of participating government entities and one member designated by each of the co-administrators. In addition, TexSTAR has an Advisory Board composed of participants in the pool and other persons who do not have a business relationship with the pool and are qualified to advise the pool. The governing body of LOGIC is a five-member board of directors comprised of employees, officers or elected officials of participating government entities or individuals who do not have a business relationship with LOGIC and are qualified to advise the pool. A maximum of two advisory board members represent the co-administrators of LOGIC.

The Comptroller of Public Accounts for the State of Texas is the sole officer, director, and shareholder of the Texas Treasury Safekeeping Trust Company, which is authorized to operate TexPool and TexPool Prime. Pursuant to the TexPool Participation Agreement, administrative and investment services to the TexPool Portfolios are provided by Federated Investors, Inc., under an agreement with the State Comptroller, acting on behalf of the Trust Company. In addition, TexPool has an Advisory Board composed equally of participants in the TexPool Portfolios and other persons who do not have a business relationship with the TexPool Portfolios who are qualified to advise the TexPool Portfolios.

Deposit and Investment Risk Disclosures of Funds with the City Treasurer

GASB Statement No. 40, "Deposit and Investment Risk Disclosures," requires disclosure information related to common risks inherent in deposit and investment transactions. Investments are subject to certain types of risks, including custodial credit risk, concentration of credit risk, credit risk, interest rate risk and foreign currency risk. Exposure of deposited funds and investment risk are disclosed in the following sections of this note.

Custodial Credit Risk

Custodial credit is the risk that, in event of the failure of the counterparty, the City will not be able to recover the value of its deposit or collateral securities that are in the possession of an outside party. As of September 30, 2016, $34,219 was fully collateralized and insured by U.S. Federal Agency securities and the Federal Deposit Insurance Corporation. The collateral pledged to the City is held in the City's name at the Bank of New York Mellon. The FDIC insures demand accounts up to $250 thousand in the aggregate. At September 30, 2016, all deposits were either insured or collateralized.

NOTE 2 - CASH, DEPOSITS, AND INVESTMENTS - Continued

Texas statutes and City policy authorize operating, capital projects, bond reserve and trust monies to be deposited in demand deposits, time deposits, or certificates of deposits. Texas statues and City policy require all uninsured collected deposits to be fully collateralized.

Concentration of Credit Risk

Investments that individually represent 5 percent or more of net portfolio assets are stated below. Investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds and external investment pools are excluded.

Agency and Securities by Issuer	Fair value	% of Total Portfolio
Federal National Mortgage Assoc. (FNMA)	$ 88,041	20.41%
Federal Agricultural Mortgage Corp. (FAMC)	49,821	11.55%
Federal Home Loan Mortgage Corp. (FHLMC)	110,196	25.55%
Federal Home Loan Bank (FHLB)	49,993	11.59%
Federal Farm Credit Bank (FFCB)	61,042	14.15%
Total agency securities	$359,093	83.25%

Credit Risk

The Public Funds Investment Act requires that investments shall be made in accordance with written policies approved at least annually by the governing body. Investment policies must address safety of principal, liquidity and yield, with primary emphasis on safety of principal. In accordance with this Policy, the City may invest in direct or guaranteed obligations of the U.S. Treasury, certain U.S. agencies and instrumentalities, and direct obligations of states and local governments with a credit rating no less than Aa3 or its equivalent; fully collateralized certificates of deposit and repurchase agreements; no-load money market mutual funds and local government investment pools with credit ratings no less than Aaa or its equivalent.

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Money Market Mutual Funds and Local Government Investment pools in the City's portfolio are rated AAAm by Standard and Poor's and/or Aaa by Moody's. U.S. Treasury Notes and Bills are obligations of the U.S. government and are not considered to have credit risk and thus are not rated (NR). Long-term bond ratings are used for the U.S. Government Agencies. Ratings for the City's portfolio are listed on the following table.

Security Type	Fair value	% of Total portfolio	S&P/Moody's ratings
Money market mutual funds and investment pools	$ 72,237	16.75%	AAAm/Aaa
U.S. Agency securities	359,093	83.25%	AA+/Aaa
Total portfolio	$431,330	100.00%	

NOTE 2 - CASH, DEPOSITS, AND INVESTMENTS - Continued

Interest Rate Risk

In order to ensure the ability of the City to meet obligations and to minimize potential liquidation losses, the dollar-weighted average stated maturity of the Investment Pool shall not exceed 1.5 years. The weighted average maturity of the securities held in the City's portfolio is as follows:

Security type	Fair value	Weighted average maturity (days)
Money market mutual funds and investment pools	$ 72,237	1
U.S. Agency securities	359,093	531
Total portfolio	$431,330	432

NOTE 3 - ASSETS RESTRICTED FOR DEBT SERVICE

Bond documents authorizing issuance of water and wastewater system revenue bonds and the related offering documents prescribe the timing and determination of amounts to be accumulated and maintained for debt service. These ordinances require that amounts be set aside in advance to provide for the next scheduled principal and interest payments. Such amounts are reflected in the accompanying statement of net position as current maturities of revenue bonds and accrued revenue bond interest. The ordinances also require that a "revenue bond reserve fund" be accumulated and maintained. If the reserve fund contains less than the future average annual principal and interest requirements of all outstanding revenue bonds, determined after each bond issue, the ordinances require equal monthly additions to the reserve fund in amounts which, after 60 months, will result in a reserve fund balance which is equal to the future average annual principal and interest requirements. At September 30, 2016, the reserve fund was in compliance with the ordinance requirements.

NOTE 4 - CAPITAL ASSETS

Capital asset activity for the year ended September 30, 2016 is as follows:

	Balance, beginning of year	Additions	Transfers and Retirements	Balance, end of year
Capital assets, not being depreciated:				
Land	$ 94,338	$ 6,649	$ -	$ 100,987
Construction in progress	683,872	375,524	(94,942)	964,454
Total capital assets, not being depreciated	778,210	382,173	(94,942)	1,065,441
Capital assets, being depreciated:				
Water rights	353,910	-	-	353,910
Buildings	525,039	-	-	525,039
Improvements other than buildings	80,068	-	-	80,068
Infrastructure	579,419	285	-	579,704
Equipment	547,168	14,474	(1,419)	560,223
Utility property	3,687,968	101,909	(235)	3,789,642
Total capital assets, being depreciated	5,773,572	116,668	(1,654)	5,888,586
Less accumulated depreciation for:				
Water rights	(112,803)	(4,112)	-	(116,915)
Buildings	(207,270)	(11,017)	-	(218,287)
Improvements other than buildings	(16,121)	(2,273)	-	(18,394)
Infrastructure	(231,735)*	(10,835)	-	(242,570)
Equipment	(384,943)	(13,058)	1,420	(396,581)
Utility property	(998,207)*	(74,205)	175	(1,072,237)
Total accumulated depreciation	(1,951,079)	(115,500)	1,595	(2,064,984)
Total capital assets being depreciated, net	3,822,493	1,168	(59)	3,823,602
Total capital assets, net	$ 4,600,703	$ 383,341	$(95,001)	$ 4,889,043

* Accumulated depreciation in the amount of $7,349 has been reclassified between infrastructure and utility property assets.

NOTE 5 - LONG TERM DEBT

Water and wastewater system revenue bonds constitute obligations of the DWU, secured solely by a pledge of all revenues of the City's water and wastewater system (operated as "Dallas Water Utilities"), after deduction of reasonable operation and maintenance expenses. All DWU revenue bonds may be redeemed at the City's option, at par value, on or after the tenth annual serial maturity date.

DWU is also obligated to pay a proportionate share of the Pension Obligation Bonds issued by the City of Dallas.

Revenue bonds payable at September 30, 2016 include the following issues. Future long term liabilities and interest rates shown on the following page are for bonds outstanding on September 30, 2016.

	Beginning Balance	Additions	Deletions	Ending Balance	Due Within One year
Dallas Water Utilities					
City of Dallas Waterworks and Sewer					
System Revenue Refunding and Improvement Bonds					
Series 2006	$ 19,710	$ -	$ 14,130	$ 5,580	$ 5,580
Series 2007	314,080	-	231,245	82,835	43,905
Series 2008	33,290	-	22,450	10,840	3,435
Series 2009A	11,125	-	9,342	1,783	700
Series 2009B	7,385	-	460	6,925	465
Series 2009C	79,403	-	5,120	74,283	5,145
Series 2010	215,015	-	88,750	126,265	6,755
Series 2011	224,495	-	54,050	170,445	11,495
Series 2012	349,040	-	31,720	317,320	15,090
Series 2013	153,975	-	2,655	151,320	2,795
Series 2015	604,260	-	2,850	601,410	3,085
Series 2016	-	540,345	-	540,345	2,530
Total Revenue Bonds Payable	2,011,778	540,345	462,772	2,089,351	100,980
Add: Unamortized Premium	135,023	82,441	27,756	189,708	-
Total Revenue Bonds for Water Utilities	2,146,801	622,786	490,528	2,279,059	100,980
Pension Obligation Bonds	51,443	-	1,512	49,931	1,543
Add: Net Premium/Discount	22,267	-	670	21,597	-
Add: Accretion on Capital Appreciation Bonds	26,961	4,005	2,910	28,056	-
Total Water Utilities Bonds	2,247,472	626,791	495,620	2,378,643	102,523
Other Liabilities					
Commercial Paper Notes Payable	90,458	180,004	222,140	48,322	-
Compensated Absences Payable	11,361	6,160	6,202	11,319	5,140
Other Postemployment Benefits	27,503	2,518	1,568	28,453	-
Net Pension Liability	121,281	373,856	67,138	427,999	-
Other: Water Transmission Facilities Financing Agreement	322,223	140,000	6,403	455,820	9,025
Total Long-Term Debt for Water Utilities	$2,820,298	$1,328,374	$798,116	$3,350,556	$116,688

NOTE 5 - LONG TERM DEBT - Continued

In June 2016, Dallas Water Utilities issued Waterworks and Sewer System Revenue Refunding Bonds Series 2016 of $540.3 million with an interest rate range of 0.60 percent to 5.00 percent and a final maturity of October 1, 2045. The bonds were issued to refund previously issued waterworks and sewer system bonds and to refund outstanding commercial paper used by Dallas Water Utilities to fund capital construction projects. Proceeds of $398.6 million were deposited with an escrow agent to be used to pay the outstanding amount of the refunded bonds. As a result, $357.4 million of these bonds are considered defeased and the liability for the refunded portion of these bonds has been removed from the financial statements. The refunding resulted in a difference of $28.8 million between the net carrying amount of the old debt and the reacquisition price. This difference, reported in the accompanying financial statement as a deferred outflow of resources, is being amortized to interest expense over the life of the old bonds. Total debt service payments decreased by $36.2 million as a result of the refunding. The City also incurred an economic gain (difference between the present value of the old debt and new debt service payments) of $31.1 million.

At September 30, 2016, and during the year then ended, the City believes it was in compliance with the financial covenants of all authorizing ordinances for outstanding water and wastewater system revenue debt.

The pension obligation bonds are allocated between the City's governmental and enterprise funds. The numbers presented below include the Fund's portion of the total issue. Of the total issue, 18.78 percent is allocated to DWU. The City-issued pension obligation bonds are to be paid through increased contributions to the pension debt service account.

DWU's pension obligation bonds outstanding as of September 30, 2016 are as follows:

	Maturity	Rates	Amount
Series 600	2035	3.24% to 5.19%	$22,323
Series 601	2035	4.10% to 5.48%	13,310
Series 632	2024	0.295% to 4.66%	14,298
Total outstanding			$49,931

Pension Obligation Bonds are paid through increased contributions to the City's Debt service fund. Operating revenues from DWU operations and interest earned on the cash balance in the City's debt service fund are pledged for repayment of the debt. Revenues are transferred from DWU to the City's debt service fund to meet annual principal and interest obligations.

NOTE 5 - LONG TERM DEBT - Continued

The future principal and interest requirements of revenue bonds and pension obligation bonds attributed to DWU are shown on the table below:

	Dallas Water Utilities					
Fiscal	Revenue Bonds			Pension Obligation Bonds		
Year	Principal	Interest	Total	Principal	Interest	Total
2017	$ 100,980	$ 79,705	$ 180,685	$ 1,543	$ 4,806	$ 6,349
2018	94,855	81,240	176,095	1,678	4,863	6,541
2019	99,013	77,936	176,949	1,622	5,117	6,739
2020	98,080	74,961	173,041	1,610	5,322	6,932
2021	101,350	71,690	173,040	5,559	1,575	7,134
2022-2026	445,740	305,700	751,440	23,038	16,990	40,028
2027-2031	366,518	223,706	590,224	7,547	40,028	47,575
2032-2036	370,890	140,814	511,704	7,334	36,194	43,528
2037-2041	288,245	60,010	348,255	-	-	-
2042-2046	123,680	11,052	134,732	-	-	-
	2,089,351	$1,126,814	$3,216,165	$49,931	$114,895	$164,826

Dallas Water Obligation for Water Transmission Facilities Financing Agreement

Tarrant Regional Water District (TRWD), a water control and improvement district and political subdivision of the State of Texas, issued Water Facilities Contract Revenue Bonds in February 2012 in the amount of $131.9 million, in January 2014 in the amount of $202.1 million, and in December 2015 in the amount of $140 million. The bonds were issued to finance the DWU share of costs for designing, acquiring, constructing, improving, repairing, rehabilitating, and/or replacing water transmission facilities capable of delivering additional raw water supply to the respective customers of the DWU and TRWD (the Project). The Project is tentatively scheduled to be completed in 2025. The City's share of the total cost of the Project is estimated to be $977.5 million. Upon completion of the Project, DWU will have reserved capacity rights in the amount of 150 million gallons per day. Depending on the timing of construction, additional bonds are expected to be issued throughout the construction period.

In order to ensure adequate funding from DWU for the payment of principal and interest, the City entered into a separate funding agreement with TRWD, a Water Transmission Facilities Financing Agreement (the Agreement). Under this Agreement, the City is obligated to make payments to TRWD for the principal and interest amounts associated with the bonds. The Agreement establishes through State statutes that those payments will be treated as operating and maintenance expenses. This interpretation of the treatment of payments to TRWD as operating and maintenance expenses is only being applied to the schedule of revenue bond coverage for the DWU and for purposes of establishing rates.

NOTE 5 - LONG TERM DEBT – Continued

The Agreement establishes that TRWD shall own and operate the Project, subject to Dallas' reserved capacity rights in the Project. The bonds are a special obligation of TRWD. Principal and interest are secured by and payable solely from payments to be received by TRWD from the City to the extent required and provided in the Agreement. The bonds do not constitute a debt or pledge of the faith and credit of the City and accordingly have not been reported in the accompanying financial statements. At September 30, 2016, the TRWD Water Facilities Contract Revenue Bonds outstanding were $456.6 million.

The City has determined the obligation under the Agreement to be a liability to the extent that such obligations are for the payment of bonds issued to fund the DWU share of costs for the Project. The City has capitalized the development of an intangible asset, Pipeline Reserved Capacity Rights, in Construction in Progress for the actual Project costs incurred by TRWD. The unspent proceeds held by TRWD for future construction costs have been recorded in Other Noncurrent Assets – Future Pipeline Reserved Capacity Rights. The interest rates for the obligation range from 0.45 percent to 6.00 percent. The obligation will be amortized over a period of 30 years. The balance of the obligation for the Agreement was $455.8 million at September 30, 2016.

The schedule of principal and interest payments required for the obligation is provided below:

Fiscal Year	Principal	Interest	Total
2017	$ 9,025	$ 16,718	$ 25,743
2018	10,095	17,874	27,969
2019	10,370	17,488	27,858
2020	10,660	17,081	27,741
2021	10,955	16,653	27,608
2022-2026	60,540	76,221	136,761
2027-2031	73,095	64,457	137,552
2032-2036	89,690	49,201	138,891
2037-2041	111,265	28,762	140,027
2042-2045	70,125	5,849	75,974
	$455,820	$310,304	$766,124

NOTE 5 - LONG TERM DEBT - Continued

Commercial Paper Notes Payable

The commercial paper notes Series D are supported by two liquidity agreements through two banks. The liquidity agreement supporting the Sub-Series D-1 and Sub-Series D-2 notes are through State Street Bank and Trust Company and Bank of America N.A., and extend to January 8, 2018. The Sub-Series D-1 notes have an aggregate available principal amount not to exceed $241.6 million, which includes $225 million of principal together with approximately $16.6 million of accrued interest for a maximum maturity date not to exceed 270 days at a rate of 10 percent per annum. The Sub-Series D-2 notes have an aggregate available principal amount not to exceed $80.5 million, which includes $75 million of principal together with approximately $5.5 million of accrued interest for a maximum maturity date not to exceed 270 days at a rate of 10 percent per annum. The commercial paper program constitutes an obligation subordinate to the Dallas Water Utility revenue bonds. Any advances made by credit providers for payments of commercial paper under the line of credit are secured by water and wastewater pledge revenues. During fiscal year 2016, $180 million was issued and $222.1 million was repaid. Upon maturity, the notes will be remarketed by the commercial paper dealers or extinguished with long-term debt.

Defeasance of Debt

In current and prior years, DWU legally defeased certain revenue bonds by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments of the refunded bonds. Accordingly, the trust accounts and the defeased bonds are not included in DWU's basic financial statements.

As of September 30, 2016 DWU had a total of $771 million defeased outstanding water and sewer revenue bonds. The following is a schedule of defeased bonds during the fiscal year:

	September 30, 2015	Additions	Deletions	September 30, 2016
Water and Sewer Revenue Bonds	$535,440	$357,445	$121,965	$770,920

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NOTE 6 - OTHER LONG-TERM OBLIGATIONS

Other long-term obligations are as follows as of September 30, 2016:

	Balance, beginning of year	Additions	Deletions	Balance, end of year
Customer deposits, payable from restricted assets	$14,848	$3,201	$1,580	$16,469
Customer and developer construction advances	1,843	3,222	3,888	1,177
Total other long-term obligations	$16,691	$6,423	$5,468	$17,646

NOTE 7 - COMMITMENTS

At September 30, 2016, commitments under construction contracts in progress and operating encumbrances were outstanding in the following amounts:

Construction encumbrances	$433,605
Operating encumbrances	4,563
	$438,168

For purposes of its water supply system, the City is contractually committed to pay a portion of the net operating and maintenance expenses of several reservoirs operated by other governmental agencies or authorities. The City is also contractually committed to pay a portion of the net operating and maintenance expenses of the Trinity River Authority's Regional Wastewater System (the "Authority"). The contract with the Authority provides in effect that amounts of capital obligation, interest, and operation and maintenance expenses vary with Dallas' proportionate share of total wastewater treated by the Authority's Central Regional Wastewater System.

NOTE 8 - CONTINGENCIES

Pending Lawsuits and Claims

Various claims and lawsuits are pending against the City and its officers and employees acting in their official capacities (hereafter collectively "City" for purposes of Note 11). Those lawsuits and claims, excluding condemnation proceedings, which are considered "probable" and estimable are accrued as a liability, while those claims and judgments, excluding condemnation proceedings, which are considered "reasonably possible" are disclosed but not accrued.

NOTE 8 - CONTINGENCIES - Continued

In the opinion of the City Attorney, the potential loss resulting from all material pending lawsuits and claims, excluding condemnation proceedings, which are considered reasonably possible and estimable, is approximately $15.6 million as of September 30, 2016. Additionally, the City is a defendant in six lawsuits filed by past and current police and fire-rescue officers and on-behalf of future police and fire-rescue officers, alleging that current and past police and fire pay schedules were adopted in violation of a referendum approved by the voters in 1979. One of these lawsuits is scheduled for trial in December 2017. The City is currently unable to predict the ultimate outcome of these lawsuits; however, if the City were to receive an unfavorable outcome, the City would likely look to other avenues of resolution, including appropriate appeals. As such, the City cannot reasonably estimate the amount of liability, if any, that might result from these lawsuits, as well as the timing of any liability, at this time.

At September 30, 2016, approximately $10.5 million has been accrued as a liability in the risk funds for pending material claims and lawsuits, excluding condemnation proceedings, considered to be probable. In the opinion of the City Attorney, this is the total amount of all such pending claims and lawsuits which represent probable loss to the City.

Gain Contingency

On October 1, 1981, the City of Dallas purchased water supply rights for Lake Fork, a water source owned and operated by the Sabine River Authority (Authority), for approximately $117 million. Lake Fork is located on Lake Fork Creek, a tributary of the Sabine River, in Wood, Hopkins and Rains Counties, approximately 70 miles east of the City of Dallas. Financial obligations of the City's share of Lake Fork water supply rights were fully paid as of December 2004. The City now has a contract with the Authority for 74 percent of the water available from Lake Fork.

The City is required to pay the Authority for a pro rata share of the operation and maintenance costs associated with Lake Fork, which was approximately $3.8 million in the fiscal year ended September 30, 2016. The pro rata share of the operation and maintenance costs owed to the Authority for the renewal of the Lake Fork contract was to be mutually negotiated with the Authority pursuant to the terms of the contract. Negotiation attempts with the Authority failed and in October 2014, the Authority unilaterally established a rate which would require the City to pay approximately an additional $24 million annually for the water to which it is entitled. The City has challenged the rate by filing petitions with the Public Utilities Commission of Texas (PUC) and district courts in Travis and Orange counties in Texas. The PUC has ordered an administrative law judge to consider setting an interim rate while this dispute is pending.

On April 2, 2015, the administrative law judge ruled that the interim rate must be paid by the City of Dallas until the rate case is resolved. The rate was set by the Authority on a take-or-pay basis, without a cost escalator. This interim rate was retroactive to November 2, 2014. The amounts the City pays in accordance with the interim rate are expensed and deposited into an interest-bearing escrow account, established by the Authority, pending the final outcome of the rate case.

NOTE 9 - LEASES NOTE

As Lessee

As lessee, DWU is committed under various leases for building and office space, data processing and communications equipment. These leases are considered for accounting purposes to be operating leases.

Year ending September 30	Rental Payments
2017	$1,199
2018	408
Total	$1,607

As Lessor

As lessor DWU is also under several lease agreements whereby it receives revenues from leasing land, building and water front facilities. These revenue leases are considered for accounting purposes as operating leases.

Year ending September 30	Rental Receipts
2017	$ 57
2018	46
2019	46
2020	46
2021	43
2022-2025	208
2027-2031	208
Minimum future rentals	$654

NOTE 10 - PENSION PLAN

Plan Description

Employees' Retirement Fund (ERF): All full-time DWU employees participate in the contributory City Employees' Retirement Fund, a defined benefit, single employer pension plan ("the Plan"). The legal authority for this plan is Chapter 40A of the Dallas City Code. The fund is for the benefit of all eligible employees of the City, excluding firefighters and police officers. The fund is administered by a seven member board of trustees consisting of three persons appointed by the City Council who may be council members, three employees from different departments of the City who are elected by members of the retirement fund and who are members of the retirement fund, and the City Auditor. The ERF issues a stand-alone financial report which is available at: www.dallaserf.org/Publications.html.

NOTE 10 - PENSION PLAN - Continued

Benefits Provided

ERF provides retirement, disability, and death benefits to its members in accordance with Chapter 40A of the Dallas City Code. All employees of the City are members except police officers, firefighters, elected officers, non-salaried appointee members of boards or commissions, part-time employees working less than one-half time, temporary employees, individuals working under contract, and individuals whose salaries are paid in part by another government agency.

Members have vested rights to retirement benefits after five years of service or to survivor benefits after two years of service. Benefits are based on credited service and the average monthly earnings for the three highest paid calendar years. Members of the fund are entitled to normal retirement pension at age 60; early retirement pension at age 55 if employed prior to May 9, 1972 or age 50 and years of service total 78; service retirement pension at any age after 30 years of credited service and disability retirement pension as determined by the board of trustees. Cost of living adjustments for retirees are made each year on January 1 by adjusting the pension base by the percentage change of the consumer price index, not to exceed 5 percent.

Amendments to Chapter 40A of the Dallas City Code, other than provisions required to comply with federal law, may only be made by a proposal initiated by either the board of trustees of the ERF or the City Council which results in an ordinance approved by the board, adopted by the City Council, and approved by a majority of the voters voting at a general or special election.

Employees covered by benefit terms

At December 31, 2015, the following numbers of employees were covered by the benefit terms:

Membership data at December 31, 2015

	ERF
Retirees and beneficiaries currently receiving benefits	6,756
Inactive members entitled to benefits but not yet receiving them	1,163
Current members	7,477
Total	15,396

Contributions

ERF: Chapter 40A of the Dallas City Code establishes contribution requirements. Changes to the contribution formula may only be made by a proposal initiated by either the board of trustees of the ERF or the City Council which results in an ordinance approved by the board, adopted by the City Council, and approved by a majority of the voters voting at a general or special election.

NOTE 10 - PENSION PLAN - Continued

The City contributes 63 percent of the required contribution and the membership contributes 37 percent. The City's contribution rate covers both the debt service tied to the pension obligation bonds and the contributions to the Employees' Retirement Fund. Although the total contribution is actuarially determined each year, it is adjusted based on the following requirements of Chapter 40A: (1) the maximum contribution percentage of covered wages is 36 percent; (2) the maximum increase or decrease from one year to the next is 10 percent; and (3) the contribution rate changes only if the actuarial valuation develops a rate which differs from the prior rate by more than 300 basis points. The adjusted contribution as a result of Chapter 40A is the Current Adjusted Total Obligation Rate (CATOR). Contribution rates are 13.32 percent of covered wages for employees and 22.68 percent for the City for the City's fiscal year ended September 30, 2016. The City's contribution of 22.68 percent is divided into 13.83 percent cash to the Plan and 8.85 percent for debt service payments on the pension obligation bonds. For 2016, the City contribution was $55.2 million.

Actuarial Assumptions

The total ERF pension liabilities in the December 31, 2015 actuarial valuations were determined using the following actuarial assumptions for the plan, applied to all periods included in the measurement:

	ERF
Inflation	3%
Salary Increases	3.50% to 7.00%, including inflation
Investment Rate of Return	8.00%
Mortality	**For actives:** Males - RP2000 Healthy Mortality Table for male employees, set forward 4 years. Females - RP2000 Healthy Mortality Table for female employees, set back 5 years. **For healthy retirees:** Males - RP2000 Blue Collar Mortality Table for male annuitants, with a 109% multiplier and fully generational mortality using improvement Scale BB. Females - RP2000 Blue Collar Mortality Table for female annuitants, with a 103% multiplier and fully generational mortality using improvement Scale BB. **For all disabled lives:** RP2000 Disabled Mortality Table for male annuitants, set forward one year.
Cost of Living Adjustments	3.00%
Long-term expected rate of return	Estimated using a building block methodology in which best-estimate ranges of expected future real rates of return are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real return rates by the target asset allocation percentage and by adding expected inflation.

NOTE 10 - PENSION PLAN - Continued

The target allocation and best estimates of arithmetic real rates of return (RROR) for the plan, by major asset class, are summarized in the following table:

	ERF	
Asset Class	Target Allocations	Long-term RROR
Domestic Equity	15.0%	6.50%
International equity	15.0%	6.50%
Global equity	5.0%	6.70%
Low volatility global equity	10.0%	6.70%
Private equity	15.0%	9.50%
REITS	5.0%	5.00%
Real assets	5.0%	6.40%
Investment grade fixed	12.5%	3.50%
High yield fixed income	15.0%	6.35%
Credit opportunities	2.5%	6.35%
Total	100.0%	

Discount Rate

ERF: The discount rate used to measure the total pension liability was 5.76 percent. In order to develop the blended discount rate of 5.76 percent, the actuarial assumed rate of return of 8.00 percent was used during the period that the plan was projected to have a fiduciary net position, and a municipal bond rate of 3.57 percent was used during the period that the plan was projected to have no fiduciary net position. The 3.57 percent is based on the Municipal Bond 20-year High Grade Rate Index as of December 31, 2015. The projection of cash flows used to determine the discount rate assumed that that (1) plan member contributions and City contributions will be made at the projected future contribution rates outlined in Chapter 40A of the Dallas City Code, under which employees contribute 37 percent of the CATOR; the City contributes 63 percent of the CATOR, reduced by the amount required to pay current debt service on the 2005 pension obligation bonds; (2) the ERF annually earns 8.00 percent on its market value of assets; and (3) the number of active members remains constant in the future. Based on those assumptions, the ERF fiduciary net position was not projected to be available to make all projected future benefit payments of current active and inactive employees.

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NOTE 10 - PENSION PLAN - Continued

Changes in the Net Pension Liability

The following table shows the net pension liability as of December 31, 2015:

	Increase (Decrease)		
	Total Pension Liability	Plan Fiduciary Net Position	Net Pension Liability
Employees' Retirement Fund			
Balances at December 31, 2014	$4,004,055	$3,398,485	$ 605,570
Changes for the year:			
Service cost	78,020	-	78,020
Interest	313,850	-	313,850
Changes of assumptions	1,238,431	-	1,238,431
Differences between expected and actual experience	(26,829)	-	(26,829)
Contributions - City	-	50,721	(50,721)
Contributions - Employee	-	50,742	(50,742)
Net investment income	-	(53,344)	53,344
Benefit payments, including refunds of employee contributions	(239,960)	(239,960)	-
Administrative expense	-	(4,598)	4,598
Other changes	-	162	(162)
Net changes	1,363,512	(196,277)	1,559,789
Balances at December 31, 2015	$5,367,567	$3,202,208	$2,165,359

The amount of net pension liability allocated to DWU was $427,999.

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NOTE 10 - PENSION PLAN - Continued

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

The following table presents the net pension liability of the City, calculated using the discount rates of 5.76 percent for ERF, as well as what the City's net pension liability would be if it were calculated using discount rates that are 1-percentage-point lower (4.76 percent) or 1-percentage-point higher (6.76 percent) than the current rates:

	1% Decrease	Current Discount Rate	1% Increase
ERF	$ 2,915,146	$ 2,165,359	$ 1,547,749

Pension Plan Fiduciary Net Position

Detailed information about the fiduciary net position of the pension plan is available in the separately issued financial reports.

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

For the fiscal year ended September 30, 2016, DWU recognized pension expense of $100,359 for ERF. At September 30, 2016, the City also reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	ERF	
	Deferred Outflows	Deferred Inflows
Differences between expected and actual experience	$ -	$31,804
Changes of assumptions	1,093,697	-
Net difference between project and actual earnings on pension plan investments	292,252	-
Contributions subsequent to the measurement date	41,613	-
	$1,427,562	$31,804

NOTE 10 - PENSION PLAN - Continued

Deferred outflows of resources in the amount of $41,613 related to pension contributions in the ERF made subsequent to the measurement date will be recognized as a reduction of the net pension liability during the fiscal year ended September 30, 2016. Deferred outflows and inflows of resources in the amount of $1,354,145 related to the pension will be recognized in pension expense as follows:

Year Ending December 31:

2016	$430,966
2017	430,966
2018	375,997
2019	116,216

The amount of deferred outflows of resources related to pensions allocated to DWU was $281,409. The amount of deferred inflows of resources related to pensions allocated to DWU was $6,315.

NOTE 11 - RISK MANAGEMENT - ESTIMATED CLAIMS AND JUDGEMENT PAYABLE

The City is self-insured for all third-party general liability claims. Claims adjusting services are provided by the City's internal staff. Interfund premiums are based primarily upon the insured fund's claims experience and exposure and are reported as cost reimbursement inter-fund transactions. The amount paid by DWU was $681 thousand in fiscal year 2016. The liability for unpaid claims includes the effects of specific incremental claims, adjustment expenses and if probable material, salvage and subrogation.

All known City property, primarily buildings and contents, is insured through commercial insurance policies, subject to a $1 million deductible per loss occurrence. The amount of settlements exceeded the deductible loss per occurrence during fiscal year 2014.

The City is self-insured for workers' compensation claims that occurred prior to October 1, 1999. Effective February 1, 2013, the City is insured for workers' compensation losses in excess of $1 million per occurrence. Claims adjusting services are provided by an independent "administrative services" contractor. Workers' compensation premiums are based primarily upon the insured funds' claims experience and exposure and are reported as cost reimbursement interfund transactions. The amount paid by DWU was $800 thousand in fiscal year 2016.

All workers' compensation losses are accumulated in a clearing fund which is being reimbursed by the premiums collected. When losses exceed premiums, the deficiencies are prorated and supplemented by the various applicable funds. Accrued worker's compensation liability consists of incurred but not reported as well as unpaid reported claims of which $35.4 million at September 30, 2016, is recorded in the risk funds of the City. Of this amount, $6.5 million is estimated to be payable in the next fiscal year.

The City maintains a group health insurance plan for employees and dependents which is self-insured by the City. The City also offers enrollment in one health maintenance organization as an alternative. Premiums are determined based on the annual budget. DWU expensed $8.8 million in fiscal year 2016.

NOTE 11 - RISK MANAGEMENT - ESTIMATED CLAIMS AND JUDGEMENT PAYABLE - Continued

The City also maintains a group life insurance plan, which offers term-life and accidental death and dismemberment benefits for employees and dependents. The City is fully insured for employee term-life. Health claims and claims incurred but not reported that are probable and reasonably estimated are accrued at September 30, 2016, in the amount of $7.2 million in the risk funds.

At September 30, 2016, the City estimates its general liability at $20.4 million, which includes $9.9 million for automobile and general liability and $10.5 million for probable claims and lawsuits (see Note 8). Of this amount, $7.5 million is estimated to be payable in the next fiscal year.

Changes in the balances of claims liabilities during the past fiscal year are as follows:

	Workers' Compensation		Health		General Liability	
	2016	2015	2016	2015	2016	2015
Unpaid claims, beginning of year	$37,015	$40,200	$ 6,713	$ 5,733	$17,330	$16,408
Incurred claims, including incurred but not reported claims (IBNRs) and changes in estimates	8,950	4,937	70,021	71,048	7,923	6,360
Claim payments	(8,611)	(7,185)	(75,422)	(71,417)	(4,455)	(5,942)
Changes to prior year estimates (IBNR)	(1,938)	(937)	5,871	1,349	(350)	504
Unpaid claims, end of year	$35,416	$37,015	$ 7,183	$ 6,713	$20,448	$17,330

NOTE 12 - OTHER POST-EMPLOYMENT BENEFITS

In addition to pension benefits, the City provides certain healthcare and life insurance benefits for retired employees through various Council resolutions. Employees who are permanent, full-time employees are eligible to participate in the benefits at retirement. The City is self-insured for these programs. The City eliminated subsidization of the plan for individuals hired on or after January 1, 2010.

For retired employees hired before January 1, 2010, the City pays on average $249 (not in thousands) per month. For pre-Medicare retirees who qualify and choose the City health plan, the City pays approximately 50 percent of the actuarial cost and the retiree pays the other 50 percent. Spouses of retirees, like active employees, pay 100 percent of premiums. There were 5,163 retired participants and surviving spouses in the health plan at September 30, 2016, the latest data used for this evaluation. Post-Medicare retirees are offered the active plans but must pay the full cost of coverage; alternatively, they are also offered several Medicare supplement plans along with a Medicare Part D prescription drug plan. The City subsidizes the Medicare supplement plans for the retirees but does not subsidize the dependent cost.

NOTE 12 - OTHER POST-EMPLOYMENT BENEFITS - Continued

The City's annual other postemployment benefit (OPEB) cost is calculated based on the annual required contribution (ARC), an amount actuarially determined in accordance with GASB Statement No. 45. The actuarial cost method used in this valuation to determine the actuarial accrued liability and the ARC is the projected unit credit method with service prorated. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years. The City has elected to amortize the unfunded actuarial liability over 30 years as a level percentage of payroll on an open basis. The discount rate used for the determination of the expense for fiscal year 2016 is 4 percent. The annual healthcare trend rates range from 8 percent to 4.5 percent per year. Total claim payments for fiscal year 2016 were approximately $15.5 million net of participants' contributions.

Actuarial Valuations

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the City are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the City and plan members) and include the types of benefits provided at the time of each valuation. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities, consistent with the long-term perspective of the calculations.

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NOTE 12 - OTHER POST-EMPLOYMENT BENEFITS - Continued

The following table shows the components of the City's annual OPEB cost for fiscal year 2016, the amount actually contributed to the plan, and changes in the City's net OPEB obligation (in thousands):

Actuarial required contribution	$ 25,687
Interest on net OPEB obligation	9,663
Adjustment to annual required contributions	(9,230)
Annual OPEB	26,120
Contributions made	(15,453)
Increase in net OPEB	10,667
Net OPEB Obligation, beginning of year	241,533
Net OPEB Obligation, end of year	$252,200

Net OPEB obligation reported by governmental funds	$194,008
Net OPEB obligation reported by business type activities funds	48,957
Net OPEB obligation reported by internal service funds	9,235
Net OPEB obligation, end of year	$252,200

The DWU's share of the OPEB Obligation is $28,453.

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for fiscal years 2016, 2015 and 2014 are as follows (in thousands):

Fiscal Year Ended	Net OPEB Obligation Beginning of Year	Annual OPEB Cost	Employer Contributions	Net OPEB Obligation End of Year	Percentage of Annual OPEB Cost Contributed
2016	$241,533	$26,120	$15,453	$252,200	59.16%
2015	229,486	26,465	14,418	241,533	54.48%
2014	207,462	36,295	14,271	229,486	39.32%

As of September 30 2016, the funded status was as follows:

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	Percentage of Covered Payroll
9/30/2016	$ -	$492,867	$492,867	0.00%	$ 850,011	57.98%

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NOTE 12 - OTHER POST-EMPLOYMENT BENEFITS - Continued

The actuarial accrued liability of $492,867 includes $287,711 for active employees and $205,156 for retirees.

	Uniformed	Non-Uniformed	Total
At September 30, 2016, membership was as follows:			
Active participants not eligible to retire	1,555	2,622	4,177
Active participants eligible to retire	1,801	881	2,682
Total active participants	3,356	3,503	6,859

NOTE 13 - DEFERRED COMPENSATION PLANS

There are three deferred compensation plans. Two of these plans are voluntary for City employees who participate in the City's pension plans. The third plan is mandatory for all employees and council members who are not covered by the City's pension plans. These plans comply with sections 401(k) and 457(b) of the Internal Revenue Code. Participants in the City's voluntary 457(b) and 401(k) plans have full discretion to choose investments from a list of standard plan options, a linked brokerage account, and a commingled pool managed by Fidelity Management Trust Company. The list of standard plan options includes mutual funds with varying styles and levels of investment risk. All the account balances in the mandatory 457 plan are invested in the same commingled pool. All contributions to these plans are deferred by plan participants from their compensation and all the earnings are allocated to each participant's account. Distributions from all the deferred compensation plans are available after termination of employment. Additionally, participants in the City's voluntary plans may also take out loans and may receive hardship withdrawals in accordance with federal regulations. The assets held in these plans are not included in the City's or the DWU financial statements and cannot be used for purposes other than the exclusive benefit of the participants or their beneficiaries or to pay the reasonable expenses of plan administration.

NOTE 14 - INTERFUND TRANSFERS

During the year, transfers out to other City funds were made in the amount of $22.8 million for payment in lieu of taxes (PILOT) and other miscellaneous transfers which are recorded as transfers-out, rather than operation and maintenance expenses, due to the nonreciprocal nature of the transactions. Under the terms of the bond ordinance, any PILOT payments and any other similar payments are not considered expenses of operation and maintenance of the fund. Additionally, they are not included in the debt coverage calculation. During the year, transfers in from other City funds were made in the amount of $739 thousand for debt service reimbursements related to software acquisition and assets constructed by other funds of the City for the DWU.

NOTE 15 - SUBSEQUENT EVENTS

A. Issuance of Debt

From October 1, 2016 through May 24, 2017, the City issued $107.2 million in Dallas Water Utilities commercial paper notes, with an average interest rate of 0.9 percent.

B. Changes to retirement benefits and assumptions

On November 8, 2016, City of Dallas voters approved changes to the Employees' Retirement Fund for employees hired on or after January 1, 2017. The changes included a reduction in the benefit multiplier from 2.75 percent to 2.5 percent; an increase in the normal retirement age from 60 to 65; an actuarially reduced benefit for retirees under age 65 whose age plus years of service equal 80; an increase in service retirement from 30 to 40 years; and elimination of the health benefit supplement. On May 9, 2017, the ERF board of trustees also voted to decrease the interest rate used for certain economic assumptions.

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Changes in the City's Net Pension Liability and Related Ratios

Last Two Fiscal Years
(Dollar amounts in thousands)

	ERF	
	2016	**2015**
Total Pension Liability		
Service cost	$ 78,020	$ 62,065
Interest	313,850	290,948
Changes of assumptions	1,238,431	292,137
Differences between expected and actual experience	(26,829)	(21,967)
Plan changes	-	-
Benefit payments, including refunds	(239,960)	(230,243)
Net change	1,363,512	392,940
Total Pension Liability, Beginning	4,004,055	3,611,115
Total Pension Liability, Ending [(a)]	$ 5,367,567	$ 4,004,055
Plan Fiduciary Net Position		
Contributions - City	$ 50,721	$ 45,833
Contributions - Employee	50,742	46,536
Net investment income	(53,344)	207,992
Benefit payments, including refunds	(239,960)	(230,243)
Administrative expense	(4,598)	(4,150)
Other changes	162	157
Net change	(196,277)	66,125
Plan Fiduciary Net Position, Beginning	3,398,485	3,332,360
Plan Fiduciary Net Position, Ending [(b)]	$ 3,202,208	$ 3,398,485
City's Net Pension Liability [(a) - (b)]	$ 2,165,359	$ 605,570
Plan Fiduciary Net Position as a percentage of Total Pension Liability	60%	85%
Covered-employee payroll	$ 393,186	$ 353,650
City's Net Pension Liability as a percentage of covered-employee payroll	551%	171%

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of City Contributions to the Pension Plan

Last Ten Fiscal Years
(Dollar amounts in thousands)

	2016	2015	2014
Employees Retirement Fund			
Actuarially determined contribution	$ 81,838	$ 68,100	$ 62,756
Contributions in relation to the actuarially determined contribution	$ 53,896	$ 49,135	$ 44,816
Contribution deficiency (excess)	$ 27,942	$ 18,965	$ 17,940
Covered-employee payroll	$ 389,706	$ 377,381	$ 357,887
Contributions as a percentage of covered-employee payroll	14%	13%	13%

2013	2012	2011	2010	2009	2008	2007
$ 54,289	$ 37,822	$ 32,865	$ 34,793	$ 18,995	$ 15,904	$ 18,121
$ 35,515	$ 28,917	$ 27,303	$ 27,668	$ 24,604	$ 22,893	$ 23,310
$ 18,774	$ 8,905	$ 5,562	$ 7,125	$ (5,609)	$ (6,989)	$ (5,189)
$ 336,483	$ 317,551	$ 318,408	$ 345,819	$ 374,395	$ 370,537	$ 347,868
11%	9%	9%	8%	7%	6%	7%

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

REQUIRED SUPPLEMENTARY INFORMATION
Notes to the Schedule of City Contributions to the Pension Plan

Last 10 Fiscal Years

Employees Retirement Fund

Valuation date	12/31/15	12/31/14	12/31/13	12/31/12	12/31/11	12/31/10	12/31/09	12/31/08	12/31/07	12/31/06
Timing	The actuarially determined contribution rate is effective October 1 after the valuation date.									
Actuarial cost method	Entry age normal.									
Amortization method	30-year open amortization period level percentage of payroll. The City ordinance authorizing the plan specfies that the rate may not change from year-to-year if the calculated rate is less than 300 basis points different from the current rate.									
Asset valuation method	5-year smoothed market value of assets.							3-year smoothed market value of assets.		
Inflation	3%									
Salary increases	3.5% to 7%, including inflation									
Discount rate	8.00%		8.25%							
Cost of Living Adjustment	The greater of (a) the percentage of change in the price index for October of the current year over October of the previous year, up to 5%, or (b) the percentage of annual average change in the price index for the 12-month period ending with the effective date of the adjustment, up to 5%.									
Mortality	**For actives:** Males - RP2000 Healthy Mortality Table for male employees, set forward 4 years. Females - RP2000 Healthy Mortality Table for female employees, set back 5 years. **For healthy retirees:** Males - RP2000 Healthy Mortality Table for male annuitants, projected to 2007 using mortality improvement scale AA, set forward two years. P2000 Healthy Mortality Table for female annuitants. **For all disabled lives:** RP2000 Disabled Mortality Table for male annuitants, set forward one year.					**For actives:** Males - 1994 Uninsured Pension Mortality Table for males, base table rates multiplied by 87%. Females - 1994 Uninsured Pension Mortality Table for females, base table rates multiplied by 125%. **For healthy retirees:** Males - 1994 Uninsured Pension Mortality Table for males, set forward two years. Females - 1994 Uninsured Pension Mortality Table for females, base table rates multipled by 125% for ages less than 85 and multipled by 135% for ages 85 and up. **For all disabled lives:**				

City of Dallas, Texas
Dallas Water Utilities
(An Enterprise Fund of the City of Dallas)

REQUIRED SUPPLEMENTARY INFORMATION
Schedule of Funding Progress (Unaudited)
Other Postemployment Benefits
Year Ended September 30, 2016
(in thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c))
9/30/2016	$ -	$ 492,867	$ 492,867	- %	$ 850,011	57.98%
9/30/2015	$ -	$ 459,643	$ 459,643	- %	$ 812,400	56.58%
9/30/2014	$ -	$ 611,397	$ 611,397	- %	$ 767,664	79.64%

The actuarial information presented is determined by an actuarial valuation and is the amount that results from applying various assumptions with regard to future employment, mortality, and the healthcare cost trend.

A re-evaluation of the Medicare Supplement plans in the 9/30/2015 actuarial valuation revealed that a significant decrease in the post-Medicare net claims cost assumption was warranted. This change of assumption caused a 28% reduction in the liability.