Downriver Utility Wastewater Authority

Financial Report

December 31, 2019

Contents

Plante & Moran, PLLC
27400 Northwestern Highway
P.O. Box 307
Southfield, MI 48037-0307
Tel: 248.352.2500
Fax: 248.352.0018
plantemoran.com

Independent Auditor's Report

To the Downriver Utility Wastewater Authority Board
Downriver Utility Wastewater Authority

Report on the Financial Statements

We have audited the accompanying financial statements of Downriver Utility Wastewater Authority (the "Authority") as of and for the year ended December 31, 2019 and the related notes to the financial statements, which collectively comprise Downriver Utility Wastewater Authority'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 entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Downriver Utility Wastewater Authority as of December 31, 2019 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.

To the Downriver Utility Wastewater Authority Board
Downriver Utility Wastewater Authority

Other Matter

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

Plante & Moran, PLLC

June 4, 2020

Using This Annual Report

Downriver Utility Wastewater Authority (the "Authority") is a joint venture of 13 communities in southeastern Michigan (the cities of Allen Park, Belleville, Dearborn Heights, Ecorse, Lincoln Park, River Rouge, Riverview, Romulus, Southgate, Taylor, and Wyandotte, Michigan and the charter townships of Brownstown and Van Buren; collectively, the "Communities"). The Authority was established in 2010 in order to acquire, finance, manage, improve, and operate the Downriver Sewage Disposal Treatment Plant and related collection systems. The system is the second largest wastewater system in Michigan, serving the Communities with a service area population of 350,000. The Authority provides services exclusively to the 13 Communities.

This annual report consists of a series of financial statements. The statement of net position and the statement of activities provide information about the activities of the Authority as a whole and present a longer-term view of the Authority’s finances. This longer-term view uses the accrual basis of accounting so that it can measure the cost of providing services during the current year and whether the taxpayers have funded the full cost of providing government services. These are followed by the statement of cash flows, which presents detailed information about the changes in the Authority's cash position during the year.

Government-wide Overall Financial Analysis

As noted earlier, net position over time may serve as a useful indicator of a government’s financial position. In the case of the Authority, assets exceeded liabilities by $97,722,260 at the close of the most recent fiscal year.

The Authority's Net Position

	2018	2019	Change	Percent Change
Assets				
Current and other assets:				
Cash and investments	$ 25,836,377	$ 22,919,532	$ (2,916,845)	(11.3)
Other current assets:				
Receivables	2,265,932	3,269,875	1,003,943	44.3
Prepaid expenses and other assets	363,294	433,268	69,974	19.3
Restricted assets	17,533,108	17,378,152	(154,956)	(0.9)
Capital assets	180,631,280	177,113,981	(3,517,299)	(1.9)
Total assets	226,629,991	221,114,808	(5,515,183)	(2.4)
Liabilities				
Current liabilities	9,300,669	6,314,851	(2,985,818)	(32.1)
Noncurrent liabilities	122,888,012	117,077,697	(5,810,315)	(4.7)
Total liabilities	132,188,681	123,392,548	(8,796,133)	(6.7)
Net Position				
Net investment in capital assets	55,215,685	57,441,469	2,225,784	4.0
Restricted	16,465,691	16,357,969	(107,722)	(0.7)
Unrestricted	22,759,934	23,922,822	1,162,888	5.1
Total net position	**$ 94,441,310**	**$ 97,722,260**	**$ 3,280,950**	3.5

The increase in net position for fiscal year 2019 can be attributed to a full year of operations of the wastewater plant. The Authority assumed control of the wastewater plant during September 2018, resulting in a partial year of operations for that year. The increase in net investment in capital assets was directly attributed to the capitalization of multiyear projects during 2019. Unrestricted net position increased due to the reduction in current liabilities, which was much higher in 2018 due to vendor invoices not being received promptly in the first year of operations.

The Authority's Changes in Net Position

	2018	2019	Change	Percent Change
Operating Revenue				
Sewage disposal and excess flow charges	$ 4,315,947	$ 25,113,678	$ 20,797,731	481.9
Other charges	238,045	1,388,142	1,150,097	483.1
Total operating revenue	4,553,992	26,501,820	21,947,828	481.9
Operating Expenses				
System operations	3,147,738	11,748,758	8,601,020	273.2
System management	60,944	219,481	158,537	260.1
Engineering	883,869	234,089	(649,780)	(73.5)
Utilities	1,038,697	2,962,777	1,924,080	185.2
Sludge hauling and disposal	275,000	1,004,393	729,393	265.2
Insurance premiums	182,871	480,392	297,521	162.7
Flow metering	77,729	302,613	224,884	289.3
Professional services	379,555	249,223	(130,332)	(34.3)
Other operating expenses	95,746	585,147	489,401	511.1
Depreciation	1,123,750	4,524,061	3,400,311	302.6
Total operating expenses	7,265,899	22,310,934	15,045,035	207.1
Operating (Loss) Income	(2,711,907)	4,190,886	6,902,793	(254.5)
Nonoperating Expense	(1,345,073)	(2,867,470)	(1,522,397)	113.2
Special Items	97,989,525	1,957,534	(96,031,991)	(98.0)
Change in Net Position	93,932,545	3,280,950	(90,651,595)	(96.5)
Net Position - Beginning of year	508,765	94,441,310	93,932,545	18,462.9
Net Position - End of year	**$ 94,441,310**	**$ 97,722,260**	**$ 3,280,950**	3.5

Fiscal year 2019 results included 12 months of revenue and expenditures, compared to approximately three months in 2018. Going forward, the revenue and expenditures should reflect consistent operations over the course of a full year.

Overall, the Authority recognized a positive change in net position of $3,280,950. Revenue primarily consisted of sewage disposal charges and excess flow charges from the municipal customers (approximately 95 percent of operating revenue). Operating expenses were primarily related to operation of the plant by an outside contractor (approximately 53 percent of operating expenses), utilities (approximately 13 percent), and depreciation (approximately 20 percent).

Operating income of $4,190,886 reflect the excess of primarily sewage operating revenue over plant operating expenditures. Nonoperating expense includes $4,118,359 of interest expense, offset by $571,788 of interest income; $315,248 of refunds related to escrow deposits from Wayne County, Michigan; and $247,368 of bond premium recognized in 2019. The special item of $1,957,534 represents reductions in existing debt balances related to SRF projects and is discussed further in the following Capital Assets and Debt Administration notes.

Capital Assets and Debt Administration

Capital assets with a net book value of approximately $3.2 million were placed in to service during the current year, which includes $2.2 million in assets that were transferred from construction in progress. Depreciation expense of approximately $4.5 million was recorded in 2019.

During the current year, the Authority paid $3,595,000 in principal towards existing debt and recognized interest expense of approximately $4.1 million on outstanding debt. As explained in Note 5 to the financial statements, during the year ended December 31, 2019, the Authority recognized a reduction to existing debt balances of $1,957,534 due to SRF projects being closed out at an amount less than the original recorded amount.

Economic Factors and Next Year's Budgets and Rates

The Authority is responsible for setting the budget and rates to cover the operation of the Downriver Sewage Disposal System. The budget is based on the fiscal year period from January through December, while the rates cover the period from July through June. The budget process began in October, and the budget was adopted by the board in December. The rates were developed in March and April and were approved by the board in May. Factors that affect the budget and rates include the flows into the Downriver Sewage Disposal System, the cost of utilities and chemicals, and capital expenditures to maintain the operation of the plant. A significant expense that is affecting the Authority is sludge disposal; the Authority is working on a long-term solution involving a biosolids dryer methodology to offset the limited availability of landfills willing to accept the disposal of the sludge and the increased costs for disposal.

Requests for Further Information

This financial report is intended to provide a general overview of the Authority’s finances and demonstrate the Authority’s accountability for the money it receives. If you have questions about this report or need additional information, please contact DNS Financial Services at DNSFinancialSvcs@gmail.com. This report, authority budgets, and other financial information are available on the Authority’s website at www. http://DUWAuthority.org.

Statement of Net Position

	December 31, 2019
Assets	
Current assets:	
Cash and cash equivalents	$ 22,919,532
Receivables (Note 7)	3,269,875
Prepaid expenses and other assets	433,268
Total current assets	26,622,675
Noncurrent assets:	
Restricted cash and cash equivalents (Note 8)	17,378,152
Capital assets: (Note 4)	
Assets not subject to depreciation	2,538,803
Assets subject to depreciation - Net	174,575,178
Total noncurrent assets	194,492,133
Total assets	221,114,808
Liabilities	
Current liabilities:	
Accounts payable	1,199,851
Unearned revenue	1,500,000
Current portion of bonds payable (Note 5)	3,615,000
Total current liabilities	6,314,851
Noncurrent liabilities:	
Interest payable from restricted assets	1,020,185
Bonds payable - Net of current portion (Note 5)	116,057,512
Total noncurrent liabilities	117,077,697
Total liabilities	123,392,548
Net Position	
Net investment in capital assets	57,441,469
Restricted: (Note 8)	
Debt service	11,488,013
Rate stabilization	3,269,956
Tunnel repair and replacement	1,600,000
Unrestricted	23,922,822
Total net position	**$ 97,722,260**

Downriver Utility Wastewater Authority

Statement of Revenue, Expenses, and Changes in Net Position

	Year Ended December 31, 2019
Operating Revenue	
Sewage disposal and excess flow charges	$ 25,113,678
Other charges	1,388,142
Total operating revenue	26,501,820
Operating Expenses	
System operations	11,748,758
System management	219,481
Engineering	234,089
Utilities	2,962,777
Sludge hauling and disposal	1,004,393
Insurance premiums	480,392
Flow metering	302,613
Professional services	249,223
Other operating expenses	585,147
Depreciation	4,524,061
Total operating expenses	22,310,934
Operating Income	4,190,886
Nonoperating Revenue (Expense)	
Investment income - Net	571,788
Loss on asset disposal	(11,623)
Community refunds	(1,006)
Reimbursements	315,248
Other income	129,114
Interest and bond issuance charges	(3,870,991)
Total nonoperating expense	(2,867,470)
Special Items - Debt adjustment (Note 5)	1,957,534
Change in Net Position	3,280,950
Net Position - Beginning of year	94,441,310
Net Position - End of year	**$ 97,722,260**

See notes to financial statements.

Statement of Cash Flows

	Year Ended December 31, 2019
Cash Flows from Operating Activities	
Receipts from member communities for monthly charges	$ 24,276,224
Payments to vendors	(20,308,548)
Other receipts	667,536
Net cash and cash equivalents provided by operating activities	4,635,212
Cash Flows Provided by Noncapital Financing Activities - Community assessments and county reimbursement	314,242
Cash Flows from Capital and Related Financing Activities	
Issuance of bonds to purchase system	56,819
Purchase of capital assets	(889,271)
Principal and interest paid on capital debt	(7,760,591)
Net cash and cash equivalents used in capital and related financing activities	(8,593,043)
Cash Flows Provided by Investing Activities - Interest on investments	571,788
Net Decrease in Cash and Cash Equivalents	(3,071,801)
Cash and Cash Equivalents - Beginning of year	43,369,485
Cash and Cash Equivalents - End of year	**$ 40,297,684**
Classification of Cash and Cash Equivalents	
Cash and investments	$ 22,919,532
Restricted cash	17,378,152
Total cash and cash equivalents	**$ 40,297,684**
Reconciliation of Operating Income to Net Cash from Operating Activities	
Operating income	$ 4,190,886
Adjustments to reconcile operating income to net cash from operating activities:	
Depreciation and amortization	4,524,061
Changes in assets and liabilities:	
Receivables	(1,531,010)
Prepaid and other assets	(69,974)
Accounts payable	(2,478,751)
Total adjustments	444,326
Net cash and cash equivalents provided by operating activities	**$ 4,635,212**
Significant Noncash Transactions - Reductions to state revolving fund loans assumed as part of system transfer	$ 1,957,534

See notes to financial statements.

Note 1 - Nature of the Authority

Downriver Utility Wastewater Authority (the "Authority" or DUWA) is a joint venture of 13 communities in southeastern Michigan (the cities of Allen Park, Belleville, Dearborn Heights, Ecorse, Lincoln Park, River Rouge, Riverview, Romulus, Southgate, Taylor, and Wyandotte, Michigan and the charter townships of Brownstown and Van Buren; collectively, the "Communities"). The Authority was established in 2010 in order to acquire, finance, manage, improve, and operate the Downriver Sewage Disposal Treatment Plant and related collection systems. The system is the second largest wastewater system in Michigan, serving the Communities with a service area population of 350,000. The Authority provides services exclusively to the 13 Communities.

On September 27, 2018, the treatment plant and collection systems were transferred from Wayne County, Michigan (the "County") to the Authority at a purchase price of $57.5 million, of which $54 million was paid at closing to the County and the remaining $3.5 million will be paid five years from closing. In the fall of 2018, the Authority engaged a private operator to operate the system under an operations agreement for a period of 20 years.

Note 2 - Significant Accounting Policies

Accounting and Reporting Principles

The Authority follows accounting principles generally accepted in the United States of America (GAAP) applicable to governmental units. Accounting and financial reporting pronouncements are promulgated by the Governmental Accounting Standards Board (GASB). The Authority accounts for its various activities in one proprietary fund, as it provides services to users in exchange for charges of fees. The following is a summary of the significant accounting policies used by the Authority:

Basis of Accounting

The Authority uses the economic resources measurement focus and full accrual basis of accounting. Revenue is recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

Reporting Entity

The Authority is a public body corporate established in accordance with Michigan Public Act 233 of 1955, as amended. In addition to this statutory authority, the governance for the Authority is found in its Articles of Incorporation, by-laws, policies, and ordinances. The Authority's governing body is composed of 13 representative members, consisting of either mayors or supervisors (or their alternates) of each of the communities. In accordance with government accounting principles, there are no component units appropriate to be reported within these financial statements.

Specific Balances and Transactions

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, demand deposits, and short-term investments with a maturity of three months or less when acquired. In addition, the statement of cash flows includes both restricted and unrestricted cash and cash equivalents.

Inventories and Prepaid Items

Inventories are valued at cost, on a first-in, first-out basis. Certain payments to vendors reflect costs applicable to future fiscal years and are recorded as prepaid items in both government-wide and fund financial statements, when applicable.

Note 2 - Significant Accounting Policies (Continued)

Restricted Assets

The revenue bonds of the Authority require amounts to be set aside for debt service principal and interest on all debt, operations and maintenance, and a bond reserve. The bonds also require establishment of a rate stabilization fund. These amounts have been classified as restricted assets. Unspent bond proceeds, if any, are required to be set aside for construction. In addition, by agreement with the tunnel communities, a minimum of $1,500,000 is restricted for tunnel repair and replacement. These amounts have also been classified as restricted assets.

Capital Assets

Capital assets include the treatment plant, interceptors, storage tunnel, equipment, and vehicles. Capital assets are defined by the Authority as assets with an initial individual cost of more than $5,000 and an estimated useful life in excess of one year. Capital assets are recorded at historical cost if purchased or constructed or, if donated, at their acquisition value on the date donated.

Interest incurred during the construction of capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

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

	Depreciable Life - Years
Buildings and improvements	40
Machinery and equipment	7
Land improvements	20
Office equipment	7
Sewer system	40
Vehicles	5

Long-term Obligations

Long-term debt and other long-term obligations are reported as liabilities. Bond premiums and discounts are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are expensed at the time they are incurred.

Net Position

Net position of the Authority is classified in three components. Net investment in capital assets consists of capital assets net of accumulated depreciation and is reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. The restricted component of net position consists of restricted assets reduced by liabilities related to those assets. Unrestricted net position is the remaining net position that does not meet the definition of invested in capital or restricted.

Net Position Flow Assumption

The Authority will sometimes fund outlays for a particular purpose from both restricted and unrestricted resources. In order to calculate the amounts to report as restricted net position and unrestricted net position in the government-wide and proprietary fund financial statements (as applicable), a flow assumption must be made about the order in which the resources are considered to be applied. It is the Authority's policy to consider restricted net position to have been depleted before unrestricted net position is applied.

Note 2 - Significant Accounting Policies (Continued)

Proprietary Funds Operating Classification

Proprietary funds distinguish operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Operating revenue represents billings to member communities based on the Authority's operating expenses, exclusive of depreciation and inclusive of capital outlay not financed by debt. Communities are responsible for passing along and collecting the charges to their individual system customers. Operating revenue also includes industrial pretreatment charges and surveillance fees charged directly to commercial users. Operating expenses include the cost of sales or services, administrative expenses, and may include depreciation on capital assets. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses.

System Operations and Management

The Authority has entered into an agreement with a contract operator for a term of 20 years commencing on October 1, 2018 to operate the system. The current agreement expires on September 30, 2038. Under the terms of the operations agreement, the operator provides all the required labor, materials, and supervision necessary for the operation of the sewage treatment plant and related collection systems, with the exception of certain costs paid directly by the Authority, such as electricity, legal, accounting, engineering, capital outlay, insurance, and overall system management. The Authority pays the operator a monthly fee. In addition, the Authority has entered into a contract with an engineering firm to provide system management services. The contract is for three years and is based on hourly rates.

Adoption of New Accounting Pronouncements

As of January 1, 2019, the Authority adopted GASB Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*. This statement establishes criteria to improve the information that is disclosed in the notes to the government financial statements related to debt, including direct borrowings and direct placements. It also clarifies which liabilities governments should include when disclosing information related to debt. See Note 5 for related disclosures.

Upcoming Accounting Pronouncement

In January 2017, the Governmental Accounting Standards Board issued Statement No. 84, *Fiduciary Activities*. This statement establishes criteria for identifying fiduciary activities of all state and local governments. An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements. The Authority is currently evaluating the impact this standard will have on the financial statements when adopted. The provisions of this statement are effective for the Authority's financial statements for the year ending December 31, 2020.

In June 2017, the GASB issued Statement No. 87, *Leases*, which improves accounting and financial reporting for leases by governments. This statement requires recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources. The Authority is currently evaluating the impact this standard will have on the financial statements when adopted. The provisions of this statement are effective for the Authority's financial statements for the year ending December 31, 2021.

Note 2 - Significant Accounting Policies (Continued)

In June 2018, the GASB issued Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period,* which simplifies accounting for interest cost incurred before the end of construction and requires those costs to be expensed in the period incurred. As a result, interest cost incurred before the end of a construction period will not be capitalized and included in the historical cost of a capital asset reported in a business-type activity or enterprise fund. This statement also reiterates that, in financial statements prepared using the current financial resources measurement focus, interest cost incurred before the end of a construction period should be recognized as an expenditure on a basis consistent with governmental fund accounting principles. The requirements of the standard will be applied prospectively and result in increased interest expense during periods of construction. The provisions of this statement are effective for the Authority's financial statements for the December 31, 2020 fiscal year.

In May 2019, the GASB issued Statement No. 91, *Conduit Debt Obligations*, which clarifies the existing definition of conduit debt, provides a single method of reporting conduit debt obligations by issuers, and eliminates diversity in practice associated with commitments extended by issuers, arrangements associated with conduit debt obligations, and related note disclosures. As a result, issuers should not recognize a liability for items meeting the definition of conduit debt; however, a liability should be recorded for additional or voluntary commitments to support debt service if certain recognition criteria are met. The standard also addresses the treatment of arrangements where capital assets are constructed or acquired with the proceeds of a conduit debt obligation and used by a third-party obligor. The requirements of the standard will be applied retrospectively and are effective for the Authority's financial statements for the December 31, 2021 fiscal year.

In March 2020, the GASB issued Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Arrangements*, which improves accounting and financial reporting for arrangements where a governmental entity contracts with an operator to provide public services by conveying control of the right to operate or use nonfinancial assets, such as infrastructure or other capital assets, for a period of time in an exchange or exchange-like transaction. It establishes the definitions of public-private and public-public partnerships (PPPs) and availability payment arrangements (APAs) and provides uniform guidance on accounting and financial reporting for transactions that meet those definitions. It requires governments to report assets and liabilities related to PPPs consistently and disclose important information about PPP transactions. The Authority is currently evaluating the impact this standard will have on the financial statements when adopted. The provisions of this statement are effective for the Authority's financial statements for the year ending December 31, 2023.

In May 2020, the GASB issued Statement No. 95, *Postponement of the Effective Date of Certain Authoritative Guidance*, which provides temporary relief to governments and other stakeholders in light of the COVID-19 pandemic. That objective is accomplished by postponing the effective dates of certain provisions in statements and implementation guides that first became effective or are scheduled to become effective for periods beginning after June 15, 2018 and later. The effective dates of certain provisions contained in the following pronouncements that the Authority has not yet adopted are postponed by one year: Statement No. 91, *Conduit Debt Obligations*; Statement No. 92, *Omnibus 2020*; Statement No. 93, *Replacement of Interbank Offered Rates*; Implementation Guide No. 2017-3, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions (and Certain Issues Related to OPEB Plan Reporting);* Implementation Guide No. 2018-1, *Implementation Guidance Update-2018*; Implementation Guide No. 2019-1, *Implementation Guidance* Update-2019; and Implementation Guide No. 2019-2, *Fiduciary Activities*. The effective dates of the following pronouncements are postponed by 18 months: Statement No. 87, *Leases*, and Implementation Guide No. 2019-3, *Leases*.

Note 3 - Deposits and Investments

Michigan Compiled Laws Section 129.91 (Public Act 20 of 1943, as amended) authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The law also allows investments outside the state of Michigan when fully insured. The local unit is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States; repurchase agreements; bankers' acceptances of United States banks; commercial paper rated within the two highest classifications that matures not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions that are rated as investment grade; and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan.

The Authority's cash and investments are subject to several types of risk, which are examined in more detail below:

Custodial Credit Risk of Bank Deposits

Custodial credit risk is the risk that, in the event of a bank failure, the Authority's deposits may not be returned to it. At year end, the Authority had $10,452,423 of bank deposits (checking accounts) that were uninsured and uncollateralized.

Custodial Credit Risk of Investments

Custodial credit risk is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party.

Interest Rate Risk

Interest rate risk is the risk that the value of investments will decrease as a result of a rise in interest rates. The Authority's investment policy minimizes interest rate risk by structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to maturity. The Authority also minimizes the risk by investing operating funds primarily in shorter-term securities, money market mutual funds, or similar investment pools and limiting the average maturity of the portfolio in accordance with this policy.

At year end, the Authority held money market funds with a fair value of $29,643,943 with a weighted-average maturity of 32 days.

Credit Risk

State law limits investments in commercial paper to the top two ratings issued by nationally recognized statistical rating organizations. The Authority's investment policy states that the Authority will minimize credit risk by limiting the investments to the types of securities listed in Section VI of the investment policy, prequalifying the financial institutions broker/dealers, intermediaries, and advisers with which the Authority will do business, and diversifying the investment portfolio so that the impact of the potential losses from any one type of security or from any one individual issuer will be minimized.

At year end, the Authority held $29,643,943 in money market funds with a rating of AAAm issued by S&P.

Concentration of Credit Risk

The Authority's investment policy minimizes concentration of credit risk by diversifying the investment portfolio so that the impact of potential losses from any one type of security or from any one individual issuer will be minimized. At year end, the Authority held $29,643,943 in money market funds, which consisted primarily of U.S. government agency debt and U.S. Treasury repurchase agreements.

Note 3 - Deposits and Investments (Continued)

Fair Value Measurements

The Authority 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 the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. Investments that are measured at fair value using net asset value per share (or its equivalent) as a practical expedient are not classified in the fair value hierarchy below.

In instances whereby inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Authority's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

The Authority has the following recurring fair value measurements as of December 31, 2019:

- Money market funds of $29,643,943 are valued using a matrix pricing model (Level 2 inputs).

Note 4 - Capital Assets

Capital asset activity of the Authority was as follows:

	Balance January 1, 2019	Reclassifications	Additions	Disposals and Adjustments	Balance December 31, 2019	Depreciable Life - Years
Capital assets not being depreciated:						
Land	$ 2,426,717	$ -	$ -	$ -	$ 2,426,717	
Construction in progress	1,473,799	(2,177,644)	815,931	-	112,086	
Subtotal	3,900,516	(2,177,644)	815,931	-	2,538,803	
Capital assets being depreciated:						
Sewer system	176,080,310	2,177,644	202,456	(11,624)	178,448,786	40
Buildings and improvements	964,081	-	-	-	964,081	40
Machinery and equipment	144,090	-	-	-	144,090	7
Vehicles	79,133	-	-	-	79,133	5
Office equipment	33,775	-	-	-	33,775	7
Land improvements	553,125	-	-	-	553,125	20
Subtotal	177,854,514	2,177,644	202,456	(11,624)	180,222,990	
Accumulated depreciation:						
Sewer system	1,100,502	-	4,431,067	-	5,531,569	
Buildings and improvements	6,026	-	24,102	-	30,128	
Machinery and equipment	5,146	-	20,584	-	25,730	
Vehicles	3,957	-	15,827	-	19,784	
Office equipment	1,206	-	4,825	-	6,031	
Land improvements	6,914	-	27,656	-	34,570	
Subtotal	1,123,751	-	4,524,061	-	5,647,812	
Net capital assets being depreciated	176,730,763	2,177,644	(4,321,605)	(11,624)	174,575,178	
Net business-type activities capital assets	$ 180,631,279	$ -	$ (3,505,674)	$ (11,624)	$ 177,113,981	

Note 5 - Long-term Debt

Long-term debt activity for the year ended December 31, 2019 can be summarized as follows:

	Interest Rate Ranges	Principal Maturity Ranges	Beginning Balance	Additions	Reductions	Special Item*	Ending Balance	Due within One Year
Direct borrowings - Revenue bonds:								
SRF Junior Lien Bonds - Due 2037	1.625-2.5%	$1,110,000 - $4,230,000	$ 60,692,135	$ 56,819	$ (3,595,000)	$ (1,957,534)	$ 55,196,420	$ 3,615,000
Wayne County Junior Lien Bond - Due 2023	0%	$0-$3,500,000	3,500,000	-	-	-	3,500,000	-
Total direct borrowings			64,192,135	56,819	3,595,000	1,957,534	58,696,420	3,615,000
Other borrowings - Revenue bonds:								
Series 2018 Senior Lien Bonds - Due 2043	5%	$1,190,000 - $4,015,000	55,225,000	-	-	-	55,225,000	-
Unamortized bond discounts			5,998,460	-	(247,368)	-	5,751,092	-
Total long-term debt			$ 125,415,595	$ 56,819	$ (3,842,368)	$ (1,957,534)	$ 119,672,512	$ 3,615,000

***Special Item** - As disclosed in Note 1, on September 27, 2018, the Authority consummated a years-long initiative to transfer the Downriver Sewage Disposal System from the County to the Authority. As part of the transfer, the Authority assumed the outstanding liabilities of the system, including the State Revolving Fund (SRF) Junior Lien Bonds. During the year ended December 31, 2019, the SRF Bonds balance was adjusted after two SRF projects were closed out for an amount that was less than the original recorded amount. An adjustment to reduce the debt balance by $1,957,534 was recorded to adjust the balances to their actual amount as of December 31, 2019.

Revenue Bonds

Revenue bonds involve a pledge of specific income derived from the acquired or constructed assets and to pay debt service. The Authority has pledged substantially all of the revenue of the system, net of operating expenses, to repay the sewer revenue bonds listed below.

Debt Service Requirements to Maturity

Annual debt service requirements to maturity for the above bonds and note obligations are as follows:

	Direct Borrowings		Other Borrowings		
Years Ending December 31	Principal	Interest	Principal	Interest	Total
2020	$ 3,615,000	$ 1,287,746	$ -	$ 2,761,250	$ 7,663,996
2021	3,705,000	1,223,156	1,190,000	2,731,500	8,849,656
2022	3,790,000	1,134,430	1,250,000	2,670,500	8,844,930
2023	7,385,000	1,043,537	1,310,000	2,606,500	12,345,037
2024	3,990,000	950,310	1,375,000	2,539,375	8,854,685
2025-2029	20,524,086	3,285,760	8,675,000	11,513,375	43,998,221
2030-2034	12,678,049	1,131,719	11,605,000	8,963,875	34,378,643
2035-2039	3,009,285	129,679	14,905,000	5,666,125	23,710,089
2040-2044	-	-	14,915,000	1,538,125	16,453,125
Total	$ 58,696,420	$ 10,186,337	$ 55,225,000	$ 40,990,625	$ 165,098,382

Note 6 - Risk Management

The Authority is exposed to various risks of loss related to property loss, torts, and errors and omissions. The Authority has purchased commercial insurance for all claims. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past fiscal years. The plans, coverage limits, retentions, and deductibles are as follows:

- General liability, hired and nonowned auto liability, public officials liability - Limits of $5,000,000 and $10,000,000; retention amount of $250,000
- Pollution liability - Limit of $5,000,000; retention amount of $25,000
- Property liability - Flood limits of $10,000,000 and $50,000,000; Quake limit of $50,000,000, All risk limit of $321,810,443; deductible of $250,000

Note 7 - Receivables

Receivables as of December 31, 2019 are as follows:

Community operating charges	$ 2,866,617
Industrial pretreatment charges	270,496
Due from Wayne County, Michigan	159,812
Estimated uncollectible accounts receivable	(27,050)
Net receivables	$ 3,269,875

Note 8 - Restricted Assets

The Authority's Master Bond Ordinance has established certain accounts to be held in trust by the trustee. All revenue of the system shall be deposited with the trustee. As of the first day of each month, amounts held in the Receiving Fund shall be transferred as follows:

First - One-twelfth of the budgeted operation and maintenance expenses are to be transferred to the operations and maintenance account.

Second - One-sixth of the next Senior Lien debt service payment is to be transferred to the Senior Lien Debt Service Account.

Third - Any shortfall in the required Senior Lien Bond Reserve Account shall be transferred to the Senior Lien Bond Reserve Account.

Fourth - One-sixth of the next Junior Lien debt service payment is to be transferred to the Bond and Interest Redemption Fund, and any shortfall in the required Junior Lien Reserve Account shall be transferred to the Junior Lien Bond Reserve Account.

Fifth - Any shortfall in the Rate Stabilization Fund shall be transferred to the Rate Stabilization Fund.

After the reserves are funded as noted above, the Authority may set funds aside for extraordinary repair and replacement or for improvement and extension. These reserves are discretionary. Any remaining funds will be retained in the Receiving Fund unless the Authority directs that they be transferred to the Surplus Fund. The Surplus Fund and the remaining untransferred balance in the Receiving Fund are deemed to consist of all funds not otherwise restricted for debt service, debt reserves, or rate stabilization.

In addition, the Authority is required to set aside funds for repair and replacement of the wet weather storage tunnel at a minimum amount of $1,500,000 per contractual agreement. The balance of $1,600,000 includes accumulated interest.

Note 8 - Restricted Assets (Continued)

At December 31, 2019, restricted assets are composed of the following:

Senior Lien Debt Service	$ 864,873
Senior Lien Bond Reserve	4,144,496
Junior Lien Bond and Interest Redemption	2,695,920
Junior Lien Bond Reserve	4,802,907
Rate Stabilization Fund	3,269,956
Tunnel Reserve	1,600,000
Total	$ 17,378,152

Note 9 - Related Party Transactions

The Authority receives utility services from the Wyandotte Department of Municipal Services (WDMS), which is a department created by the City of Wyandotte, Michigan, a member of the Communities. WDMS is operated and governed independently from the City of Wyandotte, Michigan by a separate commission. The Authority incurred utility expenses provided by WDMS of approximately $3,034,000 during the year.

Note 10 - Subsequent Events

During DUWA's first year of ownership of the system, several deferred maintenance and critical long-term needs were identified that require investment to continue the reliability of the system and enhance DUWA's environmental impact. Additionally, the system has incurred a substantial increase in biosolids disposal costs due to landfill restrictions. This provides an opportunity for conversion to a Class A biosolids product with the potential for beneficial reuse options. As a result, DUWA submitted an application for financing under the WIFIA (Water Infrastructure Finance and Innovation Act) program in March 2020. If the WIFIA borrowing is approved by the U.S. Environmental Protection Agency, the proceeds will be used towards the related major capital projects and equipment replacements. The total project costs are estimated at $30.7 million. The debt would be a Senior Lien for approximately $15.0 million payable over 37 years. As part of the borrowing, DUWA will be providing matching funds of approximately 51 percent, or approximately $15.7 million from available reserves.